

Risk assessment practices in the private rental sector: implications for low-income renters

RISK, WHETHER PERCEIVED OR ACTUAL, IS A CRITICAL FACTOR FOR PROPERTY MANAGERS IN DECIDING WHO IS ALLOCATED HOUSING IN THE PRIVATE RENTAL MARKET, AND HOW THE ALLOCATION PROCESS OCCURS.

KEY POINTS

- The main markers of risk associated with tenant characteristics or circumstances in the context of tenant selection and allocation are the '(in)ability to pay' and/or '(in)ability to care' for the rented property. Ability to pay is generally determined using a 30 per cent rent to income ratio as an affordability benchmark, whereas ability to care is often based on less quantifiable assessments.
- Risk assessment and allocation strategies employed by property managers comprise both formal and informal processes, which include: sorting and ranking of applications; 'lawful' discrimination in determining the most appropriate tenant; and 'handing over' responsibility to the owner for making the final decision, to avoid providing reasons for rejecting certain applications.
- Typically property managers conceptualise 'suitable' tenants as those who are resourceful, reputable, competent, strategic and presentable.
- A range of particular personal characteristics and circumstances are interpreted by property managers as signs of risk in property rental. Those applicants commonly considered to present a higher risk have limited resources or constrained capabilities and include people on low incomes, sole parents, people living with disabilities, and older people receiving income support.
- Access to private rental for low-income households can, however, be improved by limiting risk factors. Factors that may be perceived as limiting risks to the landlord and/or property manager include: local experience; available social and/or financial supports; financial responsibility; a preference for long-term rental and/or preparedness to agree to specific conditions of contract.
- Low vacancy rates are a fundamental parameter in the current market. Low-cost private rental housing is in short supply, and low-income households are currently not competitive at the moment of allocation.

*This bulletin is based on research by **Dr Patricia Short, Dr Tim Seelig, Dr Clive Warren, Connie Susilawati and Alice Thompson** of the AHURI Queensland Research Centre. The research explored risk assessment practices used in the selection and allocation of tenants in the private rental market with a focus on the impact of these practices on low-income renters.*

CONTEXT

The study builds on previous research demonstrating that a relatively large proportion of low-cost private rental accommodation is occupied by moderate- to high-income households, thus locking out many low-income renters. This is occurring in an environment of: reduced funding for public housing; restricted eligibility for rent assistance; reduced 'supply' due to factors such as loss of low-cost rental stock through upgrading and/or transfer to owner-occupied housing; and patterns of supply/demand driven largely by middle- to high-income owner-investors and renters.

RESEARCH METHOD

In formulating a way of approaching the analysis of 'risk-assessment' in rental housing management, the private rental market was viewed as a social institution and the research strategy was informed by institutional ethnography as a method of enquiry. Six local areas across metropolitan and regional Queensland, New South Wales and South Australia were selected as case study localities.

Initial interviews (face-to-face or telephone) were conducted with representatives from Real Estate Institutes in the three states with the purpose of documenting formal 'industry perspectives' on perceived risks, risk assessment and risk management, and to obtain industry-level understanding of variations in rental markets across localities or regions. Tenant advocates and community-housing managers were also consulted as key informants to provide information about local rental housing conditions, and the movements of low-income households into, around and away from local rental markets. Their views were considered to be of particular relevance for understanding how risks associated directly with low-income status in the private rental sector might be affecting vulnerable population groups.

The main body of research data was collected through 29 interviews with property managers in the six study localities. Interviews were conducted in three distinct steps centred progressively around: (1) describing the real estate agency's system for processing tenancy applications; (2) developing a low-cost rental property profile for the local market; and (3) a realistic scenario wherein participants were asked to 'process' a set of hypothetical tenancy applications.

KEY FINDINGS

Key markers of risk: (in)ability to pay and (in)ability to care

The study identified two principal forms of risk associated with property management: financial risk and risk of

litigation. Certain tenant characteristics and circumstances, summarised in terms of their 'ability to pay' and 'ability to care' for the rented property were the main factors taken into account in assessing risk among applicants for rental housing.

A high level of confidence in an applicant's ability to pay and to care for the property produces a perception of low financial risk (less likelihood of rent arrears, property damage, demands for property improvements), and low risk of litigation (fewer disputes). Signals of (in)ability to pay and/or (in)ability to care for the property are almost always interpreted as markers of high levels of risk. Neither criterion could be said to be a totally objective indicator of risk. Often the quantitative nature of the principal indicator of a 30 per cent (or lower) rent-to-income ratio, and the formalised nature of the process of application, mask the range of informal and intuitive assessments of risk that property managers typically describe as 'gut feelings'.

Risk assessment strategies

Four key strategies of risk assessment and avoidance of unsuitable tenants were revealed and categorised as 'sorting', 'ranking', 'discriminating' and 'handing over' responsibility for decision making.

'Sorting' might be seen as a first strategy of exclusion whereby those applicants who fail to meet the primary selection tests of ability to pay (measured against the 30 per cent benchmark and prior records of rent payments/arrears) and ability to care for the property (measured by prior records of property maintenance and bond return/damage) will not be considered eligible for follow-up, and their applications may not go beyond this initial stage of selection.

'Ranking' is a complex process of comparing tenant applications while taking into account factors perceived to be potential risks to business profitability, legal compliance, and conditions of insurance. A mix of formalised, routine practices and personal strategies is employed in the process of ranking applicants to estimate potential risk. Ranking is explicitly a competitive process, and competition among applicants in the private rental market is highly visible. It is this visibility of competition that enables property managers to say, "Sorry, you were not successful" to all but the 'most suitable' applicant, and generally without question.

'Discrimination' is implicit in both 'sorting' and 'ranking', and property managers are acutely aware of the possibility that they may be accused of discriminating unlawfully in rejecting some applicants. The tension between lawful and unlawful discrimination is palpable in the talk of property managers but discriminating between more or less suitable tenants is considered essential to

the processes of selection and allocation if profitable and sustainable tenancies are to be achieved.

'Handing over' responsibility for making decisions about tenant selection is a fail-safe strategy. It is largely a response to the challenge of discriminating between applicants, and is evident in two particular forms: first, all property managers commonly use what can be called the 'owner's decision loophole'. This works to shift the actual responsibility for selection of tenants from the property manager to the owner, who has no obligation to provide a reason for rejecting an applicant. Secondly, most property managers adopt a 'we are not social workers' stance, which works to effectively hand over unsuitable tenants to the public or community housing sector, or informal family support.

Identifying the 'most suitable tenant'

The 'most suitable tenant' is typified by property managers as being resourceful, having adequate financial resources, reputable and capable, possessing appropriate social capital (including appropriate references), having an understanding of what is entailed in applying for tenancy in the private rental market, and demonstrating an ability to care for the rental property. Other factors that reflect positively upon the applicant at the time of allocation include having all relevant documents available, offering to pay rent in advance or accept special conditions of tenancy, and presenting oneself appropriately.

Beyond expecting that applicants will have adequate income to pay rent, property managers expressed expectations that tenants demonstrate that they are capable of managing their financial resources effectively, and conducting themselves in a way that presents no risks of damage to the property or annoyance to neighbours.

Risk associated with low-income status

Property managers articulated concern about risks entailed in the following factors associated with low-income applicants:

- unemployment and the associated uncertainty about the level and stability of income;
- the presence of children in the household (perceived as causing more wear and tear, and potential damage to the property);
- experience of domestic violence and the perceived ongoing potential for damage to property;
- marital breakdown (and associated instability);
- Aboriginality and ethnicity, particularly in relation to family size, cultural practices and housekeeping;
- physical incapacity; and
- a shift from home ownership to private rental, heightened in the absence of a recent rental history.

While it would be unlawful to refuse an application and/or to not offer a tenancy on the basis of sex, marital

status, parental status, pregnancy, race, disability, age, religion, or any other characteristic noted in federal anti-discrimination legislation, the financial vulnerability of low-income applicants can be invoked. This may be expressed as a concern about their compromised capacity to manage income and/or care for the property and cited as legitimate grounds for rejection or a lower ranking in the process of tenant selection.

POLICY IMPLICATIONS

Increasing and redesigning Commonwealth Rent Assistance

In the assessment of income in the tenancy application process, Commonwealth Rent Assistance (CRA) is usually treated as a housing supplement, not income, for the purpose of establishing whether applicants meet the 30 per cent benchmark. Thus for low-income households, while CRA may effectively improve the income-to-rent ratio once housed, the fact that it is not usually considered when assessing applications for private rental means it may not benefit a tenant in the application process. Alternative ways of delivering CRA warrant investigation. Extending the eligibility for CRA to low-wage households might also be considered.

In light of recent rent increases across the market, there is concern that CRA payments have not kept pace. This indicates a need for reassessment of the level of CRA provided to private renters, taking account of real rent costs in the relevant local market.

Building applicant capacity

Vulnerable applicants may benefit by having a better understanding of what is involved in applying for private rental and what factors and skills may increase their chances of being successful in accessing private rental. The role of tenant advocate/liaison services could be extended and strengthened to include activities aimed at building applicant capacity in the application process, including providing a better understanding of assessment and allocation processes. Providing information comparable to the level and type of information provided on entering a public housing tenancy may improve some households' chances of securing private rental.

Enhancing reputations

Liaison and advocacy services and transitional housing providers assisting an applicant with or strengthening the range and content of their documentation is also likely to have some benefits for low-income and/or high-needs households. The establishment of ongoing relationships between these same services and local real estate agencies would also appear to serve applicants well in assessment and allocation processes.

One successful approach is the use of head-leasing arrangements wherein community agencies lease a rental property for sub-letting to tenants with a poor rental history or reputation. There is some evidence in the present study that in cases where community agencies build a 'good reputation', enabling profitable and sustainable lettings and/or where they are providing services to particular groups (for example, recent arrivals), the reputation of the organisation constitutes a significant foundation for members of the client group to establish 'reputable' rental histories for themselves.

Tenancy support programs

Rental guarantee programs such as the one being piloted in New South Wales have the potential to lower the perceived level of risk associated with low income and related vulnerabilities, and assist in the maintenance of tenancies in private rental markets. Similarly, the Private Rental Liaison Officer (PRLO) program, an initiative of Housing SA (South Australia) has been successful in assisting tenants to access and maintain private rental and could be used as a model in other jurisdictions.

Governance of landlords

Exploring further regulation of landlords' behaviour and involvement in the selection and allocation process warrants consideration in relation to the impact on vulnerable households, particularly in tenant selection. Requirements for landlord education and training linked to registration of landlords, and tighter regulation of investment strategies that rely heavily upon rental income to service debts, would seem to warrant further exploration as mechanisms to promote landlords as more visible and responsible actors in residential tenancies.

Increasing the supply of low-rent housing/ landlords' interests

The greater the supply of low-rent housing available to low-income households, the better able the market would be to provide for this group. Past research suggests a number of avenues to address supply issues in the private rental market, including: expanding the secondary rental market through head leasing through social landlords; increasing the supply through the

social housing sector; and supplementing low-income housing through the private rental market through low-rent housing investment incentives such as tax reform. All these seem viable in light of the findings of this research.

In this study, property managers spoke favourably of their experiences of head leasing arrangements. Property owners' interests are well protected and the property agent's management responsibilities are significantly reduced as a result of management responsibility being transferred to the community organisation.

Other modes of provision involving partnerships of state, community and commercial providers, including smaller-scale investors, may also present as attractive propositions for owner-investors and managers, and could ensure low-income households better access to appropriate and affordable rental housing. While such arrangements were not the subject of enquiry in the present study, there were indications that property managers are open to other modes of provisioning.

FURTHER INFORMATION

This bulletin is based on AHURI project 20346, *Risk assessment practices in the private rental market: implications for low-income renters*.

Reports from this project can be found on the AHURI website: www.ahuri.edu.au

The following documents are available:

- Positioning Paper
- Final Report

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



Australian Housing and Urban Research Institute

www.ahuri.edu

HEAD OFFICE Level 1, 114 Flinders Street Melbourne Victoria 3000 TELEPHONE +61 3 9660 2300
FACSIMILE +61 3 9663 5488 EMAIL information@ahuri.edu.au WEB www.ahuri.edu.au

ACKNOWLEDGMENTS This material was produced with funding from Australian Government and the Australian States and Territories, AHURI Ltd 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.

DISCLAIMER The opinions in this publication reflect the results of a research study and do not necessarily reflect the views of AHURI Ltd, its Board or its funding organisations. No responsibility is accepted by AHURI Ltd or its Board or its funders for the accuracy or omission of any statement, opinion, advice or information in this publication.