

Main findings and opinions of the National Audit Office

Cyclical renovation grant scheme

In 2008, as the Finnish economy was slowing down, the government decided to introduce an extensive stimulus package, which was partially intended to boost the construction of new buildings and renovation. The aim was to maintain and improve employment in the construction sector. There were a number of stimulus measures supporting the construction sector and one of them was the renovation grant scheme intended for housing corporations (cyclical grant scheme).

Under the government proposal HE 2/2009 vp, the aim of the cyclical grant scheme was to stimulate construction activities and provide more job opportunities in the construction sector. The aim was also to start essential renovation and repair projects so that the quality of Finland's housing stock could be maintained and improved.

The main issue examined in the audit was based on the objectives laid out for the cyclical grant scheme and the aim was to find the answer to the following question: *Was the cyclical grant scheme a successful and appropriate instrument to stimulate the construction sector and to maintain and improve the quality of the building stock?*

The scheme, which was originally planned to be of short duration, was extended twice. Cyclical grants were provided in two different forms in 2009 - 2010: All renovations and repairs carried out by housing corporations that were estimated to cost more than 5,000 euros were entitled to a cyclical grant covering 10 per cent of the expenses. Measures promoting energy efficiency were entitled to a cyclical grant covering 15 per cent of the project costs. The measures entitled to energy-efficiency grants were specified in a government decree.

Providing the grants was primarily the responsibility of the municipalities while the grants for municipalities and joint municipal authorities were provided by the Housing Finance and Development Centre of Finland (ARA). ARA also decided on the grant authorisations and paid the grants to the municipalities and it steered and supervised the activities of the municipalities. A total of 259.9 million euros in cyclical grants was paid. Grants were paid from the state budget and from the National Housing Fund, which is an off-budget fund.

The cyclical grant scheme helped to boost renovations by housing corporations and had a positive effect on employment in the construction sector and on the quality of the housing stock

The audit findings suggest that the cyclical grant scheme had its biggest effect on the implementation of already planned or prepared renovation projects. The scheme provided housing corporations (mainly housing companies) with an incentive to bring forward and speed up already planned renovation projects. The scheme helped to boost demand for renovation.

The cyclical grant scheme helped to speed up the decision-making process in housing companies by prompting them to start renovation projects that had already been under planning and preparation for some time. However, few renovation projects could be started 'from scratch' as the grant scheme was only in effect for a short period. In fact, the audit findings indicate that more consideration should have been given to the renovation process in housing corporations.

Even though the cyclical grant scheme increased demand for renovation, it is impossible to determine the overall sectoral employment impact of the scheme, which was intended as a stimulus measure. This is because there is not enough statistical information available. The employment effects of the scheme presented in the statistics are calculative, which means that they do not give the actual employment impacts of the measure. The statistics on employment in the construction sector are not detailed enough to allow us to determine the effects of the cyclical grant scheme on employment in the construction sector and the number of foreign companies and employees.

Thus, the National Audit Office is of the view that it is not practical to create the misleading impression that central government knows the actual employment impact of the scheme.

The cyclical grant scheme did not support long-term renovation in housing companies

The strategy for renovation 2007-2017 already existed when the scheme was launched. Thus, it would have been logical that the measures taken in response to the stimulus needs had also been in accordance with the strategy and promoted systematic and long-term maintenance and renovation culture. However, the audit findings suggest that this was not the case. From the perspective of the acceptability and performance of the

tools used to stimulate the construction sector, it should be ensured that the stimulus measures are in accordance with other construction strategies. The stimulus measures should be such that they also pass the test of cost-benefit analysis during normal times.

In the view of the National Audit Office, a renovation grant scheme of short duration used as cyclical tool does not encourage long-term property maintenance and development. The audit findings indicate that when used as a cyclical instrument a renovation grant scheme may actually create uncertainty in the operations of the housing companies. This is because as the housing companies do not know about the types of support available they do not have any incentive to carry out systematic long-term renovation or development in their properties. In fact, according to the audit, there seems to be a discrepancy between the stimulus objectives and the objectives concerning the state of the building stock laid out as part of the implementation of the cyclical grant scheme.

If the aim is to invest in more long-term property renovation and development in housing companies in accordance with the renovation strategy and irrespective of cyclical fluctuations, from the perspective of central government finances it would be more cost-effective and productive to make use of the steering instruments during the planning and preparation stage of the renovation projects. Housing companies should not automatically assume that it is the tasks of the central government to take part in the maintenance of privately owned properties. It would therefore be appropriate that housing companies can better understand the importance of correctly timed renovation of their properties, be it with private or public funding.

The grounds for introducing the cyclical grant scheme were not entirely logical

In 2008, there was a substantial decline in non-subsidised housing starts, and it was feared that the situation would lead to a sharp increase in unemployment in the construction sector. At the same time, there had been pent-up pressures in renovation in 2007-2008 as the demand for renovation was brisk but it was difficult to attract tenders and workforce for the projects. Nevertheless, it was decided to stimulate renovation by means of cyclical grants because the thinking was that workforce and operators would move from new construction to renovation.

However, the audit observations indicate that the labour markets for renovation and new construction are far apart. Most of the skills required in renovation are different from those that are needed in new construction.

Moreover, the companies that operate in new construction are not the same that operate in the renovation business. It was also noted in the audit that housing companies often request tenders from reliable contractors that they know, which does not help new operators to gain a foothold on the market in the short term. Neither can the argument that renovation is more labour-intensive than new construction be used as justification for directing the stimulus measures at renovation. According to experts, in proportion to the amount of money spent, renovation is as labour-intensive as new construction.

Thus, the audit findings indicate that it is not at all clear that operators and workforce would quickly move from new construction to renovation in large numbers. Especially in the short term, it is unlikely that any such movement would take place.

Thus, the existence of separate labour markets for renovation and new construction mean that a cyclical renovation grant scheme for which large sums are allocated in the state budget may generate excessive demand. This will increase the risk that the renovation grants that have cyclical aims may boost the prices of renovation contracts.

Comprehensive post-assessment of the stimulus instrument and its documentation would provide a useful knowledge basis for decision-making in cyclical stimulus situations

The introduction of the cyclical grant scheme was justified with the positive experiences from the 10 per cent renovation grant scheme in use in the 1990s. However, no comprehensive post-assessment of the impacts of the scheme had been prepared. The public servants that drafted the 2008 grant scheme had also taken part in the drafting of the 10 per cent grant scheme in the 1990s. In fact, the knowledge base used in the drafting of the cyclical grant scheme was largely founded on the empirical knowledge possessed by the public servants involved. The drafting was carried out by the public servants of the Ministry of the Environment and the Minister of Housing was also exceptionally closely involved in the process.

The timetable for the drafting of the stimulus decision and the cyclical grant scheme was extremely tight and as a result, compromises had to be made concerning the quality of statute drafting and only a superficial evaluation of the scheme's effects was carried out. Moreover, alternative ways of implementing the cyclical grant scheme, such as providing grants for the renovation of public buildings, were not examined in the drafting process.

However, from the perspective of transparent decision-making and drafting, it would have been desirable if documented information on the effects of the renovation grant scheme of the 1990s had been available. It would also have been useful to document the grounds for the decision-making connected with the cyclical grant scheme more generally.

Tight drafting timetables and a weak knowledge base create a risk that laying out policies can unnecessarily prevent an open and high-quality statute-drafting process. In this audit, too, better written documentation of the drafting of the cyclical grant scheme would have made it easier to outline the decision-making chain. When the stages of the drafting of the cyclical grant scheme were documented, it would have been necessary to get a more systematic and clearer picture of why it was decided to stimulate renovation and, more precisely, renovation carried out by housing corporations.

The fact that the knowledge base is largely composed of empirical information is also a risk because the drafting process relied on a small number of key public servants. It was quite thinkable that the public servants involved in the drafting of the grant scheme of the 1990s would no longer have been available. In such a situation even the use of empirical information would have been impossible, which would have further narrowed the knowledge base used as a foundation for the decision-making.

One stimulus method within the renovation sector worth examining would have been the provision of more grants for the renovation of public sector buildings. However, the audit findings suggest that this method would probably not have been more effective during the period in question. For example, there have been a number of shortcomings connected with the observation and repairs of the harmful effects of moisture and mould damage and the shortcomings have made it more difficult to make the buildings healthy. However, since 2010, as part of the cross-administrative moisture and mould programme, which is managed by the Ministry of the Environment, it has been possible to include in the grant scheme mechanisms that ensure better success of the renovation projects and the elimination of indoor air problems. In fact, the use public-sector building stock involves substantial health issues. If it is decided to stimulate the construction sector during a future downturn, consideration should be given to the allocation of more state support to the renovation of the public-sector building stock.

The National Audit Office is of the view that in similar stimulus situations in the future, a comprehensive post-assessment of the effects of the grants would be highly useful for the knowledge base of the decision-making and would promote high-quality statute drafting. The existence of

an independent impact assessment unit and the availability of its expertise would make decision-making more transparent and credible in crisis situations where important decisions have to be made quickly.

Well-established practices between ARA and the municipalities facilitated the implementation of the cyclical grant scheme - unexpectedly large number of applicants was, however, an administrative burden

The period of validity of the cyclical grant scheme had to be extended twice. This was because by the end of 2009 about 22,000 applications had been received, which was almost four times as many as the original estimate of between 5,000 and 6,000. The original grant authorisation had totalled 125 million euros but after it had been decided to provide grants to all applicants meeting the criteria, the final requirement for grant authorisations was twice as high (250 million euros).

The division of responsibilities in the implementation of the cyclical grant process was appropriately organised as there were already well-established procedures between ARA and the municipalities for carrying out the process. The role of ARA in the organisation of the provision of information was a substantial factor in ensuring that enough information on the grants was provided and that the information reached the municipalities quickly. The problem was, however, that the cyclical grant scheme was an additional task and had to be managed with existing resources and data systems. In fact, the implementation of the cyclical grant scheme meant a great deal of overtime work in ARA and the municipalities, in addition to which internal personnel arrangements also had to be made.

The vast number of applications was the prime reason for the administrative burden resulting from the cyclical grant scheme. Because of the data systems used in the grant process, a great deal of manual work had to be done in both ARA and the municipalities, which slowed down the processing of the grants and payment decisions. Moreover, as a result of the manual work and the stress caused by the tight timetable, there was a high likelihood of human errors. At the same time, however, the flexibility of the terms and conditions of the cyclical grants eased the workload of ARA and the municipalities, compared with the processing of annual grants. The National Audit Office is of the view that the current project of putting the grants provided by ARA on an electronic basis is important in terms of making the grants process more efficient and ensuring integrity of data.

Extension of the validity of the cyclical grant scheme and the changing of its terms and conditions fragmented the stimulus instrument and made it more difficult for municipalities to provide instructions and advice. There was some uncertainty in municipalities of what instructions housing corporations should be provided in a situation where the terms and conditions changed several times within a short period of time. The uncertainty arising from the changes in the cyclical grant scheme cannot be considered positive in terms of the workability of the scheme.

Paying the 125 million euros allocated for the cyclical grant scheme from the National Housing Fund was problematic in terms of the spending limits procedure

A total of 125 million euros was paid in cyclical grants from the National Housing Fund, which is an off-budget fund. In the audit on the effectiveness of the spending limits procedure, the National Audit Office had already drawn attention to what impacts stimulus measures would have from the perspective of the implementation of fiscal policy. There are no logical grounds for a situation where the transfers paid through the National Housing Fund were left outside the spending limits. From the perspective of an effective fiscal policy, it would be logical and transparent that all expenditure would come under the same fiscal policy rules. The flexibility required by exceptional cyclical fluctuations should be included in the system of rules.

The tight timetable and strict terms and conditions of the cyclical grant scheme of 15 per cent for energy-efficiency renovations significantly limited demand for the scheme

The cyclical grant scheme for energy-efficiency renovations proved fairly insignificant as an incentive. The entity in which the measures detailed by decree had to be implemented in an extremely tight timetable meant that the demand for the cyclical grants for energy-efficiency renovations was not at estimated level. A total of 12.3 million euros or 30 per cent of the appropriation allocated for the scheme remained unused.

The audit observations suggest that housing companies did not possess enough knowledge about the effects of the measures improving energy efficiency and thus the scheme failed to attract enough interest. Initiating renovation measures improving energy efficiency usually requires time and housing companies must also familiarise themselves with the

measures. According to experts, such decisions are too slow for the cycle of an extremely short-term grant scheme.

The measures eligible for the grants, which were laid down in a decree, were considered extremely extensive and expensive, in addition to which the repayment time of the grants might also have been in too distant future. Moreover, the housing companies had to wait for the confirmation of the final grant percentage until the grant decision. In fact, in some cases, the final grant covered less than 15 per cent of the renovation costs.

At the same time, the most efficient way of improving energy efficiency is to do it in connection with other renovation measures and a solid and workable structure should not, as a rule, be changed for the sake of energy efficiency. If the opportunity to implement energy saving measures in connection with renovations is missed the next chance will only come in the distant future. Postponing the measures makes it more difficult to achieve the targets set out in the national climate and energy strategy. When housing corporations were first provided with a general 10 per cent cyclical grant and only then with a grant aimed at improving energy efficiency, some of the chances to introduce energy-saving measures in these properties were lost. Thus, the audit observations indicate that some of the stimulus objectives laid out for the cyclical grant scheme were in conflict with energy efficiency targets.

The conclusion of the National Audit Office is that the cyclical grant scheme for energy-efficiency renovations was in accordance with the national climate and energy strategy but that the grant scheme was not successfully implemented because not enough consideration was given to the chances of housing corporations to carry out renovation projects improving energy efficiency.

Cyclical grant scheme was introduced in an environment that provides ample opportunities for shadow economy

According to experts, the role of the shadow economy in the construction business increases during an economic downturn. At the same time, however, the construction sector had already introduced a number of measures combating the shadow economy as the scheme was in effect. These include contractor's liability the aim of which is to tackle the problem of the shadow economy in the construction sector.

According to the observations made by the authorities, the available instruments did not prevent some housing companies receiving renovation grants from neglecting their statutory obligations in renovation projects. Most of the operators in the renovation sector are still very small, which

means that almost all renovation projects are subcontracts. This has made it considerably more difficult to outline the division of the total contract and the obligations of the different parties arising from it.

Moreover, based on the observations made by interest organisations and the authorities, the number of foreign companies and workforce increased in Finland during the period in question. At the same time, however, the exact number of foreign workforce and companies is still unknown.

Even though many of the foreign companies and employees manage their statutory obligations in a laudable manner the law has not permitted the Finnish Tax Administration to properly ensure that the income that should be taxed in Finland is declared and that the taxes on them are collected. However, with the programme to combat the shadow economy and the resulting introduction of the tax number system and the introduction of the monthly notification procedure in 2014, efforts are being made to put the statistics on foreign workforce and the monitoring of the management of tax obligations on a more effective basis.

The National Audit Office is of the view that as the problems caused by the shadow economy are known, the government should as part of the renovation grant schemes combat the shadow economy in a comprehensive manner. The shadow economy should be taken into account in the planning and drafting of grant schemes. When the grant schemes become more important in terms of central government finances and the Finnish economy as a whole and the likelihood of shadow economy phenomena grows, more efforts should be taken to ensure that there are fewer opportunities to engage in the shadow economy. Taking the shadow economy into consideration in the grant schemes requires cross-administrative cooperation between the Ministry of the Environment, ARA and the Finnish Tax Administration.

Even though the renovation sector is important, the statistics on it are inadequate

It was highlighted in the audit that it is impossible to make detailed estimates of how cyclical grants impact contract prices. This is because there is currently no index that would allow the monitoring of the trends in renovation contract prices. However, the audit findings indicate that the cyclical grant scheme led to slight increases in contract prices of renovation projects.

The general quality of renovation statistics has fallen behind the quality of the statistics on new construction. However, as renovation accounts for an increasing proportion of the construction business, the manner in which

the statistics are compiled should be improved. When housing-policy measures that are important in terms of central government finances are introduced in the renovation sector, it is extremely important that the impacts of the measures on building stock and the trends in the pricing of renovation contracts can be assessed.

In the view of the National Audit Office, consideration should be given to the development of a renovation contract price index, which would make it easier to monitor the price levels in the renovation sector. The index would be useful in both the public and the private sectors. The contract price index would also be a useful tool in assessing the cost-effectiveness of the support provided by the state. According to experts, it would be entirely possible to develop such a price index even though the task would be more difficult than setting up a price index for new construction.

Recommendations of the National Audit Office

1. In the future, the Ministry of the Environment should pay attention to a comprehensive post-assessment of the stimulus measures.
2. In any stimulus situations involving the construction sector, the Ministry of the Environment should consider allocating more government support to the renovation of public-sector buildings.
3. In order to promote a long-term and systematic renovation culture in housing corporations, the state should shift the focus of its steering instruments to the planning and preparation of the renovation projects.
4. The quality of the renovation statistics should be improved. The Ministry of the Environment and Statistics Finland should consider the development of a renovation contract price index.
5. The Ministry of the Environment should, in cooperation with ARA and the Finnish Tax Administration, give adequate consideration to the combating of the shadow economy in renovation grant schemes that are important in terms of central government finances and the Finnish economy as a whole.