

EXPLANATORY STATEMENT

Issued by authority of the Treasurer

National Housing Finance and Investment Corporation Act 2018

*National Housing Finance and Investment Corporation Investment Mandate
Direction 2018*

The *National Housing Finance and Investment Corporation Act 2018* (the Act) established the National Housing Finance and Investment Corporation (the NHFIC) to improve housing outcomes for Australians. The NHFIC performs this role by making loans, investments and grants to encourage investment in housing, particularly social or affordable housing.

Under the Act, the Board of the NHFIC is responsible for setting the NHFIC's strategies and policies, and for the proper, efficient and effective performance of the NHFIC's functions.

Section 12 of the Act provides that the Treasurer must make an investment mandate directing the Board in relation to the NHFIC's functions. The Board is subject to the requirements of the Act and the investment mandate.

The NHFIC will make individual investment decisions independently of the Government. The purpose of the investment mandate is to provide a mechanism for the Government to articulate its broad expectations of how the NHFIC invests and is managed by the Board.

The investment mandate provides directions about the two core functions of the NHFIC: the Affordable Housing Bond Aggregator and the National Housing Infrastructure Facility. The investment mandate also authorises the NHFIC to provide support to registered community housing providers to develop their financial and management capabilities.

A combined cap of \$175 million applies to the NHFIC's infrastructure grants and capability building activities. Details of the investment mandate are outlined in the Attachment.

ATTACHMENT

Details of the *National Housing Finance and Investment Corporation Investment Mandate Direction 2018*

Part 1 – Preliminary

Section 1 – Name of the investment mandate

Section 1 provides that the title of the investment mandate is the National Housing Finance and Investment Corporation Investment Mandate Direction 2018.

Section 2 – Commencement

Section 2 provides that the investment mandate commences the day after it is registered.

Section 3 – Authority

Section 3 provides that the investment mandate is made under sub-section 12(1) of the National Housing Finance and Investment Corporation Act 2018 (the Act).

Section 4 – Definitions

Section 4 provides definitions for the terms “AHBA”, “capacity building contract”, “Commercial Financier”, “financing decision”, “financing proposal”, “infrastructure loan, grant or investment”, “minimum target value”, “NHIF”, “Permanent Fund” and “project proponent”. Other terms used in the investment mandate that are defined in the Act (such as “NHFIC” and “registered community housing provider”) take on the meaning given by the Act, as per section 13 of the *Legislation Act 2003*.

Section 5 – Purpose of the investment mandate

Section 5 provides that the purpose of the investment mandate is to give directions to the Board in relation to the operation of the National Housing Finance and Investment Corporation (the NHFIC).

Part 2 – Activities and allocation of funds

Division 1 – The Corporation’s activities

The NHFIC is required to engage in two activities to support investment in Australian housing:

- the establishment and operation of an Affordable Housing Bond Aggregator (AHBA) to provide finance to registered community housing providers by aggregating their lending requirements and issuing bonds to institutional investors; and
- the establishment and operation of the National Housing Infrastructure Facility (NHIF) to provide grants and finance to support the creation of housing-related infrastructure.

The NHFIC is also permitted to engage in capacity building services to support registered community housing providers.

The NHFIC must operate with a commercial approach when making financing decisions. The NHFIC may not spend money, or make loans, investments or grants for any other purpose unless it is incidental to the permitted activities.

Division 2 – Allocation and repayment of funds – AHBA

Divisions 2 and 3 direct the NHFIC in relation to the allocation of money appropriated for it by Parliament.

The Board may allocate up to \$150 million to an initial reserve to support the initial operation of the AHBA. While the AHBA will fund its operation by issuing bonds, it will not be able to issue bonds until there is a sufficient amount of debt available to be aggregated into a bond issuance. Therefore, ability to initially allocate up to \$150 million is available to provide a warehouse facility that extends bridging financing to registered community housing providers until a bond issuance can be made.

The NHFIC must repay the amount allocated to the AHBA plus a margin to reflect the Commonwealth's cost of borrowing to the Government. The NHFIC must make the repayment by 30 June 2023 by which time the NHFIC is expected to have independent financial arrangements in place to support the AHBA.

The adjustment to cover the 'Commonwealth's cost of borrowing' ensures the Commonwealth recoups the real cost of financing the AHBA initial reserve. The same approach is taken in respect of the target rate of return in the Investment Mandate for the Northern Australia Infrastructure Facility. While the term itself is undefined, it is generally understood as requiring a return equivalent to the weighted average issuance yield on government bonds.

Over the long term, the Board must consider recommending the payment of a dividend to the Government under section 49 of the Act if the AHBA substantially exceeds its benchmark rate of return (see Part 3).

Division 3 – Allocation and maintenance of funds – NHIF and capacity building

The Government has committed \$1 billion over five years to the NHIF for the NHFIC to make loans, investments and grants to housing-related infrastructure projects. This funding is to be provided by appropriations made through the Budget process.

Over the medium to the long term, the Board must at a minimum maintain the value of the funds it has used and has available to use to provide infrastructure loans and make investments. To maintain the true value of the funds made available under the NHIF, the NHFIC must also recover the Government's associated costs of borrowing.

The obligation to maintain the value of the NHIF is achieved through a Permanent Fund, which the Board must establish. The Permanent Fund includes the value of the NHFIC's current infrastructure loans and investments under the NHIF, and the funds available to the NHFIC to for this purpose.

The minimum target value of the fund at a particular time is following amount, adjusted to cover the Commonwealth's cost of borrowing:

The amount is the sum of the funds appropriated for the purposes of the NHFIC, less the total value of any:

- funds allocated to the AHBA's initial reserve;
- infrastructure grants made up to that time; and
- capacity building contracts made up to that time.

This minimum target value is used to derive the rate of return that must be applied to individual financing decisions that are provided under the NHIF.

The adjustment to cover the Commonwealth's cost of borrowing ensures the Permanent Fund is maintained in real, rather than nominal terms. As noted above, the same approach is taken in respect of the target rate of return in the Investment Mandate for the Northern Australia Infrastructure Facility. As in the context of the AHBA initial reserve, the Commonwealth's cost of borrowing is generally understood as requiring a return equivalent to the weighted average issuance yield on government bonds.

For the purposes of this investment mandate, the term is applied to the value of the Permanent Fund, rather than as the rate of return for specific financing decisions. This approach provides the Board with appropriate flexibility in determining the rate of return for individual financing decisions and reflects that the Permanent Fund is intended to operate in perpetuity.

Using the sum of appropriations as the starting point identifies the total value of funds that have been provided to the NHFIC. These amounts are reduced by any amounts that have been allocated to the AHBA, reflecting that the AHBA is a different function that is subject to separate repayment conditions. Further, the value of grants and capacity building contracts do not count towards the target value because the NHFIC is not required to recoup the value of these activities, although they are subject to the cap in section 15.

Although the NHFIC's administrative and operational costs are not explicitly referred to in the target value, they must be recouped in order for the minimum target value to be maintained.

A cap of \$175 million applies to the total amount of money the NHFIC can provide in the form of grants and capacity building activities. Of the \$175 million, the NHFIC may allocate up to \$1.5 million to capacity building activities. For example, the NHFIC may issue a total of \$174 million in grants and spend \$1 million on capacity building activities.

Part 3 – The Affordable Housing Bond Aggregator

The AHBA will provide loans to registered community housing providers. A bond aggregator works by sourcing finance in the debt market and on-lending funds to a number of different borrowers for different projects. Aggregating the funding needs of

a number of borrowers into larger debt issuances allows funding to be raised at a lower cost.

In the case of the AHBA, the NHFIC is supported by a government guarantee which further reduces the NHFIC's borrowing costs. Attracting finance through the AHBA in this way will allow registered community housing providers to access more affordable finance on more appropriate terms, and will support the expansion of Australia's affordable housing stock.

The NHFIC may only provide finance to registered community housing providers in the form of secured loans. The NHFIC is required to take security for its loans on commensurate terms to commercial financiers such as banks and other lenders.

Registered community housing providers are registered with State and Territory governments to provide accommodation services for social housing and manage public housing on behalf of those governments. Providers also own their own stock of housing, which they offer to tenants with modest incomes at below-market rents.

In making financing decisions, the NHFIC is required to take a commercial approach, maintain adequate capital reserves, achieve a benchmark rate of return and manage its commercial risks. This ensures the NHFIC fulfils its functions in a prudent and appropriate manner without creating an unnecessary risk of liability for the Government.

The Board must consider a number of commercial matters in making a financing decision under the AHBA. These include the purpose for which the loan is sought, the credit-worthiness of the relevant registered community housing provider, the extent and likelihood of a return on any loan and the associated financing cost. In addition, the Board must have regard to the objects of the Act and must consider the availability of private sector finance to the registered community housing provider and whether the loan would complement other sources of government finance.

The NHFIC's capital reserve target requires the Board to aim to maintain an adequate capital reserve over the medium to long term. This is reflected in the AHBA benchmark rate of return, which the Board must set to cover its financing and operating costs in addition to maintaining the capital reserve. The benchmark rate of return is a minimum target. If the NHFIC's returns substantially exceed the benchmark, it may recommend paying a dividend.

Within six months of the commencement of the investment mandate, the Board must agree to an investment risk evaluation process to assess the risks associated with the AHBA. The Board must advise the Treasurer of this process.

Part 4 – The National Housing Infrastructure Facility

The NHFIC may use the NHIF to provide finance in the form of loans, equity investments and grants to eligible infrastructure projects which support housing development. Examples of housing-related infrastructure include:

- new or upgraded infrastructure for services such as water, sewerage, electricity or transportation; and

- site remediation works including the removal of hazardous waste or contamination.

The NHIF will not finance housing projects directly nor will it finance community infrastructure such as parks or libraries.

The NHIF will support infrastructure projects linked to new housing supply by offering innovative financing options such as equity and blended finance tailored to the needs of projects. In this context, blended finance refers both to the potential for project finance to be provided through a combination of NHIF loans and investments and to the potential for NHIF financing to be structured to complement funding from a consortium of other government or non-government sources.

Tailoring of loans may include a range of concessions, including longer loan tenors, repayment holidays, subordination in debt structures and concessional interest rate margins.

The NHIF will work in partnership with local, State and Territory governments, and registered community housing providers, to support housing-related infrastructure projects. The NHFIC may provide NHIF finance to governments, government corporations and registered community housing providers.

The NHFIC may also provide finance to housing infrastructure special purpose vehicles (SPVs) that have a purpose of undertaking housing-infrastructure enabling projects and have at least one member that is one of the above entities that the NHFIC can provide finance to (the underlying eligible member or members). In this context, the term is intended to cover any entity that has an ownership or participation interest in the SPV (for example, a shareholder if the SPV is a company, or a partner if it is a partnership).

In considering whether to provide finance to an SPV, the NHFIC must consider the extent to which the underlying eligible member or members of the SPV are involved in the proposed project. In this context, involvement has a broad meaning and would require the Board to have regard to the extent of the members' financial involvement, their level of oversight and control, their ability (if any) to appoint directors to the SPV's board, the level of finance they are providing to the project and their role in managing the delivery of the project. None of these types of involvement are determinative and the Board must make financing decisions on a holistic assessment of all prescribed matters and the broader commercial proposal. For example, it is not necessary for the members to have the ability to control the appointment of directors but the NHFIC Board may consider certain levels of involvement to be too low for particular proposals to be appropriate.

The NHIF may only be used to finance projects that can demonstrate 'additionality'. Additionality in this context refers to projects that otherwise would not proceed, or would proceed at a smaller scale or at a later time, without NHIF assistance, and the extent to which NHIF assistance would accelerate or increase housing supply. In addition, the NHFIC must limit any concessions provided under the NHIF to the minimum necessary for an eligible project to be completed in the proposed time.

In making financing decisions in relation to the NHIF, the NHFIC is required to take a commercial approach, achieve a benchmark rate of return and manage its commercial risks.

The Board must consider a number of commercial matters in making a financing decision or providing concessions. These include the eligibility of the project under the investment mandate, the credit-worthiness of any loan recipient and the decision's likely effect on the supply of affordable housing. In addition, the Board must have regard to the objects of the Act and must consider whether the loan would complement other sources of government or private sector finance.

The NHFIC must maintain the value of its infrastructure loans and investments over the medium to long term in line with minimum target value of the NHFIC's Permanent Fund. The Board has flexibility in determining the expected rate of return in relation to any particular financing decision. The Board must therefore ensure that, in aggregate over the medium to long term, the return on these loans and investments is sufficient to cover the NHFIC's financing and operating costs, the value of concessions provided, defaults and other losses, and the Government's borrowing costs.

Within six months of the commencement of the investment mandate, the Board must agree to an investment risk evaluation process to assess the risks associated with the NHIF. The Board must advise the Treasurer of this process.

Part 5 – Capacity building activities

The NHFIC may purchase capacity building services for registered community housing providers. These services can assist registered community housing providers to develop their financial capability and undertake new developments. A cap of \$1.5 million applies to the amount of money the NHFIC can spend on capacity building activities.

The NHFIC will play a central role in sourcing and funding the provision of any capacity building services. In particular, the NHFIC may procure these services from providers such as the Government's AusIndustry service. AusIndustry can utilise its existing infrastructure and networks to provide registered community housing providers with access to experienced business advisers.

Part 6 – Governance

Section 30

Section 30 provides that where it is practicable to do so, the NHFIC should communicate its reasons for making a particular decision to provide finance, or to not provide finance, to the entity that made the related financing proposal.

While this provision does not require the NHFIC to provide such reasons in all circumstances, it nevertheless makes clear the expectation that the NHFIC will, as a matter of good practice, provide applicants with information about its decisions.

Section 31 – Good corporate citizenship

Section 31 provides that the NHFIC must have regard to best practice principles of corporate governance relevant to its role. In particular, the Board must have regard to developing and annually reviewing environmental, social and governance policies.

Section 32 – Transparency of NHIF operations

Section 32 provides that the NHFIC must publish guidance on its website to assist potential applicants to lodge NHIF financing proposals and to ensure the NHFIC's decision-making process is transparent.

Section 32 also requires the NHFIC to publish details of each of decision to make a grant, loan or investment under the NHIF within six months of the decision. This requirement is subject to the NHFIC's obligation to maintain the confidentiality of commercial-in-confidence information.

Section 33 – Reputation

Section 33 provides the NHFIC must not cause damage to the Australian Government's reputation, including its reputation in financial markets.

Section 34 – Approval required if liabilities will exceed \$2 billion

A cap of \$2 billion applies to the amount of Government-guaranteed liabilities. The NHFIC may not increase its guaranteed liabilities in excess of the cap. The Treasurer and the Minister for Finance may approve a higher cap.

The cap is an obligation on the NHFIC and does not operate to directly limit the effect of the Government guarantee. If the NHFIC inadvertently breached the cap without ministerial approval, the debt issued in excess of the cap would still be subject to the guarantee.