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Canterbury Earthquake Recovery Authority

To Minister of Finance
Minister for Canterbury Earthquake Recovery

Subject Transaction design issues relating to the Crown's offer to insured, red-zone residential property owners

Action required Consider recommendations and advise CERA of decisions by **15 August**, in order to enable documentation to be printed

First Contact Rosalind Plimmer
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Sharyn Pilbrow
Advisor, Recovery Strategy, Planning & Policy *Withheld s 9(2)(a)*

- 1 **note** that the Minister of Finance and the Minister for Canterbury Earthquake Recovery have been authorised to have Power to Act until 18 August 2011 to finalise the transaction design, sale and purchase agreements and communications relating to the Crown's offer to purchase insured, residential properties in the Christchurch red zone to enable the 18 August deadline to be met [CAB Min (11) 28/16 refers].
- 2 **note** that payment of a deposit is a common feature of a residential conveyance transaction.
- 3 **note** joint ministers amended Recommendation 10 Cabinet decision [CAB Min (11) 27/13 refers] relating to deposits to state the following that either a deposit of the lesser of 50 percent of the purchase price less any insurance payments already made and \$50,000 is paid where the settlement date is less than six months from the date of the agreement, or a prepayment of up to 50 percent of the purchase price less any insurance payments is offered where the settlement is more than six months from the settlement date.
- 4 **note** that the payment of a significant deposit was to assist property owners, including those who wish to rebuild by reducing the cost of bridging finance while their home is being built.
- 5 **note** that the a deposit of 50 percent of the purchase price where the settlement date is more than six months from the date of agreement could incentivise property owners to delay settlement for six months and increases administration costs of the transaction for the Crown.

6 ~~rescind~~ the amended Cabinet decision and instead **agree** that

- a) no deposit be paid if settlement occurs within six weeks of the agreement being signed.
- b) If settlement is greater than six weeks of the agreement being signed a deposit of the lesser of 50 percent of the purchase price less any insurance payments already made and \$50,000.

~~Agree/disagree~~
Minister of Finance

Agree/disagree
Minister for Canterbury Earthquake Recovery

- 7 **note** currently under the terms agreed for the sale and purchase agreement the Crown has to give to the Vendor notice 5 days or more before settlement if it does not have all of the requisite information from insurers, EQC and the Vendor to enable it to settle.
- 8 **note** if the Crown does not provide that notice, and fails to settle on the agreed settlement date, the Crown should be liable for default interest (this is common practice in residential conveyance transactions).
- 9 **agree** to a default rate of 10% per annum to be paid by the Crown for not providing notice and failing to settle on the agreed settlement date.

~~Agree/disagree~~
Minister of Finance

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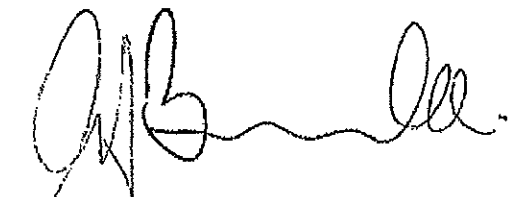
- 10 **note** given the number of special cases transaction emerging, a break clause may be prudent, this will also assist in preventing gaming in the system.
- 11 **agree** the Crown may seek the right to not complete a transaction where:

- a) The Crown considers that completion would not be consistent with its intentions (for example, if it considers the contract does not properly respond to the situation or the contract is being gamed) and/or
- b) The situation changes (for example, following another major natural disaster)

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Minister of Finance

Agree/disagree
Minister for Canterbury Earthquake Recovery

Hon Bill English
Minister of Finance



Hon Gerry Brownlee
Minister for Canterbury Earthquake
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Purpose of report

- 1 This paper discusses further transaction design issues relating to the Crown's offer to purchase insured, residential properties in greater Christchurch's red zones.

Background

- 2 For insured residential property owners, Ministers with power to act agreed on 23 June 2011 (which was noted by Cabinet on 27 June 2011) to identify four zones of land damage for the greater Christchurch area. The paper relates to the Red Zones, the worse affected residential zones, where rebuilding is not likely to occur in the short-to-medium term. In that decision, Ministers also agreed to a choice of two packages to insured residential property owners in the Red Zones.
- 3 On 18 June, Cabinet considered the design of this transaction including any adjustments to the purchase price, the form and type of additional support provided by the Crown, and issues relating to the implementation of the transaction [CAB Min (11) 27/12 and CAB Min (11) 27/13 refers].
- 4 Cabinet also authorised the Minister of Finance and the Minister for Canterbury Earthquake Recovery to have Power to Act until 18 August 2011 to finalise the transaction design, sale and purchase agreements and communications relating to the Crown's offer to purchase insured, residential properties in the Christchurch red zone to enable the 18 August deadline to be met. [CAB Min (11) 28/16 refers]
- 5 This briefing covers matters subsequently raised by the lawyers drafting the sale and purchase agreements, relating to the transaction design decisions considered on 18 June. They are:
 - Deposit payment to insured red zone residential property owners
 - Default interest payments for non-settlement
 - Giving the Crown the ability to cancel agreement or defer settlement

Deposit

- 6 Deposits are usually incorporated in sale and purchase agreements to penalise the purchaser should they not proceed with the purchase. However, there is no risk of the Crown failing to proceed with the transaction in this case.
- 7 Property owners, who accept the Crown's offer, will be able to use their deposit to purchase reduce/service debt or will be able to be put it towards a new home. Providing a deposit may also make the offer more attractive to property owners.
- 8 On 18 July, Cabinet:
 - noted that payment of a deposit is a common feature of a residential conveyance transaction
- 9 Cabinet agreed that either a deposit of \$50,000 will be paid where the settlement date is less than six months from the date of agreement, or a prepayment of up to 50 percent of

the purchase price is offered where the settlement date is more than six months from the date of agreement [CAB Min (11) 27/13 refers].

- 10 Joint Ministers subsequently amended to be "that either a deposit of the lesser of 50 percent of the purchase price less any insurance payments already made and \$50,000 is paid where the settlement date is less than six months from the date of agreement, or a prepayment of up to 50 percent of the purchase price less any insurance payments is offered where the settlement is more than six months from the date of agreement".
- 11 The payment of a significant deposit was to assist property owners we wish to rebuild by reducing the cost of bridging finance while their home is being built.
- 12 However, the larger deposit of 50 percent of the purchase price where the settlement date is more than six months from the date of agreement, could incentivise property owners to delay settlement for six months. This would not enable people to move on with their lives. It would also increase costs to the Crown, as the Crown may wish to register interest in properties, where substantial deposits have been paid to properties with long settlement and will add complexity to the administrative process.
- 13 Following this further advice from the lawyers, it is proposed that all previous decisions by Cabinet and Joint Ministers relating to deposits be rescinded, and the following is approved instead:
 - a) that no deposit be paid if settlement occurs within six weeks of the agreement being signed.
 - b) if settlement is greater than six weeks of the agreement being signed a deposit of the lesser of 50 percent of the purchase price less any insurance payments already made and \$50,000.

Default interest payments for non-settlement by the Crown

- 14 Currently under the Crown's sale and purchase agreement, the Crown has the ability to give to the Vendor notice 5 days or more before settlement if it does not have all of the requisite information (from insurers, EQC and the Vendor) to enable it to settle. However, if the Crown does not provide that notice, and fails to settle on the agreed settlement date, the Crown will be liable for default interest.
- 15 Given the non-commercial nature of the red zone transaction, the Crown considers a interest rate of 10% per annum to be fair as this is the default interest rate for residential transactions.

Giving the Crown the ability to cancel agreement or defer settlement

- 16 Given the nature of the transaction and the number of 'special cases' emerging, it may be prudent to include a discretion for the Crown not to complete. Although there could be some pushback, the existence of such a break clause may also prevent attempts to game the situation (e.g. removing fixtures from the dwelling prior to settlement).
- 17 It is recommended that the Crown seek the right to not complete a transaction where:
 - a) The Crown considers that completion would not be consistent with its intentions (for example, if it considers the contract does not properly respond to the situation or the contract is being gamed) and/or
 - b) The situation changes (for example, following another major natural disaster).

Next Steps

- 18 We recommend that the Minister for Canterbury Earthquake Recovery and Minister of Finance agree the recommendations in this report.
- 19 The letters of offer are being sent to property owners on 18 August. Therefore it is important that outstanding decisions relating to the transaction design are finalised promptly. Your advice is sought as early as possible on 15 August.

Recommendations

- 20 It is recommended that Ministers:
 - a) note that the Minister of Finance and the Minister for Canterbury Earthquake Recovery have been authorised to have Power to Act until 18 August 2011 to finalise the transaction design, sale and purchase agreements and communications relating to the Crown's offer to purchase insured, residential properties in the Christchurch red zone to enable the 18 August deadline to be met [CAB Min (11) 28/16 refers].
 - b) note that payment of a deposit is a common feature of a residential conveyance transaction.
 - c) note joint ministers amended Recommendation 10 Cabinet decision [CAB Min (11) 27/13 refers] relating to deposits to state the following that either a deposit of the lesser of 50 percent of the purchase price less any insurance payments already made and \$50,000 is paid where the settlement date is less than six months from the date of the agreement, or a prepayment of up to 50 percent of the purchase price less any insurance payments is offered where the settlement is more than six months from the settlement date.
 - d) note that the payment of a significant deposit was to assist property owners, including those who wish to rebuild by reducing the cost of bridging finance while their home is being built.
 - e) note that the a deposit of 50 percent of the purchase price where the settlement date is more than six months from the date of agreement could incentivise property owners to delay settlement for six months and increases administration costs of the transaction for the Crown.
 - f) rescind the amended Cabinet decision and instead agree that:
 - i. no deposit be paid if settlement occurs within six weeks of the agreement being signed.
 - ii. if settlement is greater than six weeks of the agreement being signed a deposit of the lesser of 50 percent of the purchase price less any insurance payments already made and \$50,000.
 - g) note currently under the terms agreed for the sale and purchase agreement the Crown has to give to the Vendor notice 5 days or more before settlement if it does not have all of the requisite information from insurers, EQC and the Vendor to enable it to settle.

- h) **note** if the Crown does not provide that notice, and fails to settle on the agreed settlement date, the Crown should be liable for default interest (this is common practice in residential conveyance transactions).
- i) **agree** to a default rate of 10% per annum to be paid by the Crown for not providing notice and failing to settle on the agreed settlement date.
- j) **note** given the number of special cases transaction emerging, a break clause may be prudent, this will also assist in preventing gaming in the system.
- k) **agree** the Crown may seek the right to not complete a transaction where:
 - i. The Crown considers that completion would not be consistent with its intentions (for example, if it considers the contract does not properly respond to the situation or the contract is being gamed) and/or
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