NATIONAL AFFORDABLE HOUSING SUMMIT

THE NATIONAL RENTAL AFFORDABILITY SCHEME

A Submission to the Senate Inquiry on the National Rental Affordability Scheme Bill 2008 and the National Rental Affordability Scheme (Consequential Amendments) Bill 2008

Introduction

The National Affordable Housing Summit group was established in 2004. It comprises the Australian Council of Social Service, Australian Council of Trade Unions, Community Housing Federation of Australia, Housing Industry Association Ltd and National Shelter. The independent chair is Julian Disney.

The group has issued a number of papers since its inception, including a detailed proposal in 2007 for a National Affordable Rental Incentive scheme (for an outline, see Appendix A). The proposed scheme had a similar goal to the Low-Income Housing Tax Credit which has operated successfully in the United States for more than twenty years. It sought, however, to provide a somewhat simpler, more cost-effective and more appropriately targeted approach.

The group's proposal is similar in many key elements to the National Rental Affordability Scheme which is to be established by the Bills under consideration by the Committee. This submission outlines some of the group's joint views on aspects of the new scheme which are relevant to the three issues specifically mentioned in the Committee's terms of reference. Some of our member organisations will also be making submissions in their own names.

Targeting affordable housing to people who are most in need

The main vehicle for providing affordable housing to those people who are most in need is, and should remain, rental housing provided by government or non-profit agencies with funds obtained entirely or almost entirely from public revenue. Government and non-profit housing of this kind has traditionally been funded principally under the Commonwealth State Housing Agreement (CSHA).

Several years ago the Summit group proposed that the CSHA should be replaced by a National Affordable Housing Agreement (NAHA) which, amongst other things, would provide a better funding system for government and non-profit housing. Our suggested improvements would generate substantial growth in the current supply of government and non-profit housing for high-need households (key aspects of the suggestions are outlined in Appendix B).

The group will continue to advocate vigorously for improvements along these lines and for the sustained increase in public investment which they would involve. The current shortfall in low-rent housing is so great, however, that it cannot possibly be addressed sufficiently by relying solely on additional government funding. In any event, there is much to be said for drawing also on private sector skills and experience in the financing and provision of housing.

A scheme which seeks to attract substantial private investment into low-rent housing needs to avoid imposing unduly onerous conditions or uncertainties. It also needs to learn lessons from the "over-targeting" of government housing which has aggravated poverty traps and work disincentives, created dysfunctional and stigmatised communities and reduced the cost-effectiveness of housing provision.

Accordingly, while the scheme should make a substantial contribution to the task of housing people in the deepest distress it should not focus solely or overwhelmingly on them and thereby tend to entrench their disadvantage. A social mix of tenants also increases the attractiveness for investors and reduces the necessary size of public subsidy per dwelling.

The scheme should also recognise that substantial rent reductions can be of great value to low-income households, even if they do not achieve an inevitably arbitrary benchmark of affordability relative to their income. Given the huge shortage of public and non-profit housing which is likely to remain for decades at least, for many such households the realistic alternative to discounted rent under such a scheme will often be full rent in the private market.

The Summit group believes that care must be taken to ensure that NRAS achieves a "social mix" of tenants including, for example, substantial proportions of both "high-need" and "moderate income" households. This may require specifying minimum proportions for each of these categories across the scheme as a whole (although not for each project).

When assessing particular applications it will be appropriate to take into account how much, if any, housing they would provide for "high-need" households. But an application should not be given automatic priority over others solely because it would provide a larger number or proportion of housing of that kind. Such an approach would weaken the effectiveness of the scheme for tenants, investors and managers.

It is also important that the new NAHA facilitates arrangements by which applicants can combine government incentives and private resources under NRAS with capital funding, land or other assistance from government or charitable organisations. This could, for example, enable housing to be let to high-need households with a greater rent discount, and for a longer period, than is required by NRAS. It is partly for this reason that the Summit group has emphasised that the scheme should be seen as establishing a source of funding, not a distinct class of housing.

Efficient and effective growth in supply of affordable housing

No single method of provision or funding of affordable housing is always more efficient and effective than all others. In some circumstances, and to some extent, provision by government or non-profit agencies with full government funding can be more efficient due, for example, to economies of scale, specialised expertise, lower borrowing costs etc. In other circumstances, private sector involvement can provide resources, expertise, innovation or flexibility which improve overall effectiveness. Moreover, relative effectiveness must be weighed against the relative availability of public and private resources at the times when choices have to be made.

NRAS provides the opportunity to substantially improve over time the range of methods which are available to meet differing opportunities and challenges for boosting the supply of low-rent housing. In particular, it provides greater encouragement for the private sector to become involved, including major institutional investors as the scheme develops. This arises not only from the direct financial incentive but also from the improved encouragement and identification of non-profit organisations with the necessary skills and resources to manage low-rent housing for private investors.

NRAS also provides greater encouragement for governments, local councils, charities etc to contribute extra resources and expertise towards provision of affordable housing. This could include, for example, providing free or discounted land, tax or rate concessions, donations or expert assistance with development and management. The availability of NRAS incentives can enable such organisations to "drive their dollar further", thereby encouraging a sustained involvement in the affordable housing area which they might otherwise have considered not worth commencing.

It is also reasonable to expect the scheme to have a beneficial impact on the supply of affordable housing by counteracting inflationary pressures on rents in the lower-end of the market. This is due partly to the overall increase in supply which it will generate and also to this increased supply being rented substantially below market levels.

Subject to maintaining a reasonable attractiveness to investors, the scheme provides good opportunities for encouraging greater long-term efficiency in the design, construction and ongoing use of dwellings. This includes, for example, looking favourably on applications that would provide housing which meets high standards of energy efficiency.

As the scheme develops, its effectiveness would be enhanced substantially if Calls for Expressions of Interest specified some particular portfolios of housing for which applications are sought. For example, applications could be sought for provision of, say, 1000 dwellings in middle-ring Melbourne within the next 3 years in accordance with key requirements in terms of dwelling size and perhaps a few other matters.

This approach would be especially important for attracting large investors and developers, generating sufficient but not counter-productive competition, and providing housing which promotes and reinforces appropriate patterns of urban development. It would usually benefit from the relevant State or States playing a key role in defining the portfolios and assessing applications.

Substantial scope should be retained, however, for applications involving small numbers of dwellings and/or not addressing any of the designated portfolios. The initial system of Partnership Facilitators could be further developed to assist in encouraging applications of this kind while also engaging specialists to concentrate on facilitating applications for one or more of the large portfolios.

The scheme would also benefit from providing a two-stage approach to submission and assessment of applications, especially for large applications which involve substantial time and expense in preparing a fully detailed application. A preliminary assessment based on outline applications could be followed by a more detailed process for refining and assessing those applications which are initially considered to be the most promising. A somewhat similar approach has been adopted for the new Housing Affordability Fund.

Achievement of strong and effective growth under NRAS would be facilitated if NAHA promoted flexible interaction with other sources of funding by establishing integrated growth targets and growth funding along the lines suggested in Appendix B.

Facilitating investment by private investors and non-profit organisations

The comments and suggestions made above relate also to facilitation of investment by private investors and non-profit organisations. A number of other points need to be mentioned here.

The Summit group has repeatedly emphasised that a scheme of this kind should not be seen as a quick fix. It is aimed at achieving substantial improvements in the supply of low-rent housing over the next couple of decades. In particular, it aims at starting to reduce the huge gap between Australia and most other developed countries in the proportions of rental housing which are owned by institutional investors or non-profit organisations. A major shift of this kind inevitably takes time and is subject to the ebbs and flows of surrounding economic circumstances.

It is likely to take several years at least before institutional investors become substantially involved in the scheme. The administrative arrangements need to be bedded down and then further developed with special attention to the needs of institutional investors. The investors, as well as possible partners from the government and non-profit sectors, need time to factor opportunities under the scheme into their general strategies as well as their planning for particular projects (which often takes some years). Non-profit organisations need to develop and demonstrate their expertise in ways which attract the interest and confidence of investors.

The current problems and uncertainties in global financial markets increase the likelihood that the scheme will take time to develop major momentum. On the other hand, they may generate conditions which are more favourable for the scheme than when it was first announced. For example, they may moderate expectations of investors and developers in relation to rates of return and increase the premium which is placed on the security of a stream of income from government. In time, they may lead to interest rates being lower and medium-term trends in house prices being less uncertain than in recent years.

It would be both unrealistic and undesirable to design the scheme so that it attracts institutional investment for affordable housing in all places and under all circumstances. For example, the basic NRAS incentive should not necessarily be set at a level which is sufficient on its own to attract investment in median-priced units in central Sydney, let alone do so at a rent which is fully affordable for a high-need household rather than just discounted to the extent required by NRAS.

However, the scheme should and does allow for variations in the overall value of the incentive which is provided by or in conjunction with it. It sets a standard amount for the Commonwealth contribution under NRAS but it clearly envisages, for example, that States could provide more than their required minimum or combine it with a capital grant. Some States have already adopted this approach.

Reliance on the States rather than the Commonwealth to supplement the basic incentive where appropriate is a key reason why the scheme sets their basic contribution much lower than the Commonwealth one. Planning and delivery of projects will usually involve providers in lengthy and detailed negotiations with State and local governments, including over whether any additional assistance will be available. Provision for variation in the Commonwealth incentive would tend to add undesirable complexity, delay, uncertainty and controversy.

It is too early to judge whether the basic incentive levels should be raised more rapidly than will occur from indexation in accordance with general rent increases (which for the foreseeable future are likely to be substantially above the general CPI). As mentioned earlier, the scheme should not be expected to automatically meet the full expectations of developers wishing to apply it to their current priority holdings using their current financing methods.

Any consideration of a further increase should be based on transparent modelling using reasonable assumptions and independent analyses of market conditions. If it is considered that the global financial crisis necessitates a short-term supplement or other form of additional assistance, it should be provided on that explicit and time-limited basis.

One of the Summit group's members, the Community Housing Federation of Australia, has made a detailed submission to the Committee outlining a number of ways in which the scheme's attractiveness for non-profit organisations could be strengthened. We endorse those suggestions, especially in relation to problems concerning charitable status, earlier payment of grants, capacity-building and consistent systems of regulation.

Conclusion

A number of the suggestions made in this submission will need to be considered before the Third Call for Expressions of Interest is issued next year. It is this Call which should start to ramp up the scale of appropriate applications and begin attracting interest from institutional investors.

The group believes it is absolutely essential that an expert and independent group of advisers be asked to assist in detailed formulation of the Third Call and related aspects of the scheme. The group could include a person with high-level experience in business and finance, another with substantial experience in provision of low-rent housing and a third person with expertise in schemes of this kind.

The group also believes it is essential that the National Affordable Housing Agreement facilitates efficient interaction between NRAS and other sources of assistance for provision of affordable housing. This should include adopting a framework of targets and funding along the lines suggested in Appendix B.

APPENDIX A

A National Affordable Rental Incentive

Outline of a Proposal in July 2007 by the Australian Council of Social Service, Australian Council of Trade Unions, Community Housing Federation of Australia, Housing Industry Association Ltd and National Shelter

Purpose

The proposal is for a National Affordable Rental Incentive (NARI) scheme which provides a financial incentive package to attract private investment into affordable rental housing for lower-income households, especially from large investors. The scheme would be established as part of the new National Affordable Housing Agreement proposed in our group's recent *Call for Action*.

Value and number

The scheme involves providing developers, investors or landlords with a financial incentive (NARI) of a specified annual value per dwelling that is sufficient to attract investment in designated types of housing. Each NARI would be made available annually for at least ten years in relation to any particular dwelling. The number of NARIs being provided each year could rise by up to 10,000 per year until a plateau of, say, 100,000 dwellings is reached.

Eligibility

At least in the early years of the scheme, NARIs might be available solely or mainly for newly-constructed dwellings that are managed by an appropriate non-profit housing organisation. They would be subject to national conditions about rent levels, household income, length of tenure and some other matters. For example, 80% of dwellings might have to be let to lower-income households at no more than 80% of market rent.

Sources

An agreed share of the value of each NARI would be provided by the Commonwealth Government to the States in the form of a cash grant or tax credits. They would be allocated between States on the basis of their populations. The States would then be responsible for contributing the remaining share and allocating the NARIs to particular providers, subject to such additional conditions as they may consider appropriate and are consistent with the national criteria. Their contribution could be provided as a grant, tax benefit, guarantee or in some other form. Where appropriate, they could seek contributions from local councils.

Other assistance

Particular dwellings could attract both a NARI and a capital grant under the National Affordable Housing Agreement, especially if the rent discount is to be greater than is required by the NARI scheme and/or to be provided for a longer period. This would be especially important for non-profit organisations wishing to keep dwellings as permanently affordable housing or to focus on households with special needs that increase the cost of their housing or management.

Impacts

The scheme would increase investors' overall rates of return as well as the proportion which comes from regular rental income rather than capital gains. As well as benefiting households in the dwellings in question, the scheme would also reduce upward pressure on general house prices. This, in turn, would improve renters' ability to save for home purchase and service their subsequent mortgage.

APPENDIX B

Growth Targets in a National Affordable Housing Agreement

Extracts from a Discussion Paper prepared in September 2008
by the National Affordable Housing Summit group

The NAHA should set a specific growth target for the overall number of dwellings in "affordable housing programs" (AHPs). This generic category would include public housing, non-profit housing, housing provided with assistance under NRAS, and some home purchase assistance programs.

For example, the NAHA could adopt a growth target of an additional 250,000 dwellings in AHPs by 2020. Of this total, a target of 60,000 could be set for achievement within the four-year period of Forward Estimates in the next Commonwealth Budget.

Within the overall growth target, maximum and minimum proportions could be specified for particular categories of AHP dwelling. These types should be defined principally by reference to the benefits provided for tenants, not by the type of provider or source of funding. The two key categories could be defined as follows:

> "*Band A*" dwellings are those for which, except in specified circumstances, rents must be kept below, say, 25% of residents' incomes for at least, say, 25 years (although actual rents may be set by other criteria).
>
> "*Band B*" dwellings are those for which, except in specified circumstances, rents must be kept at least, say, 20% below market rent for at least, say, 10 years.

By way of example, the overall growth in the number of AHP dwellings could be required to consist of at least one-third "Band A" dwellings and at least one-half "Band B" dwellings. It could also be required that "high-need households" comprise, say, 50-75% of the increase in households in Band A dwellings and, say, 25-50% of the increase in households in Band B dwellings.

The NAHA should include earmarked growth funding by the Commonwealth which is conditional on the States providing sufficient additional resources to achieve the overall growth targets in accordance with the specified profiles. It should also include a substantial Commonwealth subsidy for operating and replacement costs.