AHURI Research & Policy Bulletin

ISSUE 41 April 2004 • ISSN 1445-3428

Sustainable financing for public housing authorities

AFTER SIX YEARS OF POLICY AND PROGRAM DELIVERY CHANGE, SIX OUT OF NINE STATE HOUSING AUTHORITIES IN AUSTRALASIA ARE RUNNING OPERATING DEFICITS WHICH ARE NOT FINANCIALLY SUSTAINABLE.

KEY POINTS

- The major sources of income for State Housing Authorities (SHAs), government grants and rents from tenants, have been constrained, especially since 1996, as state and federal governments cut back real levels of capital funding through the Commonwealth State Housing Agreement (CSHA) and moved to target available public housing on low income households with multiple and complex needs.
- This has led to an increase in the proportion of public tenants receiving rent rebates and accessing public housing through priority allocation.
- Closer and more effective targeting, associated with Australian Government requirements to continuously improve the quality of service to tenants, has generated rising operating costs for the housing authorities.
- The overall consequence has been for SHA revenue to increase more slowly than total costs, moving the authorities from a position of moderate operating surpluses into rising structural deficits.
- SHAs have responded to a worsening financial position by asset sales, which have helped bridge the growing operating deficit in the short term. But this is clearly not sustainable in the longer term (i.e. eventually the authority runs out of saleable dwellings).
- If governments funded the implied community service obligation (the difference between market rent on public dwellings and the rebated rent paid by eligible public tenants), as currently happens in New Zealand, then all housing authorities bar one would be returned to operating surpluses.
- By continuing to fund the growing cost of community service obligations in this area, government could place the SHAs on a sound and sustainable financial basis. However, such a policy implies that governments would need to commit a rising level of funding to bridging this gap; the rate of rise would depend on a range of factors, including the rate of increase in tenant incomes and the rate of house price and rental inflation.

*Based on research by **Jon Hall and Mike Berry**, AHURI RMIT-NATSEM Research Centre.*

The research provides the first systematic and robust comparative analysis of the financial operating positions of the Australian and New Zealand public housing authorities.

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BACKGROUND

Key drivers of change in the public housing system have been the Commonwealth State Housing Agreement (CSHA), the amount of money provided, and the purposes for which these funds can be used.

The 1996 CSHA marked a significant shift in a number of areas that directly and indirectly affected the financial situation of the State Housing Authorities (SHAs). It introduced greater flexibility, increased accountability, new planning requirements and a greater focus on client outcomes.

Many controls that had characterised previous CSHAs were removed. The 1996 agreement offered the States and Territories more flexibility in using funds to address housing needs as part of their key responsibility for managing housing assets and delivering services. Some Commonwealth controls over State expenditure and activities contained in the 1989 CSHA were removed and some arrangements were also simplified.

The 1996 CSHA therefore enabled funds to be channelled into a broader array of 'allowable uses' than was the case earlier. This meant that, subject to agreement through the Commonwealth-State planning process, States had more flexibility to allocate funds between capital and recurrent purposes and for non-capital expansion such as head leasing (leasing dwellings from other landlords and then sub-letting them to public tenants).

Performance indicators were also established for the first time, and national measures of performance in relation to the achievement of consumer and administrative efficiency outcomes were agreed. Customer focus was given more prominence and the interim agreement required each State and Territory to develop a code of practice about housing assistance funded under the CSHA.

To summarise, the 1996 Interim Agreement effectively eliminated the separation between capital and recurrent purposes to which the grants could be applied, and focused on greater accountability for the quality, timeliness and appropriateness of the service provided and provided explicit measures of consumer satisfaction and client rights.

The 1999 and 2003 Agreements generally entrenched the direction set out in the 1996 Interim Agreement.

There have also been major shifts in housing policy across the Tasman. In 1992, Housing New Zealand Corporation was split into two entities: Housing Corporation of New Zealand and Housing New Zealand (HNZ), with the Housing Corporation of New Zealand responsible for a portfolio of residential loans and the management of the Government's surplus land assets, and HNZ, the Government's rental stock.

A full market rent regime was introduced by HNZ and income related rents dispensed with. From 1993 to 2001 both public and private tenants meeting appropriate eligibility criteria received an accommodation supplement, provided as a cash payment by the equivalent of Centrelink. When compared to an income related rent payment of 25% of income, this supplement only provided a partial subsidy, and during this time, a large proportion of public tenants were paying more than 50% of their incomes in rent.

In this period Housing New Zealand was treated strictly as a trading entity. It produced significant operating profits and paid off its debt, paid tax and produced large dividends or repatriations of equity to the New Zealand Treasury. In addition, Housing New Zealand sold to the public some 10,000 dwelling units, or 15% of the stock. At the time of its dissolution HNZ had plans to sell up to 20,000 more dwellings.

For most of its life Housing New Zealand was in large part focussed on asset sales and consequently a significant proportion of the portfolio was not maintained to a high standard. As a result, the restructured authority Housing New Zealand Corporation has inherited a large maintenance backlog.

In August 2000, the New Zealand Government passed new legislation, the Housing Restructuring Income Related Rents Amendment Act, prescribing new rules for the setting of income related rents. At this time Housing New Zealand Corporation (HNZC) was also established.

As well, the maximum income related rent payment was also set at 25% of net (after tax) income.

Accommodation supplements were abolished for public tenants. Coupled with these new rent policy arrangements the government established a procedure to fully fund Housing New Zealand Corporation for the difference between the income related rent charged to tenants and the market rent.

METHODOLOGY AND CAVEATS

This research was made possible by the cooperation of all Australian States and Territories, the Australian Government and the Housing New Zealand Corporation.

All State Housing Authorities in Australia and Housing New Zealand Corporation provided copies of their published financial statements for the years 1990-91 to 2000-01 inclusive. These statements were comprehensively reviewed. Each housing authority was requested to provide answers to a set of questions arising from the financial statements to enable all abnormals, capital, non public housing, and other ambiguities to be removed and the actual amounts of revenue and expenditure for each year to be identified in accordance with principles, definitions, core items and add back items agreed to by participating jurisdictions (the process of agreement and detail of jurisdictional differences are outlined in full in the Final Report for this research).

After obtaining all this information and making relevant adjustments the actual amounts received and spent for the core items were calculated for each year for each housing authority. These amounts were then divided by the relevant dwelling number to obtain per unit outcomes. In the case of Housing New Zealand Corporation, the numbers derived for each year were converted to Australian dollars at the Interbank rate prevailing at the 30th June each year.

All the per unit outcomes were then adjusted by the average Consumer Price Index for all capital cities for Australia. These quantitative outcomes were supported by face to face interviews with either the Chief Executive or Chief Financial Officer for all housing authorities in Australia and New Zealand. Full details of this methodology and its limitations can be found in the Final Report.

FINDINGS

FINANCING TRENDS

- Between 1990-91 and 2000-01 total annual real capital funding for public housing in Australia fell by 25%.
- The total public housing stock in Australia rose to a peak of around 380,000 dwellings (not including head leasing and inter-governmental transfers) in 1996-97, declining to around 375,000 by 2000-01. The rate of stock loss was greater in New Zealand over that period; the total number of public dwellings fell from about 70,000 in the mid-1990s to 58,000 in 2000-01.
- The proportion of public tenancies on rebated rents in Australia rose from 78% to 88% between 1990-91 and 2000-01.

Figure 1: Real percentage change in net incomes and expenditures per dwelling: (excluding net interest and depreciation): 1990/91 – 2000/01: all state housing authorities and Housing New Zealand Corp.

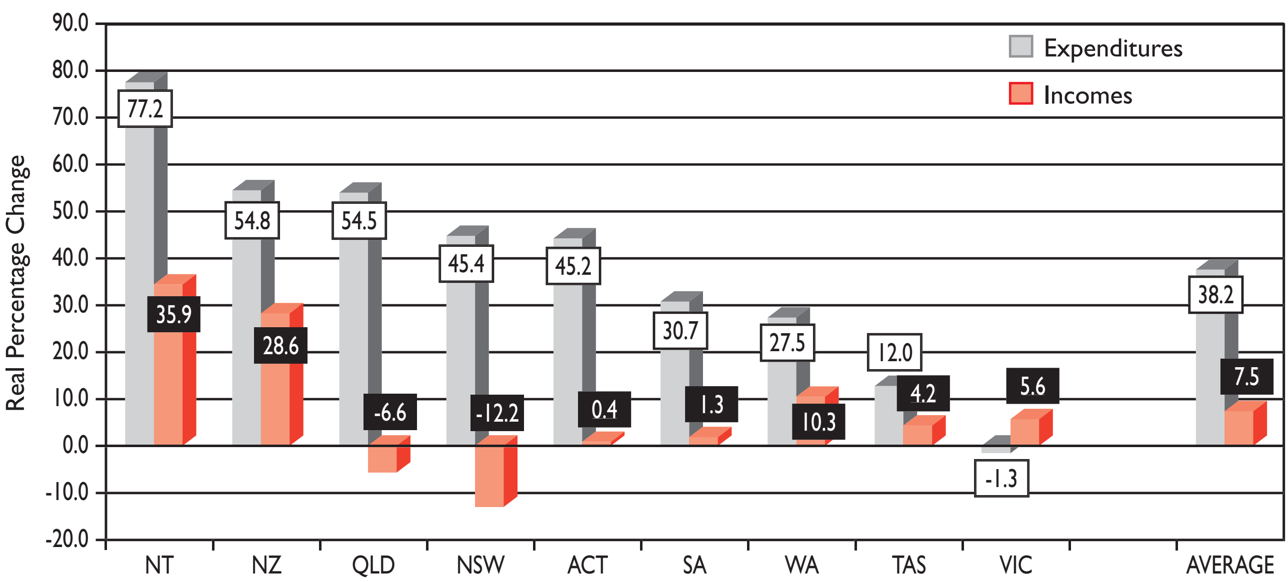
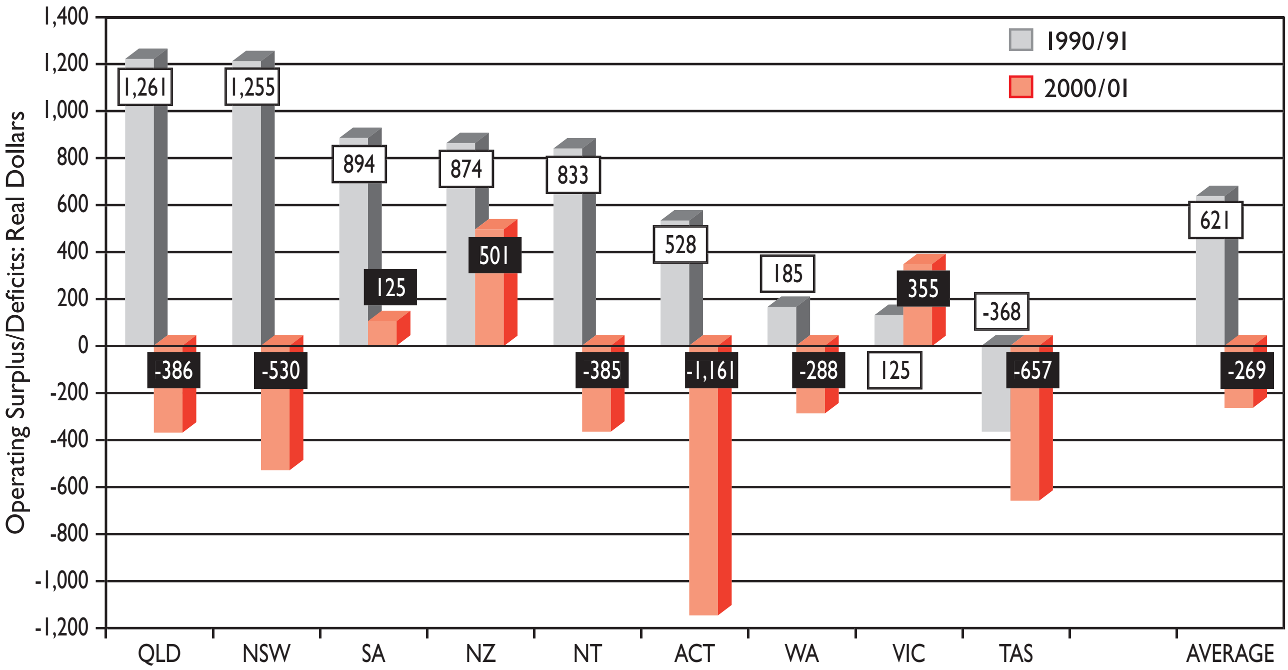


Figure 2: Real operating surpluses/deficits per dwelling: (excluding net interest and depreciation): 1990/91 – 2000/01: (June 2001 dollars): all state housing authorities and Housing New Zealand Corp.



- The proportion of priority allocations in Australia rose from 17% to 49% of new tenancies in the same period.
- Between 1990-91 and 2000-01, annual spending in real terms across all housing authorities in Australia and New Zealand rose on average by 38.2%. Over the same period, total real income (revenue) rose by only 7.5%.
- The Northern Territory had the greatest rate of real expenditure growth (77.2 %). NSW had the lowest rate of income growth – a decline of 12.2 % (i.e. a decline in real income per dwelling). The range of outcomes is summarised in Figure 1.
- Consequently, the operating result for all housing authorities, on average, moved from a surplus of $621 per dwelling in 1990-91 to a deficit of $269 per dwelling in 2000-01.
- In 1990-91 all housing authorities enjoyed operating surpluses. By 2000-01 only South Australia, Victoria and New Zealand were in surplus. The ACT had the largest operating deficit by 2000-01. The range of outcomes is summarised in Figure 2.

THE MAIN DRIVERS

On the income side, the weakening financial position appears to be due mainly to the effects of policy changes resulting in tighter targeting of public stock on low-income households and those with multiple support needs, thus reducing the rental income for SHAs.

Tighter targeting also impacted on the **operating cost side**, as tenants with multiple needs are more costly to support. This was reinforced by the post-1996 requirements to improve customer service standards and the greater flexibility allowed housing authorities in managing their dwelling assets.

More specifically:

- Salary and related administrative expenses per dwelling rose, on average, by 57% in real terms during the 1990s. Growth in this expenditure item was greatest in the ACT and NSW. This is one of the fastest-growing expenses for SHAs and appears to reflect the increasing demands placed on authority staff by the shift to clients with more complex support needs as well as the need to meet the new performance standards.
- Maintenance expenditure rose by 39% in real terms over the same period. This reflects both the ageing of the dwelling stock and the more active asset management regimes introduced by the SHAs during the past decade. As most public housing stock reaches acceptable standards, this expenditure item is likely to stabilise.
- Real expenditure on depreciation rose by 54% over the period. In the case of NSW, New Zealand, the Northern Territory, South Australia and

Queensland, depreciation charges increased by more than 100%. Regular asset revaluations combined with asset restructuring and improvements underlie this trend.

- Conversely, interest paid on borrowings per dwelling fell by 44%. Only in Western Australia did this expenditure item increase. Asset sales and debt repayment have resulted in this decline.

It is clear that greater flexibility and more active asset management regimes introduced by the housing authorities during the 1990s have resulted in the gradual selling off of public housing stock. Asset sales have helped bridge the increasing operating deficit for those authorities in the short run. However, this is not a sustainable strategy for the longer term.

As long as the underlying drivers result in continuing falls in income growth and continuing rises in real expenditures, as the graphs in this bulletin demonstrate, eventually housing authorities will run out of dwellings to sell to bridge the growing financial gap.

AN OPTION FOR REVERSING THE TREND

One alternative to the slow decline of public housing stock is for the community service obligation to be recognised and separately funded by government (as is now the case in New Zealand).

Community service obligation in this context means the cost of the difference between the commercial or market rent for a dwelling and the concessional price paid by the tenant. For public housing, the commercial or market price is market rent and the concessional price is the income-related rent paid by the tenant. The community service obligation per tenancy equals the rental rebate.

If this were done, the financial situation of all the Australian and New Zealand housing authorities would be placed on a commercially sound basis. Funding the rebate would eliminate deficits in all housing authorities, except the Northern Territory, and also provide a basis for their longer-term financial stability.

However, the research shows that housing authorities need to do more than eliminate current deficits. If deficits are not to worsen, the authorities must also achieve some real net income growth. A financial solution based upon fully funding the rental rebate would enable net incomes to at least keep pace with efficiently managed cost structures.

POLICY IMPLICATIONS

On the basis of the study findings, summarised above, the implications for policy include:

- examining ways in which the community service obligation met by Australian housing authorities can be fully funded, including changes to current funding arrangements;
- preparing detailed forecasts of the likely net income of all Australian housing authorities if there were no change to current targeting policy; and
- examining other options by which net incomes for housing authorities could grow in real terms, including:
  - relaxation of affordability benchmarks and change to current Productivity Commission targeting indicators;
  - revision of current targeting policies; and
  - growing the housing stock to diversify the income base.

FURTHER INFORMATION

This bulletin is based on AHURI project 30154, *Operating deficits and public housing: policy options for reversing the trend.* Reports from this project can be found on the AHURI website (**www.ahuri.edu.au**) by typing the project number into the search function.

Papers available:
- Positioning Paper;
- Final Report.

Or contact the AHURI National Office on +61 3 9660 2300.

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ACKNOWLEDGMENTS This material was produced with funding from the Australian Government and the Australian States and Territories. AHURI Ltd gratefully acknowledges the financial and other support it has received from the Australian, State and Territory Governments, without which this work would not have been possible.