Ka Taea e Tātou

Emerging Māori CHP Wānanga

Recorded Transcript

Financial Viability

Content	
The Financial Viability Performance Standard	John Bolsover | Community Housing Regulatory Authority

The transcript below was captured at the live webinar and includes minor grammatical adjustments for the readability of the audience.

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TE MATAPIHI

HE TIROHANGA MŌ TE IWI TRUST

The Financial Viability Performance Standard | Auckland Council

Jen Deben

Welcome everyone, now we are moving on to our presentations from the Community Housing Regulatory Authority and dear I say it, it is double trouble today with Martin Farmer and John Bolsover, So John has recently joined the Authority. He brings with him a wealth of financial expertise and has been, I think, evaluating a number of applications and as well as the monitoring reports. So while he has recently joined the Authority he is actually getting really good oversight of all the different organisations that are on the register but also that are wanting to join the register and so he has some really good insights to share with us in terms of how we can be presenting our information or the level of details that they're requiring before we are putting in an application.

John Bolsover

Kia ora Jen, and thank you, I was interested in your introduction of double the fun, sort of applied to finance and financials; we'll see what we can do. I spent most of my career as an economist, so most of my jokes are economist jokes, I'm afraid, so maybe we'll leave those to the end. Thank you for the opportunity to bring us all together and hear some of your stories, Jen. Thinking about the insights from Te Kāinga Atāwhai housing yesterday, I had a brief peek at your marae in the Taumata o Kupe cultural hub at a meeting last month; I think it was on Tracey's phone over a Zoom meeting and Christine and Ann, thank you for sharing your journey with us, it's great to see the dreams of your mum Christine, and your whānau coming true, and I love your work. One of the things at our meeting with Te Kāinga Atāwhai housing did highlight was the value in meeting people face to face. In that respect, I was able to have my questions answered by Sonia, Tracey, and Julian Brown who answered my questions, but also gave me comfort that the project was in good hands. Julian's managing director of Kauri Advisors with a wealth of experience, and he was clearly all over the management of the project, so that really did give me significant comfort, Christian, thank you for sharing your experience and vision this morning; those home ownership statistics speak to the growing divide that the recent increase in house prices have magnified and good luck in your journey to start trying to address some of these absolute inequities. It's very interesting to hear a bit about your journey to find stable housing solutions for your whānau, and your plan to progressive home ownership and well spoken. It's great to see someone so young speaking with such experience, capability and I think Jen put it well in saying richness, so good luck with your application.

Turning to the dry stuff, financials, and I guess that's what we're here for, I'm aware that people generally only take two or three things away from a presentation, so I've tried to bear that in mind, if anyone wants to go into more detail and really get into the dry stuff I'm happy to answer any questions offline if needed.

We are going to discuss financial viability, why financial viability is important, how we assess financial viability, and that's principally through your financial statements and the following years budget documents, with examples and hopefully the examples should be familiar to your finance people at least, and we'll discuss financial risk management which is basically insurance. It comes down to three elements, audited financial statements, so those can be discussed with your accountant, a budget for the following year consistent with the audited financial statements, there may be timing differences, but we should be able to reconcile the budget documents with the auditors' statements, so that's what we're looking for, and also ensuring you have adequate insurance.

[Re-recorded insert has been added]

Performance standard 1.4e, it's one of the performance standards, and I think Marty said we are going to be renaming them and it relates to relevant accounting and auditing practices. So for this we require audited financial statements, in the name of the CHP, most if not all of our entities will be eligible to apply for not-for-profit public benefit entity simple format reporting, and your accountant should be familiar with that. Public benefit entities are defined as reporting entities whose primary objective is to provide goods or services for community or social benefit where any equity has been provided with a view to supporting that primary objective, rather than for a financial return to equity holders. I think it really relates to CHPs who have expenses of less than two million dollars I think is the threshold of annual expenses. If a CHP has subsidiaries, then we will require consolidate the statements for the group. Community housing operations must be clearly visible. The statements must include statements of income and expenditure, cashflow, financial position, and changes in equity, and I've got some brief examples of each to follow. The documents should also include analysis of any borrowing and commitments which will be covered in the notes and statements, the financial statements, the accountant will generally include those in the notes, if not we will look for a summary of proposed capital expenditure which is not captured in the audited financial accounts or budget documents, particularly if you've got projects on the go, or plans, you will need to show how they are financed.

We also require budget documents for the year, these should follow the format of the audited financial statements, particularly in relation to anticipated revenue and expenditure, assets, and liabilities, cashflow, and the assumptions on which the budget is based, and we'll look to understand what your commitments and financing are for any projects. As such the budget documents should include income and expenditure, financial position, changes in equity or a reconciliation of opening to closing equity, and they can usually get that from the financial position anyway, cashflow, the assumptions upon which the budget is based, and it must factor in the cost of running the housing service, and as I say any commitments and the financing of projects.

Here we have an example, an anonymised example of a statement of financial position, so viable capital structure means your organisation has a good balance of debt and equity to finance the operation, and any planned growth. This is from a charity on the charities register, I just happened to pick one, this organisation has assets of $1.2M, funded by liabilities of $59K, so that's your overdrafts, your debts, creditors and expenses etcetera, and equity of $1.17M, so it suggests a strong financial position, so that last line, they've built up net assets over a period of time, of over a million dollars.

The CHP would be expected to demonstrate through its audits and financial statements that it has the capacity to meet it's short- and long-term obligations. If we look at this CHP it's got bank accounts and cash of $330K, up in row one, three point one, so this charity clearly has sufficient available to funds to meet its current liability, so those expenses which are likely incurred in the next year, so current means over the following 12 month period, the CHP itself much be able to maintain a viable financial position, so if a CHP is a subsidiary and not financially viable on its own the authority may require and enforceable guarantee from the parent organisation.

So, the previous slide showed the position of the CHP, the organisation, the assets and liabilities and its own funding, this shows the revenue and expenditure over the past year. Appropriate financial performance means the ability to maintain financial performance to an appropriate level, we have CHPS with a broad spectrum of revenue, from low hundreds of thousands per annum, to tens of millions, this example, which is not a CHP, had revenue approaching half a million, costs of around, let's see $480K, and a surplus of $20K, to 2013. So just a modest margin there, but it also has a strong financial position. We expect that your organisations financial position will be consistent with the type of organisation, so going to our conversation earlier, for example modest results are not unusual for not for profit organisations, so while you're commercial entities, we do acknowledge and we do acknowledge and do understand that you are not for profit organisations, however we would not expect significant or ongoing repeated instances of inappropriate financial performances, and that would be for example recurring losses or even insolvency.

Community housing operations must be clearly visible, and this is to help us ensure that Crown funding for purchase of tenancy services is used for tenancy services, this means the CHP needs to show it has the ability to generate sufficient income to meet operating expenses, service debt commitments, and where applicable grow the business without compromising existing services. Income from providing community housing should be sufficient to cover the cost of the provision, ideally there should be no cross subsidisation from CHPs other businesses. We expect that the CHP will have relevant financial policies and procedures in place as outlined by Marty yesterday, including financial reporting to the management and board.

This just shows an example of a change in equity or net assets, so this entity reported an operating surplus of $19K in the 2016 year, as shown on the previous slide, and that flowed to an increase in accumulated funds, or net assets, or equity of the same value.

For those not familiar with statement of cashflow, this records the entities cash and cash equivalents, so money in your bank accounts, entering and leaving the business, this provides a record of how well the entity generates and manages its cash to pay operating expenses and financial obligations, so the statement of cash flow complements the income and expenditure statements and the balance sheet. In this example, the charity received cash from donations and fund raising, fees, goods and services and interest, and dividends of $598K in the 2016 financial year, and made payments to suppliers of $504K, providing a net surplus from operating activities of $94K. That net surplus flowed through to an increase of cash and money in the bank accounts, from $236K to $330K. So the cashflow provides a picture of how the entities operations are running, really where its money is coming from, and how the money is being spent. It helps us determine how much cash and money in the bank ultimately is available for the entity, the fund its operating expenses and paid down debts.

Generally, the cashflow is in three parts, we are interested to see the net cash position from operating activities, but there's also, the other parts include the cash flow from investing activities, which will be around the purchase and sale of assets, for example housing and financing activities which relates to loans and repayments of debt. So they're all of interest, we'd probably look first to see what's happening with the operating activities, but then the rest needs to tie in with your plans, and your budgets.

So if we look to the next two slides, which cover the need to ensure you have adequate insurance, proportionate to your risk exposure, you should provide copies of insurance policies, the registered subsidiary must be a named beneficiary, policies and procedures should reference regular reviews, coverage and include a statement of commitment from the board, to continue to provide accommodation in the event of an occurrence requiring a claim.

If a CHP leases properties, it is not required to insure those properties, but is expected to consider whether property owner's insurance is sufficient to manage the associated risk.

Why the long faces, this is lifted from a joke, a horse walks into a pub, the barman asks why the long face, so that's my attempt to introduce some fun to what's a very dry subject.

So, if you have any questions, it's important to understand that our requirements should not be viewed as roadblocks, and understanding your financial position, outlook and commitments is important to ensure you can continue to provide your services, which is important for you and your tenants. We have a regulatory function, but in doing so will support you where we can. If you take three things out of the presentation, it comes down to the three elements, audited financial statements, a budget for the following year, and ensuring you have adequate insurance. Thank you.

[Re-recording inserted here]

Jen Deben

Thank you, John, that's good insight, are there any, in the time that you've been with the authority, are there any I guess common themes that are coming through that you're seeing where there are additional requests or requirements that are needing to be asked, that you could share with us today just to help people as they're preparing their applications?

John Bolsover

I guess with the budget documents possibly not having the, a lot of them focusing on cash flow, some may focus just on the main projects without being in relation to the entity as a whole, and sometimes not providing that link between the budget documents and the financials I'm struggling to see much to get that continuity between the budget documents and the financials, and so that request for information just to clarify what the entities budget documents relate to and how they relate to the audited financial statements because sometimes there's been a little mismatch. Sometimes it's just purely timing because the budget documents were put together earlier in the year and the audits were for another period, and of course one of the things we have at the moment is the environment is changing, so we've been through a very benign period for 10 years, and all of a sudden you've got inflation, you've got supply disruptions, you've got all kinds of things which could impact on the budget, so I've just come back maybe with one or two questions in relation to some of their assumptions or trying to tie back how the budget relates to the financial documents.

A number of them may be not showing all the income, the balance sheets the income expenditure and the cashflow, so they'll just show one part in those budget documents, so for the most part that's been sufficient to give me comfort, but we'll go back with a recommendation suggesting we would like to see it next year, more just to fill in some of the gaps possibly, but again we're not looking to create roadblocks, but we're trying to make an understanding of what it is we do require as well. But we will also review our processes too, and our requirements.

Jen Deben

Thank you, John, and do you think that, you've mentioned some of the difficulties that are happening in the system and in the economy, so there are the supply chain difficulties which is pushing out how developments are progressing, there's also increased inflation, there's also increased interest rates, do you think it's become more difficult to show future financial viability?

John Bolsover

Yes, I mean who knows what, if you look at the federal reserve, 12, months ago they were forecasting inflation in the States to be around about two per cent, it's sitting up about seven and half, eight per cent, so if the federal reserve are finding it difficult to forecast what's going on a year ahead, it makes it very difficult. Your plans a year ahead need, they're about having the processes in place and trying to understand what is going to impact your business, but it has, it is a more difficult environment. Planning, I think it's been attributed to Lincoln or Winston Churchill, people who fail to plan are planning to fail, look you do need to have those plans in place, and we're looking to have budgets in place, and if it looks like you'll forecast inflation at three and a half per cent or two per cent and it's sitting at six per cent now, I might ask the question, but we're not going to ask you to redo your budgets or something like that, you're aware of the environment, it's about having the process, as much as anything as having the process in place because we don't know what's going to happen in six months or a year ahead, but you need to be, a business does need to have those plans and those budgets in place to know where it's going and it's great to see Christian talking about those long term plans as well and those visions, we're looking to see just over the year ahead, and most of the CHPs that we would look at, you're looking at the audited financial statements, and the one's I've seen are in a reasonably strong position, so that's the basis really that gives me the comfort, but we're also then looking at the budget just to ensure, just to get a view of what projects you have in place, how they're being financed, feasibility studies and things like that.

It's the audited statements that give the comfort, the position, where the CHP is at the moment, then the budget gives us a feel for what's your planning, and you are, at least you are doing the planning which is important for viability for organisations, but we do understand that it is a changing environment, and it will be more challenging for CHPs in the following decade and businesses than it has been, it's been particularly benign environment over the last 10 years with falling interest rates, inflation contained and with the growth that we've had on the back of support from central banks and governments around the world. I think it's going to be a more challenging period over the next decade, so it will be important to plan, but yeah, we're not saying that you should know what's going to happen in 12 months' time, you've got to think about it, and think about what some of the obstacles are going to be, and think about what your servicing requirements are going to be, and whether your organisation has that ability to meet those servicing requirements.

Jen Deben

Thank you, John, you're right, I can hear what you're saying in terms of your risk management and showing that your plans are in place, even if you can't forecast exactly what's going to be happening 12 months down the track. So, thank you for answering those questions, I'm just going to open it up to the ropu and see if there are any questions that you would like to ask of John around financial viability.

Matthew Heke

Thank you, Jen. Kia ora John this is Matthew Heke here from Te Taumata O Ngāti Whakaue. Just a couple of questions and I think Jen has sort of possibly answered it, and I'm using Te Rau o te Korimako as the example where a limited liability was set up, so they have no record, so with

Ngāti Haua and Ngāti Tamaoho, did those parent companies need to provide their audited financials?

John Bolsover

So, we need the financials of the entity, the subsidiary, so whatever…

Matthew Heke

So, in this instance they're not a subsidiary, it's actually a new company, there's the joint ownership, so there was a separation from Ngāti Haua and Ngāti Tamaoho.

John Bolsover

So, it's the new company that will be looking to understand and need the financials for.

Matthew Heke

That's right, so with the new company I have no financials, I haven't started, and I suppose because I like this idea of the limited liability and I wanted to go and talk to some of our commercial entities, but it's whether they're prepared to say right, audited accounts for your application process, or and I did hear before, where we could take a guarantee from them that they'll make sure that there's a financial viability but I'm assuming that you'd still need to see the audited financials, and not just a letter of guarantee.

John Bolsover

So, we would need, say, the financials for the company, or the entity which is providing the guarantees. Do they have financials?

Matthew Heke

Yes, yes, they do, I'm just sort of prepping myself to start a couple of conversations.

John Bolsover

Yes, I mean talk to us, but the audited financials for the company offering the guarantee. There are instances where, you know, we do have entities where you understand that while we're interested in the CHP, when you're looking at it, and there's trusts involved, and things like that, and parent companies, you do, and in fact we'll note it in some of our reviews, that actually the viability of the CHP is intrinsically linked to the viability of the organisation of which it is a subsidiary of, it's not like in the banking sector where with the banks they've got open bank resolution for banks in New Zealand, whereas if the banks in Australia fall over, the banks over here can open their doors the next day, there will be instances where really the CHPs are, they will probably stand and fall by the performance of the parent organisation, but in this instance yes, we will look at the financials of the entity offering the guarantee.

Matthew Heke

Kia ora.

Dean Straker

Kia ora John this is, Dean Straker from Te Awhina Marae Redevelopment Committee, one of the things I was a bit confused on was how, are you expecting us to set a market rent in the financials, or are we following the policy, I didn't really understand the difference between the IRRS rent, and the affordable rent, and a market rent, and which one we would put into our financials for you to look at.

John Bolsover

We're not necessarily looking for a market rent, we're just looking for whatever represents the model for your business, so we understand that you're not for profits, and a lot of these charities and trusts are not necessarily charging a market rent, so whatever is relevant for your entity, we're not particularly looking for one thing or the other.

Martin Farmer

So market rent of course is what the property could achieve on the open market in the private rental market, an income related rent subsidy tenancy is where the tenant is taken from MSD social housing register and the tenant pays 25 per cent of their income and the Crown pays the remainder, the difference between that 25 per cent of their income that's contributed by the tenant and the market rent on the property, so the CHP would still receive a market rent for that property, but it would be the Crown that would be paying the main portion of that rental income.

Affordable rent is when the community housing provider owns the property, they're not receiving any direct government assistance, the tenant might receive assistance through the accommodation supplement, but in order to make that property affordable for its tenant group it will offer that property at a discount to market rent, so say 80 per cent of the market rent, and it would be the CHP that actually takes the hit in terms of it loses out on that 20 per cent of market rent to make that property affordable. But under an IRRS tenancy, because the Crown contributes the rest of the rental income up to a market rent, the CHP still receives the market rent, so it is useful for the CHP to receive an IRRS subsidy and become registered with us. I hope that made sense.

Robert Macbeth

A portfolio of properties for a registered CHP you could have a mixture of things, you could have some houses that you're just subsiding, some houses that you're getting funding from Te Puni Kokiri from, that requires you, that is grant funded to you charge a rent that looks like 30 per cent of income and you might also be getting IRRS, in relation to some tenants, in which case you can model your business on market rent.

So anyway it's all a mixture, and we've got some papakāinga that would have, you know they're managed through a registered CHP, half of the papakāinga would be on an income related rent subsidy, so the tenant's paying 25 per cent of income, the other half are not, for various reasons getting IRRS, so the ropu would be charging a different rent, probably based on about 30 per cent of income and some registered CHPs would charge a discount to market which could be like 80 per cent of market.

John Bolsover

Thanks Rob, that's very true, you do, you see different models and different mixes for various entities with these mix of government contracts and IRRS, and also some who are, and also through regional councils and things like that, also some are on leased land which is subsidised, or at maybe a peppercorn rental, so their expenses are lower, and also at the end of the day, they're not for profit, a lot of these, so they're not looking to make commercial margins, so they are able to offer non market rentals and still achieve their goals.

Matthew Heke

That's excellent information, the only other thing I'd like to ask is how would we, we are funded by TPK, we don't know whether people who are renting will get IRRS, and we do want to charge an affordable rent, what are you expecting to see in our financial documents, and we're just going to have a guess on what we would get.

Robert Macbeth

Jen, can I go here first in terms of advice in terms of you dealing with Te Puni Kokiri, so and I have in house knowledge of this, when you're talking to TPK, they are going to want you do what's called the PVAD, which is basically your financial model assumptions for the papakāinga, or for the housing. I literally have physically got one in front of me at the moment, my advice to ropu is to, unless you're absolutely certain, you're going to get IRRS, unless you are absolutely certain that the tenants are going to be off the social housing register, and you're going to have an IRRS contract with HUD, my advice would be to model your PVAD on the assumption that you're not going to get the IRRS, so where there's a box in the PVAD which says IRRS yes or no, I would go for no, and just model it on the assumption that you're going to charge the tenants an affordable rent, which is based on 30 per cent of income, TPK generally accept that as a viable model, unless there is some certainty that the IRRS is going to apply, like I mentioned yesterday with

Mahurehure Marae, right from the outset we knew that that was going to be an IRRS scenario, so that was built into the model.

But most of our papakāinga don't assume IRRS, most of our papakāinga trusts are not registered CHPs. Then TPK then put in a, there's a clause that they'll put in the funding agreement, which basically says that the grant is assumed on the basis that you're not going to get IRRS market rents for the properties. In the event that you subsequently get IRRS, or that you're rent revenue is higher than what the model suggests, these are the sorts of things we expect you to put the surpluses into, and there's a sort of list of things, so it can be put aside for fund for future affordable housing, you can do other things with it, you can provide different support.

So Te Puni Kokiri is basically accepting that there is the possibility that you're going to get more revenue than what the model suggests, that's ka pai, as long as you commit to reinvesting the surplus back into housing for your whānau, and then they've got this new clause that says you know, just talk to us once a year for the first ten years about how you're applying the surpluses.

So, my advice would be unless you are absolutely certain you're going to have some IRRS applying there, err on the conservative side and just assume that IRRS is not going to be there and that you're going to charge a rent that's affordable to your whānau.

Matthew Heke

Thank you Robert, that's excellent advice and that's what we do, it makes it easier to produce the financial documents.

John Bolsover

Thank you Robert, that's I think, the key thing was having a financial model and what assumptions is it based on, so that we can just understand what those assumptions are, for example you may go to the tenancy services bond register to get an estimate of what the medium rental is, in your area and you're going to charge 80 per cent of that, then that would be good to know in your assumptions, this is how we got there.

Martin Farmer

And it sounds from what Robert said there are benefits to doing it the way he suggested and as John said as long as you've got a consistent model we'll be happy with that.

Jen Deben

Thank you everyone for all those pātai, definitely delving a little bit more into some of the complexities on the additional information you might need to provide if you're putting forward a subsidiary, or even if you're putting forward just a completely new and different CHP entity that is actually separate from what might be thought as the parent entity but is actually part of our wider group.

Dean Straker

Kia ora Jen, it's Dean again, it's not a question, but it's just something that we learnt in our papakāinga development is that if you are applying to be a community housing provider, the development levies from the council are waived in the process, we didn't actually know that, until we went to council and they asked us if we were going to be a community housing provider, so for a 20 house build, you're looking at over $500K being saved just by you being a community housing provider, so a lot of groups aren't aware of that, as we weren't, so I'd just like to share that information with everyone.

Jen Deben

Kia ora Dean, that is really valuable information, I think everyone will welcome knowing that, so, which Council is that with Dean?

Dean Straker

That was with Tasman District Council, TDC, and I think it applies with most councils, but that was TDC.

Jen Deben

Great thank you, which segue ways in quite nicely into some mahi that Te Matapihi is doing, so because Auckland Council and the IMSB have supported us to bring together these wananga you may have picked up that we did have a wananga last year which was in person, and we were also hoping to have this wananga in person as well, but just with the Omicron outbreak we couldn't guarantee a date that we could bring everybody together or a date that the members of CHRA were able to travel and attend, which is why we've gone online. But as part of that, some great information has been coming our way, so we are developing some documents and we're going to be going over what those are going to look like tomorrow, but one of the ones we're developing is the benefits of becoming CHP registered. And the intended benefit of the regulatory framework is for you to be able to access the income-related rent subsidy, but as more information has been coming our way, there's quite a long list of other benefits as to why it could actually suit your organisation to become a CHP. IRRS is part of it, but in addition because of the high level of due diligence, there are other agencies and funders that look very favourably on community housing providers, and it looks like we've also got another one here from councils in terms of waiving their development costs which makes a really big difference to the bottom line.

I did notice that Thalea, I think that you had your hand up, were you wanting to ask a question?

Thalea Tane

Kia ora Jen, you just answered it actually, it was really around what other benefits are we unaware of, the other, I guess, wonderful essence about these type of wananga is we can actually share that type of knowledge of, you know, the knowledge that we know of, so just wanted to quickly share one thing that I've learned through Kāinga Ora, because we are also looking to develop some whenua, in south Hokianga, and that is that we were unaware that Kāinga Ora actually have specialists that will jump on board with us to help us change a zoning, you know, via Far North District Council. So, you know, these are some of the wonderful benefits and tips, I guess, or sharing of knowledge and networks that could help us all. So just to repeat that Kāinga Ora actually have a specialised team that actually helped to negotiate zoning changes. And so you could just appreciate where we are located a lot of our zoning, our whenua is what they call rural production, so based on that zoning we are quite restricted in terms of how many houses we can build, however if we change that zoning into residential then of course those numbers increase. With the help of a specialist team from Kāinga Ora, you know, we aspire to do that in the very near future, so just a little bit of information sharing for you all. Kia ora.

Jen Deben

Kia ora Thalea, thank you so much for that, that's great insight and one that we're definitely going to note.

So that brings our session today to a close, it has been another wonderful session, there's been some great information, I'm really pleased that today we were able to capture a lot more questions, and also for many of you to participate and ask questions that were really relevant, to either your area of business or your rohe, and to be able to build up those connections with the Regulatory Authority. And also, to Christian, thank you so much for sharing in the way that you did. I'm sure that you've seen in the chat and also in the comments from people that what you have shared with us today has resonated very strongly and there's a lot of gratitude for you coming on board and sharing that today.

Thank you, Christian.

Christian Dennison

Thank you very much and thank you everybody for a rally great hui this morning, I have learnt lots, hopefully we all have, and we'll see you tomorrow. Ngā mihi nui tātou.

Kia tau ki a tatou katoa, te atawhai o to tatou Ariki, a ihu karaiti, me te aroha o te Atua, me te whiwhingatahitanga, Ki te wairua tapu, Ake, ake, ake, Amine.

Kia ora.