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**REPORT 4**  
*(1215/11/IM)*

## **GOVERNMENT PROPOSAL ON WEATHERTIGHT HOMES**

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### **1 Purpose of report**

This report follows on from report 3 (1215/11/IM) and the resolutions made by Council on 26 May 2010. The purpose of this report is to seek Council agreement to opt into the Financial Assistance Package (FAP) by signing a binding heads of agreement with the Crown.

### **2 Recommendation**

It is recommended that Council:

1. *Receive the information.*
2. *Agree that Wellington City Council opt-in to the Financial Assistance Package subject to:*
  - (a) *Third party legislation protection being introduced and passed to the satisfaction of the Chief Executive; or if legislation is not passed, an alternative agreement being reached that indemnifies Council for all liability and associated costs (to the satisfaction of the Chief Executive);*
  - (b) *Eligibility criteria not being extended beyond the current class of eligible claimant including through the evolution of case law;*
  - (c) *Eligibility issues around the class of commercial operators who are not accessing High Court or the WHRS service, being resolved;*
  - (d) *Insurance issues around existing weathertightness claims opting into Financial Assistance Package, being resolved;*
  - (e) *In all other respects the key features of scheme design for the Financial Assistance Package attached as an appendix to this report are not materially changed;*
  - (f) *A side agreement being agreed between the Crown and the Council that neither will apply to the FAP for their own housing stock.*

3. *Agree to delegate the Chief Executive negotiate and execute both the heads of agreement with the Crown and the key operational features of scheme design for the Financial Assistance Package;*
4. *Agree not to apply for assistance to repair any Council owned leaky homes under the Financial Assistance Package;*
5. *Note that the funding of Leaky Homes liability (under the status quo and under the Financial Assistance Package) will be considered further by Council as part of the 2011/12 Annual Plan and the 2012/22 LTCCP.*

### **3. Executive Summary**

The prime focus of the Government's FAP proposal to Council is to maximise the number of leaky homes getting fixed at an affordable price. The FAP scheme aims to achieve this through a combination of assured contributions from local and central government, and by using the money that homeowners would otherwise spend on legal and expert costs on repairs to their homes.

At the Council meeting of Wednesday 26 May 2010, the Council agreed unanimously to support and assist in the development of the proposed FAP. Council also delegated the Chief Executive to work with government officials and the local government sector to agree the details of the FAP for reporting to Council for final approval.

The scheme is substantially the same as that advised to Council in May; that is, Government and local authorities will each contribute 25% of repair costs towards the repair of leaky homes. The balance of 50% would be contributed by the homeowner. Central Government will also cover the costs to administer the proposed process.

Since May, joint (Government and Councils) work on the FAP scheme has centred on clarifying eligibility criteria, scheme administration and liability minimisation.

Councils have also clarified the decision-making and consultation requirements and the result of this work is significantly covered in this paper. At the time of writing this report there are a number of matters which are still to be resolved before a final draft of the heads of agreement with the Crown is completed. The matters still outstanding include:

- Introduction and passing legislation protection or an alternative agreement being reached that indemnifies Council for all liability and associated costs of third party claims;
- Eligibility issues around the class of commercial operators who are not accessing High Court or the WHRS service, being resolved;
- Insurance issues around existing weathertightness claims opting into Financial Assistance Package, being resolved.

Analysis of the FAP, including peer review by the Council's actuary (Melville Jessop Weaver) shows the FAP proposal strikes a better balance between financial exposure and financial certainty, and is likely to achieve better social outcomes by getting more leaky homes fixed and fixed faster.

Officers consider the Council will be better served by accepting the proposal than continuing with the existing litigation-only route. Further, by opting into the FAP, Wellington homeowners with leaky homes will be able to take advantage of the FAP and have a choice other than the current litigation option.

With this point in mind, the Council currently has three options in dealing with the leaky building issue:

1. Agree to opt into the FAP as proposed by the Government;
2. Agree to opt into the FAP, subject to the resolution of outstanding matters;  
or
3. Opt out of the FAP and continue only with existing litigation based approach.

Officers **recommend option 2**, with the Chief Executive being delegated authority to execute the heads of agreement,

#### **4. Background**

A number of New Zealand buildings suffer from weathertightness issues (so called "leaky buildings"). The Courts have ruled that territorial authorities (councils) are legally liable to contribute to the costs of repair of residential dwellings that have been damaged through a lack of weathertightness. Wellington City Council, and many others through New Zealand, face such claims.

The Government, through the Department of Building and Housing (DBH), has developed a financial assistance package for the owners of such dwellings. In essence this package involves the Government and the councils funding 25% each of the cost of repairing the leaky home, with the owners being responsible for the other 50%. The intention is to make available to such owners an option whereby they can receive guaranteed money quickly, and to get on with fixing the leaky building.

On Wednesday 26 May 2010 the Council agreed unanimously to support and assist in the development of the proposed FAP which was tabled by the Government on 17 May 2010. Council also delegated the Chief Executive to work with Government officials and the local government sector to agree the details of the FAP for reporting to Council for final approval. Since this time the Chief Executive has been working with Government officials to assist in preparing the final FAP. This assistance has been via the FAP Steering group; FAPTA Steering group and DBH/TA Working Group with WCC represented by Garry Poole, Greg Orchard and Stephen Cody respectively.

On Tuesday 7 September 2010, the Minister of Building and Housing, the Hon. Maurice Williamson, wrote to the Mayor, setting out the final government proposal and requesting Wellington City Council to participate in the FAP. The proposed package as outlined by the Government is attached as Appendix One.

The Minister has asked for Council's response (and the response from the other most affected Councils) before the end of the triennium in order to facilitate timely implementation of the FAP and to provide certainty to homeowners.

## **5. Decision making**

The matter for decision is how Council responds to its potential liability arising from involvement in the construction of residential dwellings that are not weathertight. In particular, Council needs to decide whether to "sign up" to the proposed FAP by 8 October 2010. The alternative is to retain the status quo (i.e. the current litigation process).

The decision of how to fund the cost of leaky homes (whether under the FAP or under the status quo litigation route) will be made when the Council makes the necessary funding decisions under s101 (3) of the Local Government Act 2002 when it considers the 2011/12 Annual Plan and the 2012/22 Long Term Council Community Plan.

The decision for Council does not involve a broader consideration of weathertightness issues. Council has an existing liability and has limited ability to change the status quo (ie the litigation only option) without the support and involvement of central government. The choice, therefore, is a narrow one, between opting out of the FAP and continuing with the litigation only approach, or opting into the FAP. The FAP is the preferred policy option of the present government and Council cannot control the process by, or timeframes within, which that policy is being developed.

Legal advice has been obtained that has confirmed that there is no requirement to consult on the decision to opt into the FAP or retain the status quo. Further it is considered that the decision is not a significant decision (ie one with a high degree of significance) although it is considered for the reasons set out in the decision making template to this report that the decision has a moderate degree of significance.

Council must nevertheless give consideration to the views and preferences of persons likely to be affected by, or to have an interest in, the matter for decision, and identify and assess the reasonable practicable options.

### **5.1 Community views**

While no specific consultation is required and has not been undertaken in this case, the Council has sufficient knowledge of community views to be able to give them consideration in the course of this decision making process. In particular, problems with the weathertightness of newer residential dwellings are well known. It is considered that there is a good level of public awareness (and

awareness within Council) about weathertightness issues, including the role territorial authorities play in subsequent litigation.

The range of views held by different sectors of the community have been publicised in various media over the years. The FAP in particular has already been the subject of four articles published in the Dominion Post. It is known that community views already expressed regarding the FAP are varied depending on perspective and/or degree of knowledge of the issue. They include:

- the FAP will provide a better outcome than litigation, albeit that the stakeholders such as HOBANZ see the proposed 50% contribution by the Crown and territorial authorities is seen as being too low.
- despite its cost and delay, litigation will ultimately provide a better outcome than the proposed FAP.
- Weathertightness issues are in large part the fault of territorial authorities, and therefore a material portion of the costs should be borne by them.
- Weathertightness issues are more the fault of other parties, such as building product manufacturers, architects or builders so why should territorial authorities (and indirectly ratepayers) pay more than their 'fair share' simply because other parties cannot be held liable, no longer exist or are insolvent.
- Weathertightness liability is something territorial authorities need to manage, and it cannot simply be avoided given the way that weathertightness litigation 'works' (ie that territorial authorities often end up contributing more to settlement or judgment than their proportionate liability).
- the Council should not opt into the FAP because of its impact on rates (a view that is held if the costs are looked at without comparing the FAP costs with the baseline cost of Council continuing to respond to weathertightness litigation on a case by case basis).

Councillors will also have their own knowledge about community views from contact with ratepayers and residents, and this should also be considered in the course of this decision making process.

## ***5.2 Identify reasonably practicable options***

Council's options are to either opt into or reject the FAP. The key scheme design of the FAP and those issues which Council and other territorial authorities wish to see resolved are known. A 'third' option is therefore to delegate authority to execute the heads of agreement, subject to the resolution of outstanding matters to the satisfaction of the Chief Executive. It is this third option that is recommended by officers.

## **6. Discussion**

### **6.1 Process**

The process for owners of both single dwellings and multi-unit properties accessing the leaky home financial assistance package (FAP) is the same as for homeowners accessing the Weathertight Homes Tribunal for litigation purposes. A step by step guide will be published for affected parties at the commencement of the scheme. To ensure repair quality, and to limit overstatement and escalation of costs and claims for betterment, the DBH and Councils will be jointly responsible for reviewing and accepting the owner's "Repair and payment plan".

One of the significant benefits of the FAP is that there will be an agreed remediation guide. This will provide more certainty to homeowners and it is also expected that the guide will mitigate the risk in designing and undertaking the repair scope and lead to more sensible repairs and repair bills.

Council contribution will be made on a progress-payment basis as critical milestones throughout the repair are achieved.

Regular inspections will be undertaken to ensure that the fix is being correctly implemented; these are separate to the mandatory building inspections carried out as part of the building consent process. It is proposed that councils will employ contact administrators to make assessments and monitor the quality of repair work.

### **6.2 Eligibility**

Eligibility of those homeowners who can opt in to the FAP is a key issue for Councils and much of the debate in developing the FAP has been centred on ensuring the class of possible claimants for whom councils are liable remains only those who are eligible to claim today.

Both Government and Councils are in agreement that private certifier claims are eligible but only for the Government's 25% contribution. This reflects current case law and the principles of the Building Act which never suggested that a Council should provide a further backstop to an insurer for default by a private certifier which was carrying out the inspections and assessment of the building when the Council had no role in this process. As this is a package to encourage homeowners to get on and repair their houses, those who have already repaired will not be eligible to access the FAP. The government has agreed to exclude HCNZ owned houses on the basis that Council-owned houses also do not access the FAP. The officer recommendations seek approval to make this commitment to the Crown on behalf of the Council.

There is an outstanding issue in relation to commercial buildings with a residential component. Currently the Council is not subject to claims from the owners/developers of such buildings, so the officer recommendations make provision for this issue to be negotiated by the Chief Executive.

### **6.3 Third Party Legislation**

The FAP is an optional path for homeowners to choose to get their leaky homes repaired. They can still, if they wish, sue other building parties such as developers, builders etc (other than the government or relevant council) in either the Weathertight Homes Tribunal or District/High Court. Councils can be linked back into a claim by a third party (builder, architect, product supplier etc) who argues that they are entitled to a contribution from the Council towards any compensation they pay to the homeowner

A key issue for Councils has been that having signed up to contribution to fixing homes under the FAP on a 'no fault' basis, that they are adequately shielded from further liability in relation to a claim that has been settled under the FAP (i.e. where otherwise third parties i.e. builders and developers etc could cross claim against the council or file a notice to join them as a third party to the litigation).

Councils have strongly advocated for legislation to "cap" their contribution to 25% of the repair costs where a building is repaired under the FAP. Introducing legislation is considered the most simple of a range of options and the most significant benefit is that council will have certainty about the extent of the cost of their liability to owners of leaky homes who opt- in to the FAP.

Minister Williamson has advised that the Government has committed to introduce legislation to remove this risk, although he has noted that it cannot guarantee that legislation will be passed, or passed in the same form it is introduced. Therefore, the Minister has suggested that should the Council agree to participate in the FAP, it do so conditional on territorial authorities' liability being "capped", whether by legislation or by an alternative method. The officer recommendations provide for this approach.

### **6.4 Review**

It is expected the government and council review the FAP six months after commencement to ensure it is working as anticipated. The terms of the review and Council participation will be clearly specified in the contractual arrangements supporting the FAP.

### **6.5 Insurance**

Discussions with DBH on the impact of the scheme design on Council's insurance arrangements are continuing, and appropriate arrangements are sought to resolve this issue to the Chief Executive's satisfaction.

### **6.6 Development of mitigation strategies**

It is acknowledged that mitigation strategies which will limit ongoing and future damage to at risk homes is crucial to ensuring homeowners take greater ongoing responsibility for maintaining their homes. Although this issue is important in the medium - long term, the completion of the planning for this issue is not critical to the decision of Council whether or not it should opt in to the FAP.

## **6.7 Sector capacity**

The Department of Building and Housing continue to work with the sector to address this issue. The availability or otherwise of the sector does not affect the viability of the FAP itself and will tend to affect more the timeframe for which repairs are carried out. Therefore, this factor should not be a determinant of whether Council should opt-in to the FAP or not.

## **6.8 Previous issues**

When Council considered the original proposal on 26 May 2010, a number of issues were highlighted where further detail was required, including:

- a. how the cost of repairs will be independently assessed to ensure quality and to limit betterment and escalation of costs and claims for betterment;
- b. confirmation on how the assessment and monitoring of repair work will be independently monitored to limit the risk of over remediation;
- c. the development of mitigation strategies to limit ongoing and future damage to at risk homes;
- d. impacts of capacity of the sector and the sector's capability to effectively manage and carry out the work; and
- e. the impact on insurance arrangements for claims already made in years where insurance cover is in place, but the homeowner elects to opt into the package

These matters along with other key issues are discussed in detail in sections 6.1 to 6.7 above. The financial impacts of the FAP are set out in section 7.

# **7. Financial implications**

## **7.1 Financial Model**

Following the report to the Council in May this year, Officers have developed a financial model to determine the likely cost to Council. The model is based on comprehensive analysis of consents issued during the at risk period (2000 to 2006).

The model assumptions are sensitive to changes in key assumptions around the number of houses affected, take-up rates, cost of repairs and claim route opted by the claimant. The model has been reviewed by our actuary (Melville Jessop Weaver) and while a few suggestions were made to fine-tune the assumptions, these have since been incorporated to be reflected in the costings below.

## **7.2 Estimated Costs**

Council has an increasing exposure to weathertightness claims due to insurance no longer being available for claims lodged after 31 August 2009, the likely increasing proportion of Council contribution and the increasing cost of repairs



and level of damage to the properties, due to the time lag of water ingress. Based on joint and several liability, where the Council is often the “last party standing”, Council’s liabilities have been steadily increasing from a historic rate of 30% of the final amount settled in a mediation. Some adjudication decisions have recently seen the Council being found joint and severally liable for more than 90% of the amount claimed. These costs continue to rise each year with a significant number of affected dwellings still yet to make a claim.

Indicative but best estimates of the expected cost to Council of weathertightness claims over the duration of the FAP are approximately \$70 million. This is based on 8,400 dwellings identified from the high risk period resulting in a projected litigation or FAP claims for 1,260 dwellings.

As a comparison, if only litigation was available (because the Council did not opt in to the FAP) officers have estimated the cost to Council for the same number of dwellings getting fixed, would be approximately \$95 million.

In this latter scenario, if Council rejects the FAP, the Crown will still provide the home owner with its 25% contribution, leaving the homeowner to pursue Council and other third parties. The publicity around the FAP scheme and the receiving the 25% from the Crown may increasingly incentivise homeowners to pursue a claim that they may not otherwise have taken. For this reason, officers consider that the numbers under the litigation only route would be higher than what Council has seen occur to date.

Using the best estimate cost to Council, the total cost to Council is estimated at \$88 million; \$70 million from new claims (per above) plus \$18 million Council has already provided for existing claims (adjusted from the \$19.8 million in the 2009/10 Annual Report to account for claims now likely to follow the FAP route rather than the litigation route). The \$19.8 million in the financial statements assumed that all claims would opt for the litigation route, which was appropriate as that was the only route available to claimants at that time.

Therefore, based on Officers’ financial modelling, peer reviewed by Council’s actuary, Melville Jessop Weaver, the financial cost to council is best managed by Council opting in to the FAP scheme.

### **7.3 Funding Options**

Council provided \$19.8 million in its 2010/2011 Financial Accounts for the estimated cost of “known” weathertightness claims. As the potential costs of future weathertightness claims have become clearer, officers have undertaken preliminary analysis in relation to the funding options available to Council. Detailed analysis of the options will need to be undertaken and considered in conjunction with other funding requirements and priorities.

Broadly speaking, the options to fund the potential liability will require Council to consider the appropriate balance of rates funding, operation and capital works reductions and increased debt. These options will need to be considered alongside issues of affordability for ratepayers, levels of service, Council’s recent

debt rating and funding policies; as part of the 2011/12 annual plan process and subsequently in the 2012-22 Long-Term Council Community Plan.

## **8. Climate change impacts and considerations**

This proposal does not require any immediate consideration in respect of climate change.

## **9. Conclusion - assessment of options and recommendation**

It is considered that the FAP will have positive effects when compared to the status quo. Analysis of the options shows the FAP proposal strikes a better balance between financial exposure and financial certainty, and that it is likely to achieve better social outcomes by getting more leaky homes fixed and fixed faster.

Officers consider the Council will be better served by accepting the proposal, subject to certain matters being resolved, than continuing with the existing litigation-only route. Further, by opting into the FAP, Wellington homeowners with leaky homes will be able to take advantage of the FAP and have a choice other than the current litigation option.

The increased repair of leaky buildings will improve the quality of the housing stock with a potential spin off in reduced health care costs from living in damp conditions. Money which might otherwise have been spent on legal fees will be used to fund repairs and to reduce homeowner's borrowing costs. The sooner repairs are commenced the less it is likely to cost to effect repairs. Finding a solution without recourse to adversarial process will also reduce the level of stress to affected homeowners with consequential social benefits.

Contact Officer: *John Scott, Group Manager, BCLS and Stephen Cody, Manager Compliance (Building)*

## Supporting Information

### **1) Strategic Fit / Strategic Outcome**

*This paper relates to Building Control and Facilitation.*

### **2) LTCCP/Annual Plan reference and long term financial impact**

*Council will consider the funding options under section 101(3) Local Government Act 2002, as part of the 2011/12 Annual Plan and the 2012-22 Long-Term Council Community Plan.*

*Section 97 of the Local Government Act 2002 does not apply to the proposed decision and no amendment to the Long-Term Council Community Plan is required (see 4 below).*

### **3) Treaty of Waitangi considerations**

*N/A.*

### **4) Decision-Making**

*Council has obtained legal advice and it is considered that the proposal in this report is not a decision to which section 97 applies. (Section 97 of the Local Government Act 2002 provides that certain decisions are to be taken only if they are provided for in Council's Long-Term Council Community Plan).*

*Even if this conclusion challenged, section 97 will not prevent Council from opting into the FAP unless it is a decision that will, directly or indirectly, significantly affect the cost to Council of meeting its potential liability arising from involvement in the construction of residential dwellings that are not weathertight. Having regard to Council's policy on significance below and the analysis in section 7 of this report, it is not considered that this cost will be significantly increased. If anything it is likely to decrease. Accordingly there is no need for the proposed decision to be explicitly provided for in Council's Long-Term Council Community Plan.*

*The decision is not significant (as legally defined – ie a decision with a high degree of significance) and for the following reasons the decision is assessed as having moderate significance:*

- It is considered that Council's response to weathertightness issues may have a moderate impact on social well being, while the FAP in particular may have a moderate impact on the economic well being of particular home owners and*

- *The proposal's likely impact on and consequences for persons who are likely to be particularly affected by, or interested in the matter are moderate. While rejecting the FAP may impact some home owners (for instance any who cannot fund litigation), opting into the FAP will provide a choice between the status quo and, at the election of home owners, another option to litigation.*
- *The proposal's likely impact on and consequences for the capacity of Council to perform its role and the financial and other costs of doing so are moderate (refer to section 7).*
- *The financial impact of opting into the FAP (as opposed to the status quo) will not exceed 10% of the total rates revenue in any year to which the proposal relates.*
- *While any rates increase necessary to fund Council's overall liability arising from its involvement in the construction of residential dwellings that are not weather-tight may have some effect on a large portion of the community, opting into the FAP will only be material to the relatively small number owners of homes which have weathertightness issues. Of itself, the FAP is anticipated to either reduce or not materially alter the quantum of Council's overall liability.*
- *While weathertightness issues have a history of wide public interest in the community, it is expected that any 'public controversy' generated by the proposal will be moderate*

## **5) Consultation**

### **a) General Consultation**

*Refer to section 5.1 of this report.*

### **b) Consultation with Maori**

N/A

## **6) Legal Implications**

*Council's General Counsel and external lawyers have been consulted during the development of this report.*

## **7) Consistency with existing policy**

*There is no current Council policy.*