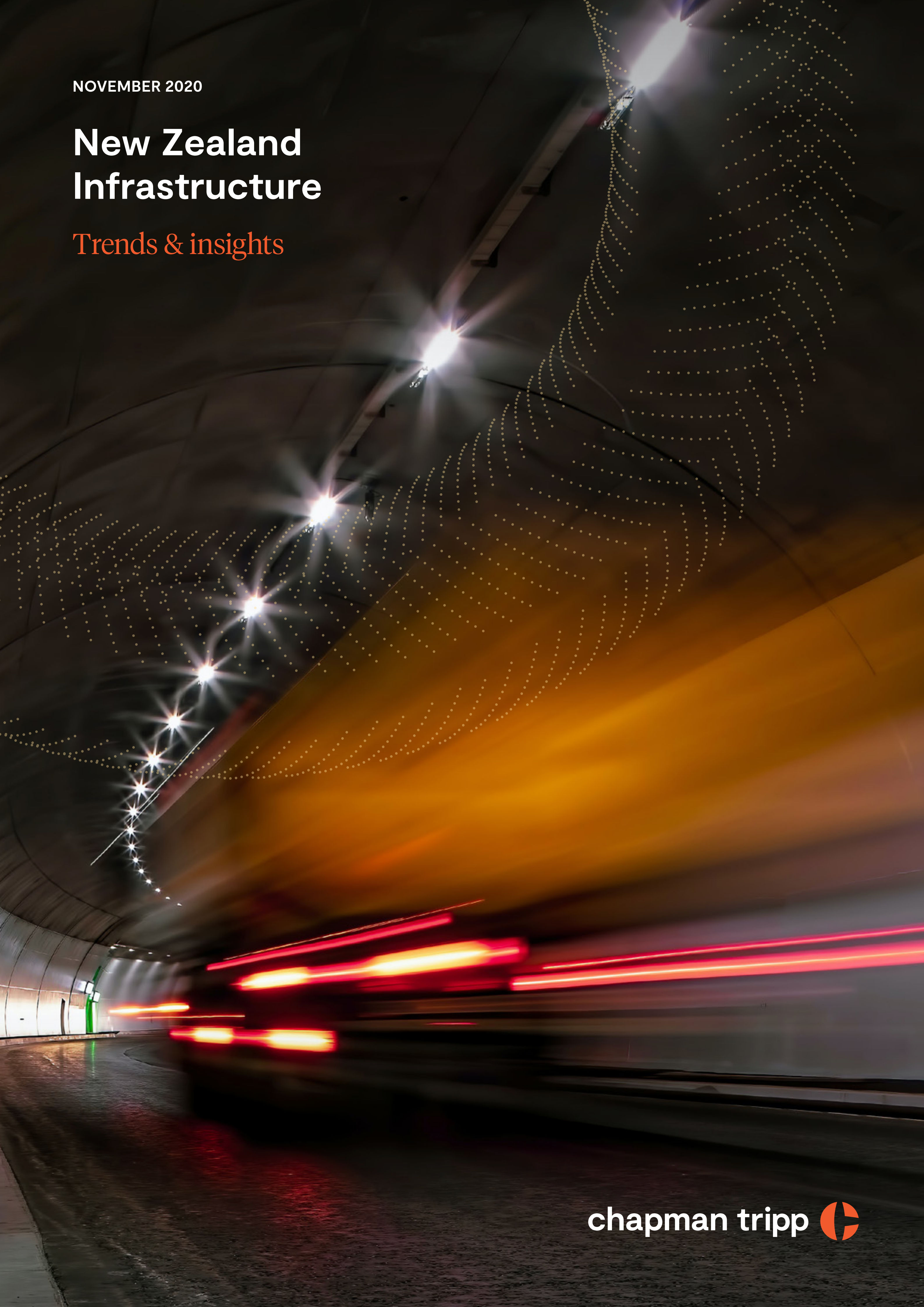
NOVEMBER 2020

# New Zealand Infrastructure

## Trends & insights



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# Contents



# New Zealand infrastructure – ready for lift-off?

Pressure on all forms of infrastructure remains high with little evident physical progress since our publication of August 2018 *What next for infrastructure?* But we may now be about to obtain lift-off.

This is mainly due to the huge infrastructure spend the Government has embarked on as part of its response to the economic impact of COVID-19. However, there has also been significant policy action to address the pinch-points we identified in our 2018 analysis – in particular a channel to attract private sector funding and financing, but also across the broader regulatory framework.

Examples include, but are not limited to:

- the creation of Te Waihanga: Infrastructure Commission to develop a dependable project pipeline
- the establishment of Kāinga Ora, with the power of compulsory acquisition to promote residential development
- the National Policy Statement on Urban Development requiring all councils to provide sufficient land and infrastructure to meet expected population demand
- the three waters package
- the amendments to the Building Act to reduce the barriers to pre-fab construction, and
- the fast track process for shovel ready projects.

As many of these reforms are relatively recent, they have yet to translate into much physical activity – but they will. And there are more changes on the way, most obviously, and most significantly, the repeal and replacement of the Resource Management Act.

This should facilitate timely infrastructure development. Whether it is able to constrain the effects of NIMBY-ism while protecting property rights and democratic rights of participation in resource allocation and decision-making will be a much sterner test.

Climate change will also create a spur for investment, both through its weather effects and increasingly, through the incentives created by the Zero Carbon Act and the Emissions Trading Scheme.

But the size of the job is huge, especially in the electricity sector where Transpower estimates we will need a 55% increase in generation capacity to achieve New Zealand's Paris Agreement commitment to net carbon neutrality by 2050. In our view, it will take a paradigm shift to pull this off.

And, although COVID-19 has opened the Government's cash faucet, the border restrictions are exacerbating New Zealand's persistent skills shortages and the COVID-induced recession has put many businesses into retrenchment mode.

So, while there are many reasons to believe that New Zealand's decades-long pattern of under-investment in infrastructure may be about to end, delivery to the levels required to spark a meaningful improvement in productivity, social wellbeing or emissions reduction is still far from guaranteed.



**Paula Brosnahan**
Partner


**Mark Reese**
Partner


> "Although COVID-19 has opened the Government's cash faucet, the border restrictions are exacerbating New Zealand's persistent skills shortages"

# Wild ride ahead for electricity sector

## Within weeks of Rio Tinto's announcement that it would close the Tiwai Point smelter by August next year, Transpower put out a paper updating its central planning scenario for New Zealand's energy future.

The modelling assumes that to meet New Zealand's commitment to be net carbon zero by 2050, electricity demand will be pushed up by 55% – which will require the construction of 25 new grid-scale renewable power stations and battery storage schemes within the next 15 years.

That is a frighteningly short timespan given the levels of investment that would be involved, the long lead times associated with large infrastructure projects, and the uncertainties around trying to predict movements in wholesale electricity prices.

It was in recognition of these factors that Transpower shot out its publication. It created a context to guide investment decisions and to mobilise a collective action response.

This included an assurance to potential investors that Transpower will do its bit to expand capacity in the national grid. The Clutha to Upper Waitaki Lines project is already underway and it will consult on further upgrades and expansions.

Meanwhile, Contact Energy has put a new geothermal power station at Tauhara on hold and Meridian Energy has deferred the Harapaki wind farm in the Hawke's Bay pending a final decision about the smelter's close date.

### Towards a more positive investment environment

The Labour Government has committed to replacing the Resource Management Act (RMA) along the lines recommended by the Randerson report (see our discussion on page 11), which include moving to an outcomes based approach rather than focusing on effects.

The Labour-Green Co-operation Agreement also commits both parties to achieving the purpose and goals of the Zero Carbon Act through decarbonising public transport and the public sector, increasing the uptake of zero-emission vehicles and supporting the use of renewable energy for industrial heat. In short, strengthening the commitment to stimulate material increases in demand for electricity.

In the meantime, acting on recommendations from the Productivity Commission and the Interim Climate Change Committee (ICCC), the Government is exploring ways to provide more direction to consenting authorities, including through amendments to the National Policy Statement (NPS) for renewable electricity generation.

And it is trying to broker a cheap power deal to entice Rio Tinto to maintain current employment at the Southland site over the next three to five years and to work with the Government on finding future uses for the plant.

**But...**

Working against these positives are major uncertainties that may deter the private sector from making the necessary investments at the required volume and velocity.

Even if Rio Tinto is persuaded to delay its departure, it will be a reprieve rather than a rescue, and there are currently question marks over a number of other major power users, among them the New Zealand Oil Refinery at Marsden Point, the Tasman Mill at Kawerau, New Zealand Steel's Glenbrook Mill, the methanol production facilities at Taranaki, and the James Hardie cement factory at Penrose.

The Government has compounded this uncertainty by advancing its 100% renewable electricity target from 2035 to 2030. It did this against the advice of both the Productivity Commission and the ICCC.

- The Productivity Commission advised in August 2018 that "no options exist to completely eliminate greenhouse gas emissions from electricity generation without greatly increasing wholesale electricity prices".
- And the ICCC advised in 2019 that, while technically feasible, the last few percentage points would be very expensive to achieve – pushing up residential power prices by 14% and industrial prices by 39% – which would slow the decarbonisation of the rest of the economy.

Labour has linked the 100% goal to the use of pumped hydro, in particular through a huge facility at Lake Onslow in Central Otago, although Energy and Resources Minister Megan Woods says other smaller options in the North Island will also be investigated.

But the Lake Onslow proposal would take four to five years to complete and a further two to fill the reservoir, would be eye-wateringly expensive to build (at least $4b and probably closer to $6b), and would have wafer thin profit margins. The Government has only committed $100m for a detailed business case.

And, even if the project proceeds, it will take many years for the design detail to be finalised so that the market knows exactly what is proposed. How would it operate? As well as providing dry year supply, would it also intervene to smooth price peaks in a more usual year? If so, when? And how would that not crowd out other generation investment?

Would you advise your board to approve a major construction project for new generation while all these balls were still up in the air?

### How to achieve the necessary paradigm shift

These questions underscore the fact that we have a market model in New Zealand which is geared to incremental change. So, to power a massive increase in electrification, a paradigm shift will be needed.

Historically it is the state that builds generation – even in large economies like the UK where the Government has contracted China General Nuclear Power Group to develop a new nuclear plant, and has absorbed the economic risk by locking in a long-term pricing curve.

In New Zealand, the Government owns Transpower and holds a majority stake in three of the four major gen-tailers: Genesis Energy, Mercury Energy and Meridian Energy. But the 49% private shareholding in these companies will restrain the Government's ability to strong-arm them into making major investment decisions.

Will that mean acting as under-writer to the private sector or entering Public Private Partnerships? Or will the Government incentivise private investment through a sky high Emissions Trading Scheme – and how would that affect low income earners or the broader economy.

These are the issues which the Government and the energy sector will need to work through in the current term. Transpower has laid out a path. Everyone else now needs to chart a course.

**Andy Nicholls**
Partner

SECTOR HOT SPOTS:

# Three waters

## The 2016 Havelock North drinking water contamination has catalysed significant reform to the country's three waters infrastructure.

This will be administered by Taumata Arowai – a Crown agent created by statute this year to regulate the provision of drinking water, and to oversee wastewater and stormwater services across the country.

To address persistent structural problems of council fragmentation and under-capacity, the Government is dangling a $630m carrot for distribution as grants to councils which agree to amalgamate their three waters infrastructure with others in the region. The allocations range from Canterbury on $100m to Gisborne on $11.04m.

Participating councils will receive 50% of their allocation directly. The remaining 50% will be assigned to the regional grouping, members of which must sign a Memorandum of Understanding that commits them to develop and enter into service delivery entities:

- of a scale that will enable benefits from aggregation to be achieved over the medium-to-long term
- with balance sheet separation to support improved access to capital, and
- with competency-based boards.

This is deft politics which achieves territorial amalgamation without buying into parochial turf disputes. As Infrastructure Commission Chief Executive Ross Copland says:

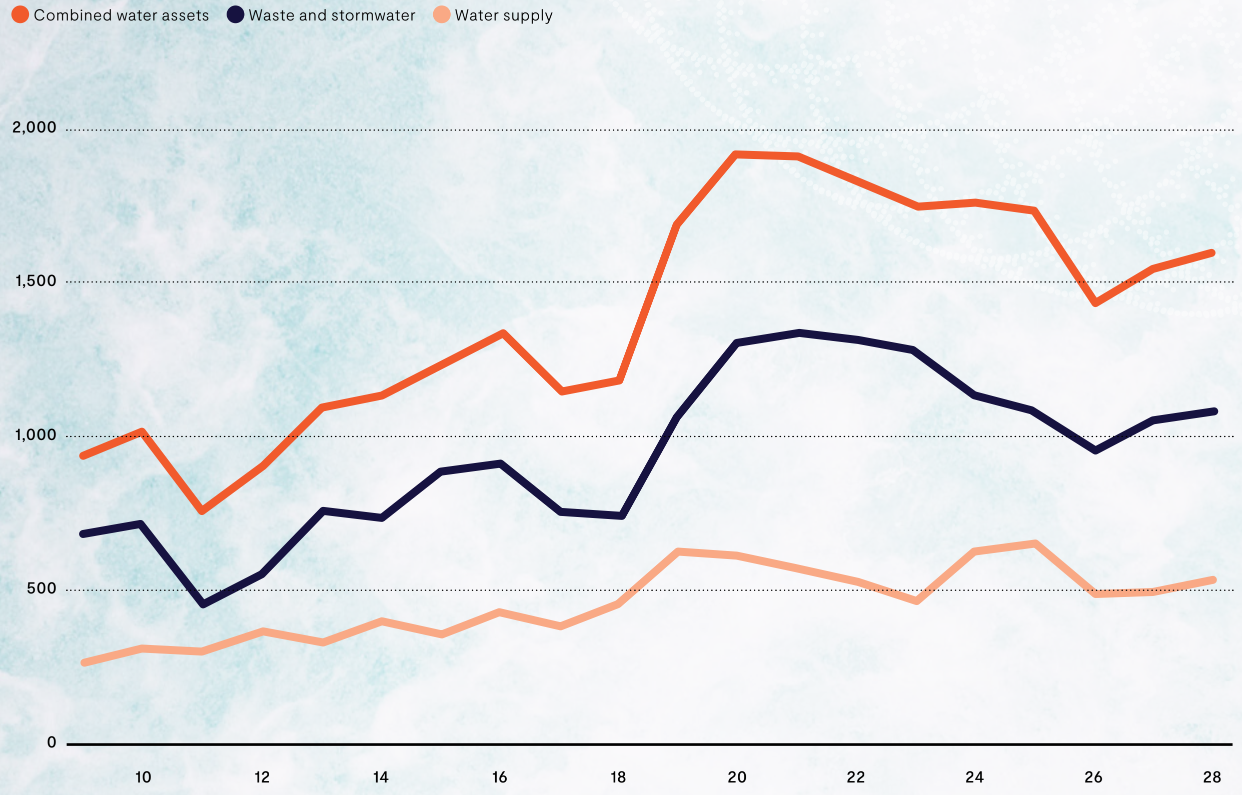
"The decision to focus this investment on Councils who commit to work with the Government on three waters reform is a pragmatic, incentive-based approach to unlocking the procurement and operational efficiencies which can be gained through consolidation".

Local government forecasts have investment reaching $17.2b over the next 10 years, which is an increase in numerical terms of 60% over the previous decade.

> And yet, Infometrics considers this may not be enough to meet the costs of previous depreciation, population growth, urban densification and higher water standards.

## Investment in New Zealand water assets set to rise

$m, historical and forecast capital investment in water assets




Source: Infometrics

> “The decision to focus this investment on Councils who commit to work with the Government on three waters reform is a pragmatic, incentive-based approach to unlocking the procurement and operational efficiencies which can be gained through consolidation.”

SECTOR HOT SPOTS:

# Social infrastructure

## In our 2018 publication we said that New Zealand's social infrastructure – public housing, schools, hospitals, prisons etc – was in poor shape because it had played Cinderella to debt reduction for decades.

In this metaphor, the debt mountain created by the Muldoon Government's borrowing binge through the mid-1970s to the mid-1980s becomes the wicked stepmother with the GFC in 2007 and the Canterbury earthquakes in 2010 and 2011 playing the two ugly sisters. Now we have COVID-19 which, in this narrow context, is in the role of Fairy Godmother because it has released large amounts of cash for infrastructure spending.

The Government's 'wellbeing approach' has also loosened the purse strings. And the shift to a rolling four-year budget capital allowance (from single year allowances) should provide more investment certainty – although this effect should not be over-stated as budget decisions are always vulnerable to changes in the fiscal position or in the balance of political power.

The first four-year allocation, made in 2019, was for $10.4b. At Budget 2020, $4.4b was still in the kitty. The Government increased this by $1.7b, taking it to $14.8b, and committed to a further $8b capital expenditure in the current financial year.

The priority areas for capital investment over the last three budgets have been health around $3.5b; and education around $2b.

So loads of dosh sloshing around but so far, not much to show for it on the ground. This is not surprising given the long lead times associated with construction projects, but it is a source of some frustration.

The public health sector in particular is struggling against tight budgets and tired infrastructure with large project pipelines and inconsistent procurement. Structural reform is coming through the Heather Simpson-led health and disability system review. But the pressure on the Government's balance sheet will constrain both the scope and the pace of change.

The area of greatest achievement is probably in social housing where, according to the Government's Housing Dashboard, between June 2018 and 30 September 2020, 7,378 state and community houses had been either built or were under construction. Labour is committed to increasing this to 18,000 by 2024.

And yet this will not be enough to accommodate the current waiting list which is at record heights with around 20,000 applicants.

**Capital investment – education**

# $2b

**Capital investment – health**

# $3.5b

**Between June 2018 and 31 August 2020**

# 7,313

houses built
or under
construction.

**At Budget 2020**

# $14.8b

# $8b

capital expenditure in the current financial year.

SECTOR HOT SPOTS:

# Transport

## Transport in all its forms has been a big beneficiary of COVID-19 and the 2020 general elections. COVID-19 because of the need to stimulate job-heavy investment, the election campaign because Labour and National see new roads as vote-winners (the Greens, not so much).

The Government Policy Statement (GPS) for 2021, released on 17 September, provides for $48b of transport spending over the next decade, $10b of which will be spent on driving down the road toll. The $48b is on top of the $6.8b already allocated to the New Zealand Upgrade Programme, across road, rail, public transport, walkways and cycle ways.

These large numbers carry their own kind of comfort, especially in a sector which has the benefit of coordinated, mode neutral planning by Waka Kotahi NZ Transport Agency.

> And yet the two hero projects – Transmission Gully in Wellington and Auckland Light Rail – have been beset with difficulty. But easier times may be ahead.

The Auckland Light Rail tender process was officially pulled in June this year because of opposition from New Zealand First, but should get the green light now that Labour's got a clear majority and is in control of its own destiny.

And the current review by the Infrastructure Commission into the Transmission Gully Public Private Partnership (PPP) may create an opportunity to reset the contract terms to the benefit of both parties.

SECTOR HOT SPOTS:

# Housing

## KiwiBuild was set up for failure by the impossibly ambitious 100,000 new homes within 10 years target. As at 30 September 2020, the Housing Dashboard had just 645 completed and another 912 under construction.

But much has been done at the policy level to unblock some of the blockages in the system, in particular:

- the creation of urban development authority Kāinga Ora, with the power to compulsorily acquire land and to fast track developments
- changes to the Building Act to reduce the barriers to pre-fab construction
- the NPS on Urban Development, requiring all councils to provide sufficient land and infrastructure to meet expected demand over the short, medium and long term, and imposing specific density requirements on the five highest growth areas – Auckland, Hamilton, Tauranga, Wellington and Christchurch, and
- the Infrastructure Funding and Financing Act giving local authorities access to off-balance sheet finance.

Most of these only came into effect in the second half of this year so have yet to register an impact. But they can only improve housing availability and affordability at the margins because – like all markets – the housing market is governed by the laws of supply and demand, and the facts are brutal.

## Housing (continued)

**Fact One**

New Zealand population grew by

17%

2010 to 2020

**Fact Two**

over this period, housing stock increased

12.5%

**Fact Three**

That creates a shortfall of

74,000

– half of it in Auckland.

**Median house price**

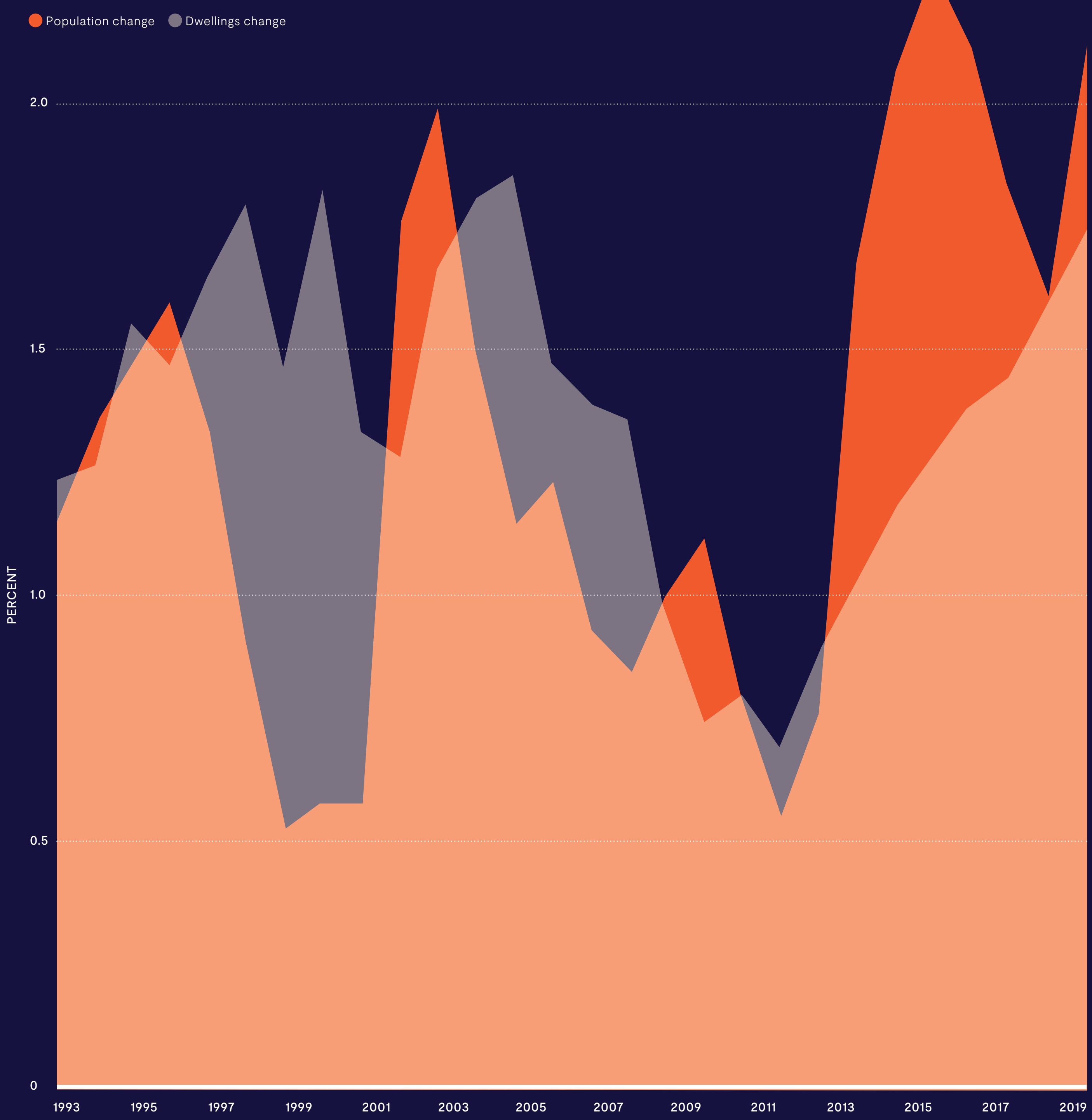
19.8%

year to October. Now

$725,000

## Population vs housing stock

Annual change in resident population and private dwellings (estimates)




Source: Stats NZ

# The RMA – what next and how long?

It all seems very promising. We have a general acceptance that the Resource Management Act (RMA) has done its dash, an expert panel report that has broad support across the political spectrum, a Government with a clear majority and, in David Parker, a Minister with a proven record in managing complex reform processes.

Parker is confident in his mandate and has confirmed his commitment to implement the Randerson Panel package within this three year term.

The Panel has recommended that the RMA be replaced by three separate Acts: a Natural and Built Environment Act (*NBEA*), a Strategic Planning Act (*SPA*), and a Managed Retreat and Climate Change Adaptation Act and that:

- the number of local government resource management plans should be drastically reduced to one per region (which would bring it down to 14 from more than 100 currently), and
- there should be more national direction to better protect environmental bottom lines for biodiversity and ecosystems, and to enable urban development.

At the time this publication was released, however, we were still waiting for detail on the reform timeline.

**Good process will be essential**

Replacing the RMA with a framework that will be workable and durable will require huge amounts of consultation, patience and skill – especially as it is extremely unlikely that the consensus around the RMA's repeal will carry over into a consensus around the RMA's replacement.

It will not be a simple matter of implementing the Randerson review as many of the review's recommendations give considerable room for interpretation and creative licence so would need to be developed and refined before they could be translated into law. They are also not universally agreed.

It is worth remembering that the RMA was largely developed under the Fourth Labour Government and was passed by the Fourth National Government. Yet despite this bi-partisan inception, it has been through 18 rounds of amendments since its passage in 1991 – a frequency rate of more than one every two years.

**Tensions will remain**

The job of the RMA, and of whatever replaces it, is to weigh competing interests – economic development against environmental protection, regulation in the public interest against private property rights, new housing against an environmentally significant wetland, network infrastructure against outstanding natural landscapes.

It controls almost all decision-making relating to the way we manage the use of land, air and water – from major new motorways to whether you can add a second storey to your home. These tensions cannot be legislated away – a point the Parliamentary Commissioner for the Environment, Simon Upton, made recently, saying:

> "I must warn that statutory spring cleaning is not going to lead to peace, harmony and goodwill towards planners. Some of the conflicts that are giving rise to current dissatisfaction are eternal and will persist no matter what statutory framework is enacted."

Minister Parker echoed this sentiment last week, saying the RMA shouldn't be blamed for the "ills of society".

The fact that often neither party is entirely satisfied with an RMA outcome may mean that an appropriate accommodation has been found.

This is not to suggest that the balance between development and protection cannot be struck more efficiently and with greater public confidence, but to walk into this exercise expecting to secure your full wish list of resource management outcomes is to set yourself up for disappointment.

**RMA as scapegoat**

The RMA has been endlessly tinkered with over its 30 year history, gaining more pages and losing a little more coherence with each amendment. Over that same period, the population has increased by almost two thirds, house prices have gone stratospheric, agricultural land uses have intensified, and we are starting to bump up against severe resource and infrastructure constraints.

Whether the RMA, properly administered and enforced, could have managed or prevented these outcomes we will never know because it was never really given a serious shot at success.

The intention was that it would be reinforced by NPSs and National Environmental Standards (*NES*) but these were slow to develop. The first NPS came into effect 17 years after the RMA came into force, and the first NES, 13 years after.

Central government could also have done a lot more, carrot and stick, to improve the administration and enforcement of the RMA at the local level.

However, this is all academic now. The fact is that, fairly or not, the RMA is now widely perceived as a failure. Here's Minister Parker on why reform is needed:

> "The RMA has doubled in size from its original length. It has become too costly, takes too long, and has not adequately protected the environment. There are significant pressures on both the natural and built environments that need to be addressed urgently. Urban areas are struggling to keep pace with population growth and the need for affordable housing. Water quality is deteriorating, biodiversity is diminishing and there is an urgent need to reduce carbon emissions and to adapt to climate change."

**Our view**

The Ministry for the Environment will be tasked with dividing the reform into manageable parts. Our strong view is that the proposed NBEA and the SPA should be developed and progressed in tandem. The Managed Retreat and Climate Change Adaptation Act could be dealt with separately to reflect its more specific subject matter, and the inherent property law and fiscal complications it presents.

We expect that aspects of the recently passed COVID-19 Recovery (Fast-track Consenting) Act will be transferred across to the NBEA – in particular the more stringent Treaty of Waitangi tests and the 'consistency with national policy statements' test.

We also expect that the place of environmental 'bottom lines' will be a key issue, with contrasting positions already being advocated by the Chair of the Panel Review, Justice Randerson, and the Parliamentary Commissioner for the Environment, Simon Upton.

Resource management is a complex business. Even if all the experts agreed on the end objectives, they could still have quite sharp differences of opinion on how best to deliver those objectives.

Already we have subtly different models from the Randerson Panel and the Environmental Defence Society, and a significantly different model from Simon Upton, who considers that the improvements sought by the Panel could be "easily dealt with within a recast RMA".

For these reasons, there may be value in circulating exposure drafts of the NBEA and the SPA before proceeding to the Bill stage. This would allow a further opportunity for public input, and it is important that there are as many opportunities for public and stakeholder engagement as possible.

**Take-outs**

The regime that replaces the RMA will reach across business and the economy, influencing what is possible in the infrastructure space and the compliance costs associated with new developments.

The earlier you engage the better as it is easier to influence the direction and content of reform before policy design decisions are taken and before momentum builds in a particular direction.

It is essential that the Government and the infrastructure sector engage constructively to avoid RMA reform having a stifling effect on infrastructure projects, which form the bedrock of New Zealand's COVID-19 recovery.

So now is the time to start thinking about what the problems are that we need to fix, and how that might be achieved. You might also consider joining forces with others who share your interests or perspective to provide a strong coherent voice.

**Paula Brosnahan**
Partner

# Coasting on a COVID cash bonanza

## The funding and financing issue we identified in our 2018 infrastructure report was how to access private capital in an environment where central government was focused on paying down debt and councils were constrained in how much borrowing they could carry on their balance sheets.

In particular, we argued the need for "a robust and replicable transaction structure to match the vast resources of pension and sovereign wealth funds to the demand for infrastructure projects". A large step in this direction has now been delivered through the Infrastructure Funding and Financing Act 2020, although it only passed in August and no transactions have yet been completed under it.

There is still an enormous amount of money under institutional management around the globe which is on the hunt for long-haul investments offering secure returns in politically stable countries, like New Zealand.

What's changed is that those funding sources are now in competition with the huge amounts of cash released by the Government directly, and to a lesser degree, by the Reserve Bank of New Zealand (RBNZ) indirectly, to support the economy through the COVID crisis.

We offer a quick overview of the market dynamics currently in play and the various funding options available.

### Equity

Sovereign funds, including the New Zealand Superannuation Fund and ACC, and insurance companies and managed funds, are on the look-out for infrastructure assets which can deliver relatively certain income streams that match the relevant investor's investment profile. The NZ Super Fund's unsolicited bid with CDPQ Infra to deliver the Auckland Light Rail project is a high profile case in point.

To facilitate private sector investment in infrastructure, there needs to be a well understood and replicable framework.

The PPP was used for numerous projects throughout 2012-2017 but has been less available since due to Labour's objection to using PPPs for social infrastructure projects and to the issues which have affected Transmission Gully.

A revised PPP model and a pathfinder IFF transaction should be prioritised to provide investors with confidence about the opportunities for investment.

Risk allocation will need to reflect the risk appetite of different investors:

- sovereign funds may be prepared to take a long term NZ Inc view and invest in both the construction and operational phases of a project, but

- private capital is typically more cautious about taking on construction risk and may prefer to wait until the asset is in the operational phase, depending on the nature of the asset involved and the way in which those risks are managed.

### *COVID and private infrastructure investment*

While infrastructure assets have historically offered a 'safe' investment, in the post-COVID world other asset classes, like health care, may offer a safer and more profitable investment opportunity.

In particular, we expect that equity investors will not readily be prepared to accept revenue models based on demand without significant compensation through cost of capital, and will instead look for those based on availability with stronger protection in the event of Force Majeure.

There is also a risk that international capital (and debt and contractor resources) will be in simultaneous demand across multiple jurisdictions as all governments look to kick start their economies – the obvious case in point being our friends across the ditch.

New Zealand may be less attractive due to our remoteness and lack of scale, and the Government may need to do something special to counter-balance this. The de-politicisation of the future project pipeline represented by Te Waihanga: Infrastructure Commission is important to attract this capital.

Other inducements could include:

- a revised set of risk allocations that make it easier to price, transact and trade equity participations in New Zealand, and
- agreed transaction modes and alliance/partnering models to encourage and support long term presence and investment.

### Debt

As financial markets start to factor in the prospect of negative interest rates, bank debt is cheap (in nominal terms) and looking for a home – which should support infrastructure investment.

But this stimulatory effect is being blunted by the higher capital requirements that the RBNZ is also bringing in. Aware of the policy clash, the RBNZ has deferred implementation of the new capital adequacy rules until 1 July 2022.

### Government funding

Labour's fiscal plan, released during the election campaign, anticipates borrowing $42b over the next four years for infrastructure spending. This is on top of the $12b New Zealand Upgrade Programme, announced on 29 January, which signified a new (pre-COVID) willingness by Finance Minister Grant Robertson to relax his debt reduction target in order to take advantage of historically low global interest rates.

In addition, Kāinga Ora has borrowed $5b to fund the construction of 8,000 public houses over the next four to five years, and $48b has been allocated to the Waka Kotahi NZ Transport Agency through the GPS on land transport 2021.

***A caution*** – Government funding is cheaper and can be easier to access than commercial bank lending but there are reasons why bank lending should be encouraged. Banks have a number of practices in place which put controls around a project in order to ensure that it is delivered on time and on budget, and with a clear allocation of risk.

Direct government funding can support an infrastructure project in full or alongside other financing mechanisms.

***Grants***

Most of the $3b assigned to the Infrastructure Reference Group's "shovel ready" projects, and some of the disbursements from the Provincial Growth Fund, have been advanced as grants which are repayable in limited circumstances.

The objective is speed, which was a key driver for the "shovel ready" projects. Legal documentation is simpler and financial due diligence is more limited, meaning funds can be advanced faster.

***Loans***

In some cases, the Government has chosen to advance funds by way of debt – often on terms that are more attractive than bank lending, and sometimes because the banks were unwilling to lend.

This practice has evolved out of the Provincial Growth Fund and has very much been a feature of the COVID intervention. Our view is that it will be replaced by more conventional funding options once some form of normalcy returns and the focus switches to chiselling back the COVID-created debt mountain.

Regardless, a lot of the loans that have been advanced by departments and crown entities are on terms of five to 10 years and the Government will need to monitor, and potentially restructure some of, this lending.

**Infrastructure Funding and Financing Act (IFFA)**

The IFFA is targeted to the local government sector, where the ability to borrow is limited by debt constraints, and is expected to be taken up by councils in high growth areas.

It creates a multi-year levy on the beneficiaries of infrastructure assets which is paid to a Special Purpose Vehicle (SPV) so that the development costs are appropriately allocated to the people who will most benefit from the investment.

As the asset will generate revenue via the levy, borrowing can be undertaken on the strength of the levy.

While the IFFA is silent on this point, our understanding is that the Government will likely provide a government support package to facilitate access to the debt capital markets (and to perhaps cover other 'tail risks'), in line with similar transactions overseas.

**Private Public Partnerships (PPPs)**

The Level 4 lockdown created all sorts of problems for the construction sector – not just closing sites but disrupting procurement lines and relationships with sub-contractors. For the Transmission Gully PPP, which was already behind deadline, it just compounded some already existing issues.

The review by the Infrastructure Commission should offer some valuable lessons and a chance (if needed) to put the project on to a firmer footing by resetting the governance and structuring arrangements and the risk allocation.

PPPs tend to be high profile because of their public sector element, and can be controversial with those segments of the population who are opposed to any form of privatisation. However, they provide a format to attract private capital and commercial disciplines to public enterprise, and to share risk.

A recent evolution of the PPP market in New Zealand is the PPP for the Auckland South Corrections Facility, which was developed by an SPV (with three equity investors) through the construction and operational stages under contract to the Department of Corrections.

InfraRed sold a 40% equity stake in the SPV to AMP Capital in January this year and John Laing sold a 30% equity stake in the SPV to AMP Capital in the months following – pioneering the development of an active secondary PPP market in New Zealand.

**Mark Reese**
Partner

# Climate change – the elephant in the room gets bigger

## From the perspective of 2030, assuming effective vaccine distribution, COVID-19 will be fading from the collective consciousness, but climate change will be a clearer and ever more present danger.

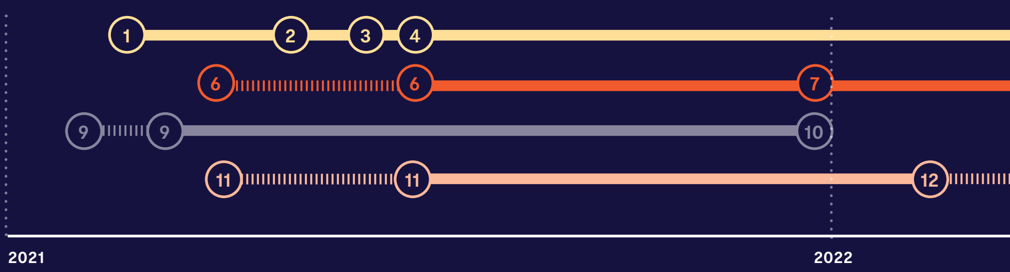
The physical disruption effects on infrastructure will be large, with $14b in local government assets alone at risk from sea level rise. But there will also be opportunities, both in the development of replacement infrastructure and in harnessing new technologies to improve existing asset resilience.

New Zealand has significantly strengthened its institutional and structural climate change response in the last 12 months through:

- the passage of the Zero Carbon Amendment Act (*ZCAA*) which introduces binding long term emissions reduction targets reinforced by "stepping-stone" emissions budgets and ongoing mitigation and adaptation plans
- reforms to the Emissions Trading Scheme (*ETS*) which change how emission units are priced and supplied and provide a backstop date for the inclusion of agriculture in a carbon pricing system, and
- provision in the RMA for greenhouse gas emissions to be considered in resource consenting and for planning decisions to link back to ZCAA policy documents.

Although much of the impact from these changes is yet to be felt in the infrastructure sector, the initial ripples are evident. Climate change is (and should be) on the board agenda of most infrastructure owners and operators, insurers are already building in climate risk to the price of policies, and emission unit prices have skyrocketed (up 40% on this time last year).

To assist with this task, the following timeline picks out the key known and anticipated events over the Government's next term:




- Key ETS Events
- Key RMA Events
- Key ZCAA Events
- Other relevant climate change events

1. **17 Mar 2021**
ETS: First NZUs auction

2. **31 May 2021**
ETS: Final surrender round with $35 fixed price option available

3. **23 Jun 2021**
First NZU auction - subsequent auctions scheduled for June, September and December 2021

4. **30 Jun 2021**
Climate Change Commission to advise the Minister on progress towards farm level obligations

5. **31 Dec 2022**
Ministerial report due on a system to put a price on emissions from agricultural activities as an alternative to joining the ETS

And that is not the end of it. The Government's climate change reform agenda will continue throughout this term, including:

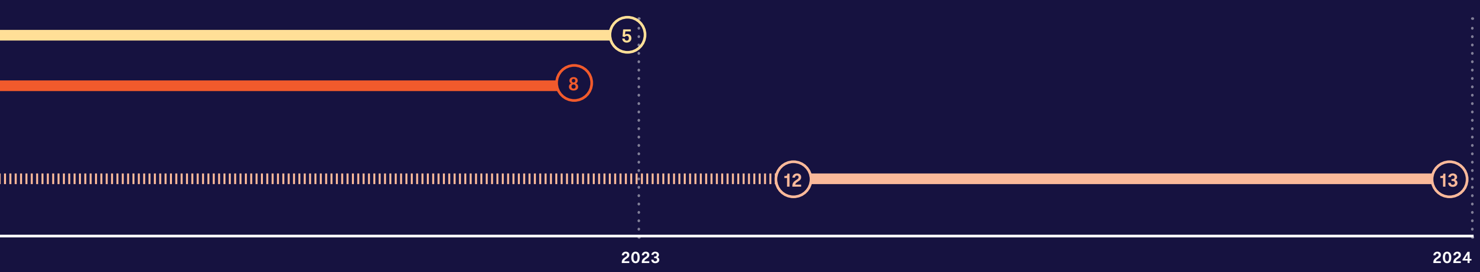
- a major focus on achieving near term emission reductions through the setting of emissions budgets supported by a national emissions reduction plan (Minister Shaw told a conference last week that he is "absolutely committed to following the advice of the Commission" and that he expects the country's first carbon budgets will be "pretty shocking to a lot of people")
- mandatory climate-related financial disclosures for all NZX-listed companies and most large fund managers and financial and insurance entities
- direct government intervention through infrastructure investments to speed the transition to a low carbon economy – e.g., Auckland Light Rail, hydrogen fuel infrastructure, and (depending on the business case analysis) the Lake Onslow pumped hydro project
- the development of a National Direction under the RMA that enables regional and district plans to more proactively and directly manage emission-intensive activities
- anticipated legislation enabling the forced retreat of buildings and assets from climate change affected areas (i.e. affected by anticipated sea level rise and flooding and fire risk), with the potential for compensation. This has been recommended as part of the overhaul of the RMA, although it is likely to be a longer term prospect given the inherent complexities and competing values, and
- the impending regulation of embodied emissions in building materials – the initial Ministry of Business, Innovation and Employment (MBIE) consultation paper relates only to new buildings but there are obvious parallels for infrastructure projects.

As this river of reform flows into existing large work streams to implement 2019/20 climate change reforms, the challenge for the infrastructure sector will be identifying:

- where the real risks/opportunities lie, and
- how engagement and watching brief efforts can be targeted to achieve business drivers within COVID-19 balance sheet restrictions.

The timeline below traces key events for the next three years (to the end of 2023).


**Alana Lampitt**
Senior Associate


6 **Early - mid 2021**
Proposed RMA National Direction on greenhouse gas (GHG) emissions anticipated to be consulted on
***Opportunity to engage**

7 **31 Dec 2021**
Earliest date that GHG emissions become relevant to RMA planning and consenting decisions

8 **30 Nov 2022**
Latest date that GHG emissions will be relevant considerations in RMA planning and consenting decisions

9 **February - 14 March 2021**
- Climate Change Commission's first package of advice to the Government open for consultation. Will cover:
- emission budgets 2022 - 2035
- emission reduction plans the agricultural emissions target
- NZ's Paris Agreement target

10 **31 Dec 2021**
Goverment must have an emission reduction plan and emissions budgets for 2022 - 2035 in place

11 **Early - mid 2021**
Consultation expected on draft legislation on climate-related financial disclosures for listed and financial entities

12 **FY 2022/2023**
Obligations on climate-related financial disclosures expected to commence.

13 **By end of 2023**
First Paris Agreement global stocktake

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