

Transportable Housing Finance Issues

Summary of report by Find Finance for PrefabNZ
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1 Introduction

Transportable housing manufacturers are struggling to sell their houses to first-home buyers as many cannot obtain traditional mortgage financing. This also means that transportable housing is currently not an 'affordable housing' measure.

PrefabNZ

The lack of availability of mortgage finance is a constraint on the uptake of manufactured housing. Generally, offsite manufacturers of homes do not provide finance to purchasers of these houses. The purchaser of a manufactured home must provide progress payments of up to 90% of the cost of the house while it is under construction in the builder's yard.

First-time buyers or buyers with low or no equity in an existing property cannot fund these pre-delivery payments in full and banks will not provide mortgages to purchasers until the dwelling is on-site, connected to services, and fulfills Council compliance requirements.

The lack of availability of mortgage financing for manufactured housing reduces the demand for that type of housing and contributes to New Zealand's housing affordability problems.

Research Question:

How could it be possible for a first-home house purchaser to buy a transportable home from an offsite manufacturer with only 10% or 20% equity and needing finance for the balance?

Example scenario:

A buyer is choosing between a \$400,000 existing house or buying a \$200,000 prefabricated house on a \$200,000 section (including all costs such as connection to services, landscaping etc).

Version A: Existing house

The buyer has 20% equity ie \$80,000. If a buyer wishes to purchase an existing house then getting an 80% mortgage for a \$400,000 house is relatively straightforward (subject to normal mortgage lending criteria).

Version B: Transportable house

If a buyer with low equity wishes to purchase a transportable house the situation is difficult. The house builder will require say \$180,000 (ie 90% of the full contract price) or a similar amount before the house can leave the builder's yard and is delivered.

The buyer will usually make progress payments. Typically, there will be an initial payment upon signing the building contract and progress payments at certain milestones (eg. when wall framing is up or when roofing is on). The proportion and timing of progress payments will vary by builder. However, it is typical that most of the price is paid before the transportable house is delivered.

So a buyer wishing to purchase say a \$200,000 house who has \$80,000 equity cannot do so unless they can find a substantial sum by way of mortgage. Also it may be that the buyer's equity has been spent purchasing the section - so in practical terms they have no cash available to make any progress payments to a builder.

Please note: the assumption is that the dwelling is a one-piece, fully-built house transported to a site on its completion. Other forms of off-site manufacture such as modules, kitsets and building components will present other issues which are worth exploring also.

Granting mortgages to first-time or similar buyers with low equity is more difficult for banks than for an existing house. Things can go wrong during construction and installation that could lead to a lender losing money. Enforcing security over the house may be difficult. Recovering enough money to repay the loan may be difficult and expensive. However, it may be possible to reduce risks for the bank enough to encourage them to make a high-LVR loan.

2 Work to date

PrefabNZ has been aware of this mortgage finance issue since being alerted to it by members of the public and PrefabNZ members – the following bullet-points mark key points to date.

- Emails on file alerting PrefabNZ to issues – Researcher in July 2012, Lawyer in October 2013, Client in April 2014
- PrefabNZ workshop with Anthony Harper lawyers (Chch) – October 2013
- BRANZ + PrefabNZ 'Getting Prefab to Market' programme – February - March 2014
- Kiwibank representatives on panel discussion at PrefabNZ CoLab, March 2014, Auckland
- PrefabNZ Workshop with Kiwibank – May 2014
- Report to Kiwibank – May 2014
- Report disappears into black-hole and PrefabNZ follows-up – 2014 / 2015
- Find Finance (Peter McDermott) meeting with PrefabNZ – November 2014
- Find Finance report to PrefabNZ – December 2014
- PrefabNZ meetings with Heavy Haulage Association, Jonathan Thompson – ongoing
- PrefabNZ meetings with Murray Wu, then Kelly McNaul, Kiwibank – early 2015
- PrefabNZ Board agreement to re-visit Finance project in second-half 2015 but little achieved due to PrefabNZ resource constraints – late 2015
- BRANZ report on disruptive innovation by Clark-Reynolds and Pelosi – June 2016

PrefabNZ has outlined a way forward based on Find Finance's report which provides some direction and action steps.

3 Preferred Way Forward – bank provides mortgage

As for any property transaction, there may be a number of alternative ways to obtain finance. These range from the major NZ banks through to secondary lenders and other players. Clearly bank loans tend to have lower fees and interest rates. They also have stricter lending criteria. Issues to consider:

- Can I get a loan (and if so is it economic)?

- Can I get the level of leverage I require?
- What are the conditions, fees and costs?

It will be most advantageous for buyers if they can get loans with lower fees and interest rates. An interim measure, before banks can be persuaded to lend on these transactions, may be to use more expensive non-bank sources of finance.

The following scenarios are possible and the first preferred option is explained below:

1. Bank provides mortgage
2. Second-tier lender provides mortgage
3. Bank provides mortgage and also benefits from additional support
4. Bank provides mortgage upon delivery and connection only. Third party funds up to this point.
5. HNZC Welcome Home Loan Scheme – include transportable houses

Scenario 1 - Bank provides mortgage

A loan for the construction of a house off-site to transport to a section and connect to services is more risky for a bank than one for an established house on land.

The bank will wish to have adequate security so if there is a default under the loan they do not lose money. Depending on the circumstances of the particular loan, the bank may be faced with a vacant section and a partially completed house as its security. This is poor security compared to an existing house and section.

Bare land is more volatile in value and difficult to sell in hard times – hence the reason banks lend smaller LVRs (Loan-to-Value ratios) on bare land.

Manufactured houses may be difficult to sell to another buyer and may need to be discounted substantially to find a purchaser who will accept the size, specification and price, and has a suitable site. Demand for a particular type of home may be very limited in that geographic location.

It is therefore unsurprising that presently banks do not wish to fund the progress payments on a manufactured house where the buyer has low equity.

Possible bank funding scenario

It might be possible to interest a bank to fund a transportable home and land package on the basis set out below. Please note: it may be that not all suggestions below are required.

Steps

1. Bank valuer checks the land, and house plans and specifications, and confirms the future value of the completed house and land.
2. Bank confirms all the costs required to complete the house relocate it, and install it at site to the condition required for the valuation to be applicable, eg. Council consents

landscaping and utility connections. This will include a contingency sum to cover cost overruns.

3. Bank makes mortgage offer.
4. Buyer contributes their equity. Note: discussion will be needed to consider the permutations of land ownership and buyer's equity situation.
5. Buyer makes initial payment to builder using own equity.
6. Bank receives security interest over house in builder's yard including the materials as in specification.
7. Bank will be granted access to complete house at yard or remove it from yard in case of default.
8. House will not be subject to prior security interest, eg. of building company's bank, or building material supplier.
9. Construction commences.
10. Mortgage is partially drawn down.
11. Bank funds pre-agreed progress payments to builder upon confirmation from bank valuer or quantity surveyor that work has been completed.
12. Bank may not be comfortable with 90% payments to builder and may require a lower amount so builder is taking some risk and incentivised to ensure house delivery and installation on-site goes well.
13. House transported to site.
14. House set on foundations and all connections made.
15. Builder may not get full payment until house is in place and rest of mortgage draws down, ie. not on physical delivery.
16. Bank Valuer confirms house is fully complying, has all necessary consents, is what was assumed in prior valuation and is connected to services as necessary.
17. Buyer draws down remainder of mortgage.
18. Final payment made to builder.

4 Action Steps

The following action steps are suggested to be taken in conjunction with PrefabNZ, Find Finance, Heavy Haulage Association, and BRANZ.

4.1 Understand the issues very clearly

Workshop with PrefabNZ Members to satisfy possible Bank queries including:

- How and when will the buyer acquire the land? Will first mortgage security be available and if so when?
- Will the buyer use all their equity on the land purchase, leaving none for the progress payments on the house?
- Who will coordinate the required works at the house site eg connections, landscaping, gaining Council consents, etc? Could a single reliable party manage these steps?
- What if the builder goes into receivership at any point? Will the bank have the house (and materials) as security or will the builder's bank, or a building material supplier, claim it?
- If the house is partially completed, can a third party gain access to complete it for the Bank (access to plans consents etc)? Is that practical eg would unpaid subcontractors interfere? What if a unique building system is being used?
- Does the builder have experience building this particular house, or is it new and different?
- What experience does this builder have? How many houses have they built and delivered? Any problems?
- What is the history of the people behind this building company ie bank experience, credit rating etc?
- What is the value of this house before delivery if it had to be sold to a third party to help repay the debt?
- Will the buyer 'accept' the house? What if there is a dispute? Is there a clear dispute resolution process? What happens if we as lender don't accept the house eg damage in transit? Has this builder had any past disputes over acceptance or quality/defect claims?
- Have all costs and permits necessary to connect the house been granted? How do we know all costs are covered? Is there an adequate contingency?
- How long will Council approvals take?

- If we had to repossess the house and sell it after delivery do we have the Council consents required (removal/demolition) and do we have the right to access eg from land owner?
- How much would it cost to repossess the house, transport it and store it? What if the house-in-a-yard doesn't sell?
- What if the buyer's situation changes before delivery eg they lose their job?
- What is the situation if a buyer requests variations that reduce specification and or increase cost? Is it realistic to stop this?
- Will the builder consider a lower level of total progress payments before delivery and can they afford to?
- If the bank puts in place mortgages for buyers with low equity to increase builder house sales, will the builder take the first loss if things go wrong eg put the first 25% of 'progress payments in themselves to be repaid on final payment?
- Given we could just make a loan to a buyer of an existing house with much less administration and risk, what fees and expenses will we need to charge to make it worthwhile for us to make this type of loan? Given the number of mortgages, is it worth it?
- If builders could accept a reduced level of payments prior to delivery this would make a transaction much easier to fund. For example, builder sights mortgage offer from bank and agrees to release house with 70% payments, with balance after house is on site. This will require careful thought about the competing interests of the different parties eg buyer's bank, builder's bank, builder's material supplier.
- How could the builder or another party take care of all the various tasks (consents, building work on-site, landscaping, etc) so the bank knows it will all be taken care of?.

4.2 Meet with bank lenders

Meet with a number of major banks (3-4) and make sure it is clear exactly what issues are causing difficulty for the banks and discuss preliminary solutions. Clarification of lending criteria would also be sought.

NB: Also possible to meet with NZ Bankers Association to elevate the problem to bank CEOs.

4.3 Post-meeting actions

After these meetings it should be clear if finance is available or, if not, what hurdles are in the way of achieving suitable mortgages for first-time transportable homebuyers. Further steps could then include:

- Mapping out any feasible solutions.
- Work with PrefabNZ members to resolve issues.
- Approach Central and Local Government agencies to see if some form of assistance could be possible.
- Work towards establishing an alternative funding mechanism if no solution is found, eg. a bespoke finance company.

4.4 Provide client guidance on how to buy a transportable home

These steps could form the basis of an infographic hosted on websites of PrefabNZ, Heavy Haulage Association, housing manufacturers, and house movers:

1. A buyer enters into a contract with a builder to purchase a house. (Question to PrefabNZ – are most agreements on the Master Builder’s standard contract?).
2. An initial deposit/progress payment is made.
3. Building consent is obtained from the Local Authority.
4. Builder commences construction at their premises.
5. Buyer makes progress payment at various stages of construction eg wall-framing up; roof on.
6. Local Authority inspections occur during construction.
7. Construction complete, a Code Compliance Certificate is obtained for the house ie that its construction complies with the building consent.
8. Builder will not agree to release house until say 90% of contract price has been paid.
9. Necessary consents are obtained for the building work on-site (building consent and, if necessary, resource consent, effluent discharge consent, water consent).
10. Engineer geotechnical report for site (if required).
11. The (insured for moving) house is transported to site.
12. House transporting company or a third party may build the foundations.
13. The house is positioned on foundations.
14. Home insurance policy coverage commences.
15. House is affixed to foundations.
16. [Builder expects the final 10% payment at this point?].
17. Connections to services (sewer/ septic tank; stormwater; water; electricity; and telecommunications).
18. Any landscaping done and fences, paths, clothesline, letterbox, decking, steps, driveway, garage.
19. Council completes building Inspection.
20. Council issues Code Compliance Certificate.
21. Council releases any bond.
22. A fully-consented and complying dwelling is now on site. No further work or consents are necessary.

5 Legal issues

Please note that many of the suggestions above will require legal advice to ensure all laws are fully complied with and respective obligations are fully understood and appropriately documented

6 Risk Transfer Matrix

Construction Off-site	Delivery	On-site works & consenting	Complete
Bank Mortgage			
Second-Tier Lender			
Second-Tier Lender			Bank
Third Party			Bank
Plant & Equipment Lenders Trade Finance Lender House Builder (gets payment after delivery) PrefabNZ Members Lending Fund or Guarantee			
Bank Mortgage + Other 'Risk Reduction' for Bank			
Comprehensive Building Guarantee Builder Accepts Lower and or Later Progress Payments PrefabNZ Members provide 'First Loss' guarantee to Bank Council provides (limited) 'First Loss' Guarantee to Lender PrefabNZ Members agree to buy house if a default occurs Housing NZ Welcome Home Loan Guarantee to Bank Builder or Third Party provides on-site 'Package' for all tasks			
<i>Note: Other risk mitigants such as comprehensive insurance will also be required.</i>			

7 Relevant Parties	
<p>BRANZ</p> <p>Richard Capie Richard.capie@branz.org.nz 027 272 6933</p>	<p>Assist with funding towards opening up better financing for transportable homes as an affordable housing solution, and in turn for large 'chunks' of prebuilt parts of buildings to be financed through traditional mortgage funding, to enable more innovative housing methods to flourish.</p>
<p>PrefabNZ</p> <p>Pamela Bell pam@prefabnz.com 021 972 635 (3 or 4 House builders) Keith Hay Homes Leisurecom Laing Homes Cottages NZ</p>	<p>Understand limit of finance. Check if any partial solutions already exist. Understand how land purchase would fit in with house purchase, eg. timing. Explore changes to contract and their feasibility or otherwise, eg. lower payment before release of house provided buyer has mortgage offer. Confirm assumptions in this paper.</p>
<p>Find Finance</p> <p>Peter McDermott Petermcdermott@xtra.co.nz 027 282 4786</p>	<p>Assist with interpreting needs of housing manufacturers with abilities of banking sector, as conversation mediator and impartial negotiator.</p>
<p>Heavy Haulage Association</p> <p>Jonathan Thompson nzhha@rtfnz.co.nz 027 417 5554</p>	<p>Work with PrefabNZ housing manufacture members to agree assumptions in paper and flexibility on contract lump sum agreements going forward.</p>

<p>Banks (2 or 3 of) ANZ ASB BNZ Westpac Kiwibank TSB Heartland</p>	<p>Understand current policy for new transportable homes. Discuss objectives of PrefabNZ. Identify issues to be resolved to banks' satisfaction. If possible, solve the issues.</p> <p>NB: contacts at Kiwibank (PrefabNZ) and BNZ (HHA) to date</p>
<p>Non-Bank Lenders (4 or 5 of) Finance company (2) Plant and equipment Co. eg UDC Resimac or similar</p>	<p>Find out if a lender will finance the construction/delivery/connection phase until final completion when a bank will provide the mortgage. These meetings could result in a referral to a lender we have not yet identified.</p>
<p>Building Guarantee providers Master Builders Certified Builders CBL Insurance Limited</p>	<p>Understand any limitations of guarantees. Explore possibility of a PrefabNZ 'bespoke' policy that addresses the issues with transportable homes. If successful revert to lenders with counter-proposal.</p>
<p>Government/ Local Government HNZC Large Councils with strong interest in housing issues eg Akld, Wgtn, Chch. Local Govt. NZ Reserve Bank of NZ Cabinet Minister's Offices if necessary MBIE</p>	<p>Subject to existing PrefabNZ work which may already cover this. Ensure policy development recognises funding issues. Explore application of HNZC Welcome Home loan scheme. Explore possibility of Council or Local Govt pilot scheme to bridge finance transportable 'Affordable Homes' until buyers can obtain their mortgage finance. Possibly address Reserve Bank regulation issues if they affect banks' willingness to lend</p>