Final Report

Operating deficits and public housing: policy options for reversing the trend: 2005/06 update

authored by

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for the

Australian Housing and Urban Research Institute

RMIT-NATSEM Research Centre

October 2007

AHURI Final Report No. 106

ISSN: 1834-7223

ISBN: 1 921201 71 1

Australian Housing and Urban Research Institute

ACKNOWLEDGEMENTS

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.

AHURI comprises a network of fourteen universities clustered into seven Research Centres across Australia. Research Centre contributions, both financial and in-kind, have made the completion of this report possible.

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EXECUTIVE SUMMARY

Government-assisted or sponsored public housing represents a key component of affordable housing in Australia, yet at end of the 2005/06 financial year the total stock of public housing has again fallen well below that which applied in 2000/01. The erosion of the level of public housing stock over this period is similar to that which occurring over the previous five-year period, recorded in our 2004 report, *"Operating Deficits and Public Housing: Policy Options for Reversing the Trend"*.

A key constraint on the continued provision of mainstream public housing in Australia is that the net incomes after rebates received by housing authorities should at least pay for their operational costs (net of interest paid or received). If this is not the case, any addition to stock expands the funding required to pay for the growing deficit. If funding is not forthcoming, the only option for reducing or freezing the additional funding requirement is to sell stock and therefore reduce the number of households provided with longer-term assistance (Donald, 2001). The evidence is now mounting that it is this latter scenario that is happening.

The rate at which these deficits are growing, and the time at which deficits outstrip current real levels of grant funding, are matters of critical policy concern.

The 2004 Report was based on information up to and including the 2000/01 financial year. Consequently, that report is now five years out of date. Mindful of the difficult issues facing public housing in Australia, and in need of more current information on operating deficits, the Housing Ministers Advisory Committee (HMAC) requested that AHURI seek cooperation from the authors to update the 2004 report.

Research aims and objectives

This project examines the trends in the financial performance of the eight state and territory housing authorities (STHAs) between 2001/02 and 2005/06, and compares these trends with those analysed in our earlier research. The report examines the similarities and differences between trends in the current period and those applying to the 2004 report, and discusses the reasons for these similarities or changes.

Aims

The aims of the project are to:

- clarify the impact of public housing operating deficits on the activities of STHAs for the period 2001/02 to 2005/06 and compare these outcomes with the analysis in the 2004 report;
- document STHAs views on the policy options available to reverse the current real underlying trend to growing operating deficits.

This report sets out:

- a quantitative analysis of the trends in the main components of these deficits and the rate at which the various components are increasing or decreasing;
- the reasons for the development of these deficits and whether or not they are long-term structural outcomes or medium-term results which may revert at some point in the future.

Public housing trends

Over the decade between 1990/91 and 2000/01, total real capital funding for public housing in Australia fell by 25 per cent. Furthermore, the Productivity Commission's latest report (2006, p. 16.12) on housing indicates that total real Commonwealth State

Housing Agreement (CSHA) expenditure from all sources has fallen in real terms by 30 per cent since 1995/96.

The total stock of public and community sector housing in Australia rose to a peak of around 382,000 dwellings (net of head-leasing and intra-governmental transfers) in 1996/7, thereafter declining to around 375,000 dwellings in 2000/01. Between 2000/01 and 2005/06 there has been a further loss of 10,100 dwellings.

With the introduction of the 1995/96 CSHA, the Commonwealth Government placed considerably greater priority on ensuring that new public and community housing allocations were targeted to those most in need (i.e. experiencing the lowest incomes or in dire or emergency situations and/or both). Many STHAs responded by introducing segmented waiting lists whereby 'priority applicants' received first call on available allocations. In consequence, from 1990/91 to 2000/01 in Australia:

- the proportion of public tenancies on rebated rents rose from 78 per cent to 88 per cent
- the proportion of new tenancies allocated to priority recipients rose from 17 per cent to 49 per cent of new tenancies.

From 2000/01 to 2005/06, the proportion of public tenancies on rebated rents has fallen marginally to 87.3 per cent, as has the proportion of new tenancies allocated to priority recipients (down to 41.8 per cent).

The research process

The 2004 project encompassed all Australian states and territories. In this study a process was established that:

- determined appropriate definitions for establishing operating deficits;
- clarified and finalised the component research questions;
- reviewed and finalised the questionnaire used for the Chief Financial Officer (CFOs) interviews.

The HMAC agreed that this study would use the same definitions, line items and units of analysis as the 2004 study.

All STHAs in Australia provided spreadsheets for the period 2001/02 to 2005/06 inclusive. These spreadsheets are consistent with the previous analysis.

All the per unit outcomes were adjusted by the average Consumer Price Index (CPI) for all capital cities for Australia to bring all revenues and costs to 'real' June 2005/06 dollars. All the financial data from the 2004 report were also adjusted to June 2006 dollars.

These quantitative outcomes were supported by a questionnaire returned by the Chief Financial Officer for all housing authorities in Australia. This questionnaire is the same as that used in the 2004 report.

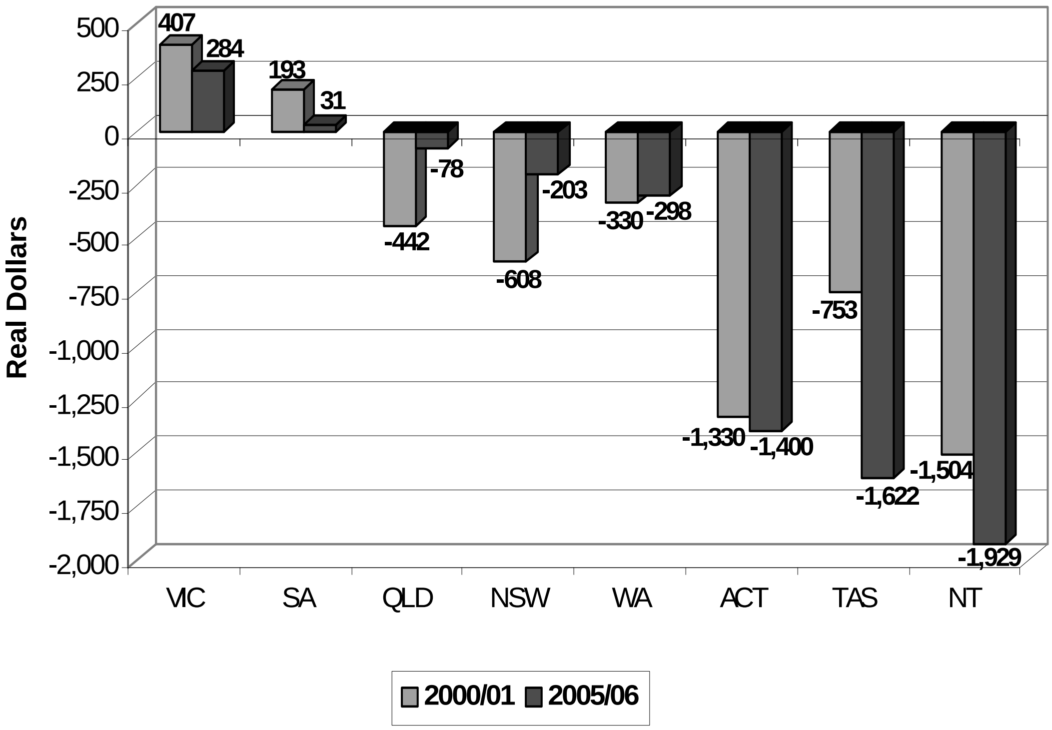
Key research findings

In general, the 1990s saw all the housing authorities move from small or moderate operating surpluses into deficits. Real rental, and total income, per dwelling remained either flat or declined for six of the nine housing authorities, and the rate of growth of real income for the remaining three authorities has been significantly slower than the rate of growth of real net expenditure.

Real net expenditure per dwelling unit grew rapidly for all authorities except Tasmania and Victoria. As a result, operating outcomes declined markedly.

In 1990/91 all STHAs except one were in surplus. However, as Figure 1.1 indicates, in 2000/01 only Victoria and South Australia were in that position. Since 2000/01, in real terms the operating deficits per dwelling improved in only three states: Western Australia, Queensland and New South Wales. The improvement in Western Australia was only marginal. In five states the operating positions continued to deteriorate and only one state, Victoria, has anything other than a marginal surplus. In both Tasmania and the Northern Territory the deterioration has been substantial.

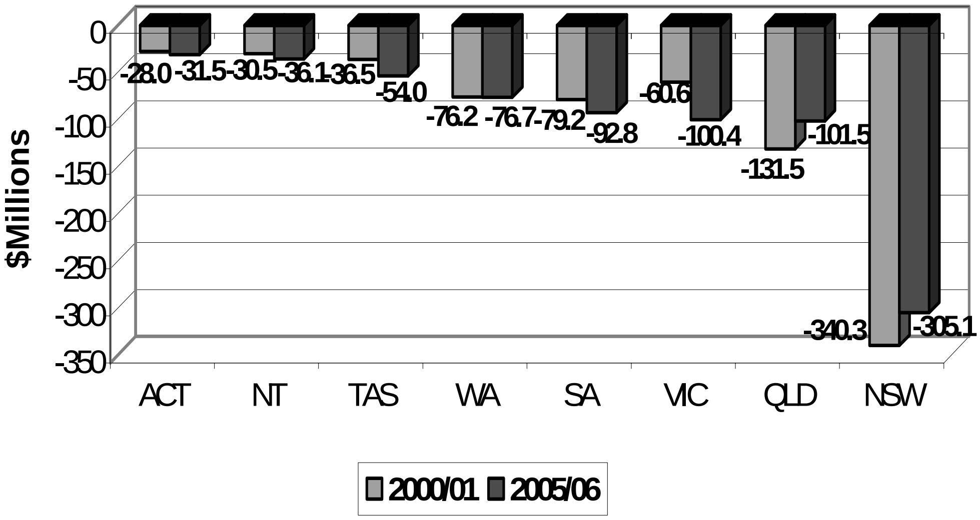
Figure 1.1: Real operating surpluses/deficits per dwelling, 2000/01 and 2005/06 (excluding interest and depreciation), all state and territory housing authorities (June 2006 dollars)



* Leasing expenses are excluded from the analysis to enable the 2005/06 comparisons across states and territories, and comparison with the 2000/01 analysis. In Victoria this excludes $12.9 million of leasing expenses from the total annual operating surplus/deficit. For the same reason (i.e. to enable comparisons), provisioning for bad debts has been excluded, though bad debts actually incurred have been included.

Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; returned spreadsheets of STHAs to the 2005/06 Operating Deficits Project

Figure 1.2: Total real operating deficits ($m) including interest and depreciation, all state and territory housing authorities, 2000/01 and 2005/06 (June 2006 dollars)

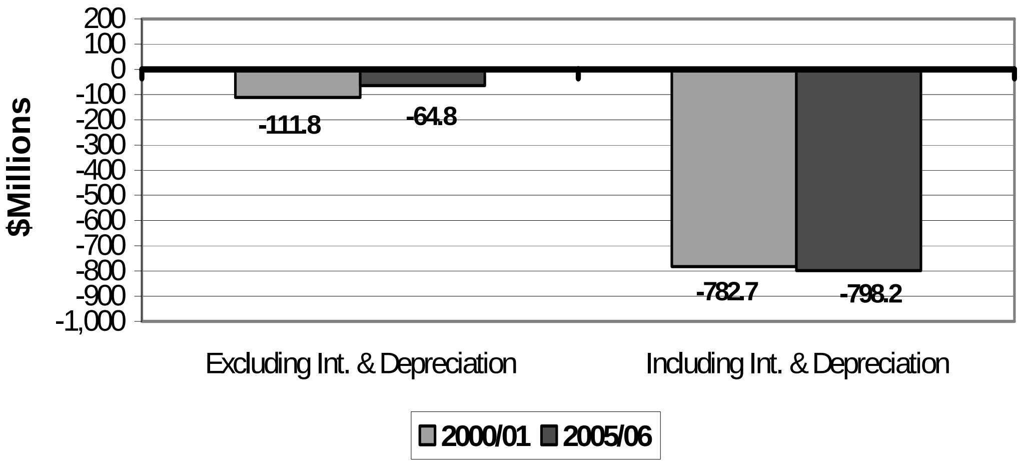


Sources: Hall J and Berry M, 2004, Operating Deficits and Public Housing, Policy Options For Reversing The Trend, AHURI; returned spreadsheets of STHAs to the 2005/06 Operating Deficits Project

After adding in net interest and depreciation the position worsens, improving in only two states (Queensland and New South Wales). The deterioration was marginal in Western Australia, moderate in both the ACT and the Northern Territory, and substantial in Tasmania, South Australia and Victoria.

Figure 1.3 shows that for all STHAs, the current operating deficits after net interest and depreciation ($798.2 m) substantially exceed the total of the base grant to STHAs under the current CSHA ($725.2 m)[1]. Whilst the graph suggests that the overall position has not deteriorated, this is entirely due to the improvements in Queensland and New South Wales.

Figure 1.3: Total real operating deficits ($m), all state and territory housing authorities in Australia, 2000/01 and 2005/06 (June 2006 dollars)

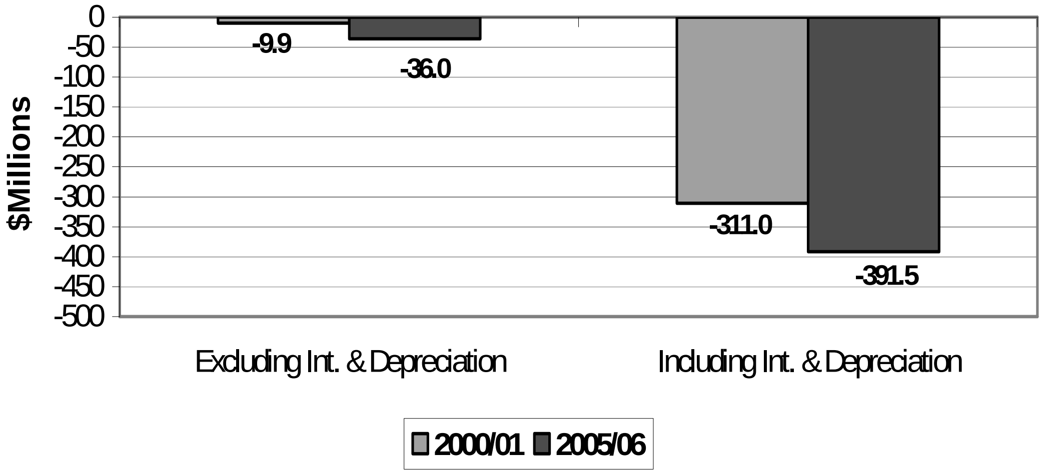


Sources: Hall J and Berry M, 2004, Operating Deficits and Public Housing, Policy Options For Reversing The Trend, AHURI; returned spreadsheets of STHAs to the 2005/06 Operating Deficits Project

[1] Productivity Commission of Australia, 2006, *Report on Government Services*, 2006, p. 16.17

Figure 1.4 shows that operating deficits continued to deteriorate once Queensland and New South Wales are excluded. This deterioration in the other six states has been dramatic, with deficits after net interest and depreciation growing by more than 25 per cent.

Figure 1.4: Total real operating deficits ($m), all state and territory housing authorities excluding Queensland and New South Wales, 2000/01 and 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, Operating Deficits and Public Housing, Policy Options For Reversing The Trend, AHURI; returned spreadsheets of STHAs to the 2005/06 Operating Deficits Project

What are the drivers?

Targeting and income growth

The 2004 report outlined how, on the income side, the weakening position appears to be mainly due to the effects of policy changes resulting in tighter targeting of public stock directed to low-income households and those with multiple support needs.

The report noted that there is an almost perfect negative correlation between the rate of net income growth experienced by a housing authority and the rate of growth in the proportion of its tenants who are rebated and/or receiving priority allocations.

As at 2000/01 it appeared that the process of tighter targeting had yet to fully run its course and that, in the foreseeable future, reductions in net income per dwelling would accelerate.

These predictions did not eventuate, for two main reasons:

- The movement to greater proportions of rebated tenants and priority allocations appears to have levelled out. The majority of public housing authorities may be developing 'mature' portfolios where the loss of income associated with the replacement of a non-rebated tenant with a rebated tenant may be matched by income growth in existing longstanding tenancies. If this is the case then it can be expected that real rent revenues will stop declining and at least stabilise for the foreseeable future.
- Seven of the eight STHAs carried out significant upward adjustments to their rent-charging policies, increasing the proportions of income paid by rebated tenants.

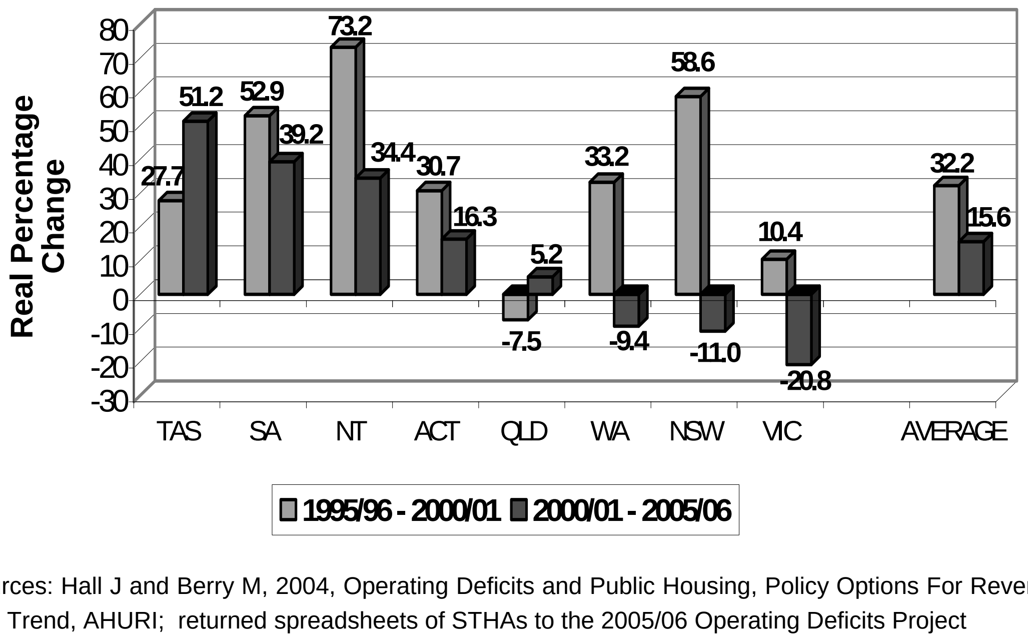
Operating costs continued to grow, but at a slower pace

- *Real expenditure on depreciation* rose, on average, by 44 per cent over the period 1995/96 to 2000/01 but has since moderated to an average of 21.2 per cent for the period 2000/01 to 2005/06.
- *Real expenditure on maintenance* rose by 30 per cent in the period 2000/01 to 2005/06, double the rate of the period 1995/96 to 2000/01. Real maintenance expenditure grew faster than the CPI for building materials for all authorities other than the ACT, Tasmania and Victoria. Much of the increase in the Northern Territory can be attributed to the unique circumstances applying in that location and the difficulties of obtaining a competitive tender market for building repairs.
- The 2004 report noted that the rapid increase in maintenance expenditure can also be attributed to housing authorities assuming a more proactive and information-rich role in asset management and the development of 'stock audits' throughout Australia. All these processes have, of course, added to costs.
- It was predicted that, as the majority of stock reached acceptable standards, the rate of growth in average maintenance spending per dwelling would decline. However, this has not yet occurred. STHAs continue to focus heavily on asset revitalisation and redevelopment to reduce the potential for future cost blowouts.

Growth in salary, administrative and related costs has moderated

- Costs associated with salaries, administration and related overheads ('Overheads') rose by 32 per cent on average per dwelling in real terms between 1995/96 and 2000/01. Figure 1.5 shows that growth in this expenditure item was greatest in the ACT, the Northen Territory and New South Wales. During that period, overhead expenditure was the fastest-growing cost facing housing authorities in general, exceeding maintenance expenditure in five authorities and exceeding rates expenditure in eight out of the nine authorities examined.
- There is no doubt that a substantial part of the increases in costs has been due to the drive by housing authorities to improve the quality and responsiveness of customer services.

Figure 1.5: Real percentage change in total overhead per dwelling, 1995/96 to 2000/01 and 2000/01 to 2005/06, all state and territory housing authorities



Sources: Hall J and Berry M, 2004, Operating Deficits and Public Housing, Policy Options For Reversing The Trend, AHURI; returned spreadsheets of STHAs to the 2005/06 Operating Deficits Project

- Since 2000/01 the average real expenditure has grown by 15 per cent, due entirely to increases in the smaller states.
- STHAs have generally sought to rein in overhead expenditure in the period 2000/01 to 2005/06, and in the three largest states maintenance has taken over as the largest single component of operating expenditures before net interest and depreciation. However, the rate of growth of overhead expenditure is still unreasonably high in three STHAs (Tasmania, South Australia and Northern Territory).
- The impact of non-housing support services on operating expenditures has been the subject of debate among housing professionals. At least half the STHAs have now attempted to estimate the cost of these services. The consensus view of the STHA respondents to this project is that non-housing support services add between 5 per cent and 10 per cent to total overheads.
- Total overhead expenditure averaged 43 per cent of operational expenditure for all STHAs, so a conservative estimate is that non-housing support services cost about 4.3 per cent of total operational expenditure before interest and depreciation. If this is a representative outcome, then these costs are significant. Put another way, 10 per cent of overhead costs equates to 4.9 per cent of rents after rebates, across Australia. This is more than two-thirds of the 6 per cent of the gross rents amount that private sector residential managers commonly receive for their services.
- Conversely, the impact of borrowing costs has not been a cost driver. The interest cost paid per dwelling fell, on average, by 44 per cent during the period. Only in Western Australia did this expenditure item increase.

Backlogs appear to have worsened slightly

The 2004 report noted that greater flexibility and more active asset management regimes introduced by the housing authorities during the 1990s has resulted in the gradual selling off or restructuring of public housing stock.

It appears that the demand for asset revitalisation is growing only slowly. The current STHA estimate totals $1.3 billion and will require continued, moderate applications of capital for the next few years.

Over the period 2000/01 to 2005/06, and at a conservative replacement estimate of $250,000 per dwelling, the stock liquidation of 10,100 dwellings has wiped about $2.5 billion from the asset base of STHAs.

Most STHAs have advised that because of the squeeze on operations, the strategy has been to heavily invest grants in asset and estate revitalisation; and because grants have been inadequate, proceeds from the sale of older and inappropriate stock have been applied to both debt repatriation and asset revitalisation.

An option for reversing the trend

As noted in the 2004 report, an obvious alternative to the slow selling off of the public housing stock to shore up a weak financial position is for the community service obligation to be recognised and separately funded by government (as is now the case in New Zealand).

The argument presented in the 2004 report is as follows:

- In all other corporatised government services the difference between the commercial price and the amount paid by the recipient of a concession is recognised as a community service obligation (CSO) and is fully funded. For example, for electricity and water supply, the difference between the price per unit of consumption and the amount charged to concessional consumers is treated as a CSO and is normally provided as a Treasury payment to the authority concerned.

- 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 is the cost of the difference (i.e. the rental rebate).
- There is, in principle, no distinguishing or special reason why the principle applying to CSOs in other corporatised government organisations should not be applied to public housing authorities and the CSO (rebates) fully funded by government.

The conclusions set out in the 2004 report are still valid for six of the eight STHAs.

Figure 1.6: Real operating surpluses/deficits per dwelling (including net interest and depreciation) if rebates fully funded, 2005/06 (June 2006 dollars), all state and territory housing authorities

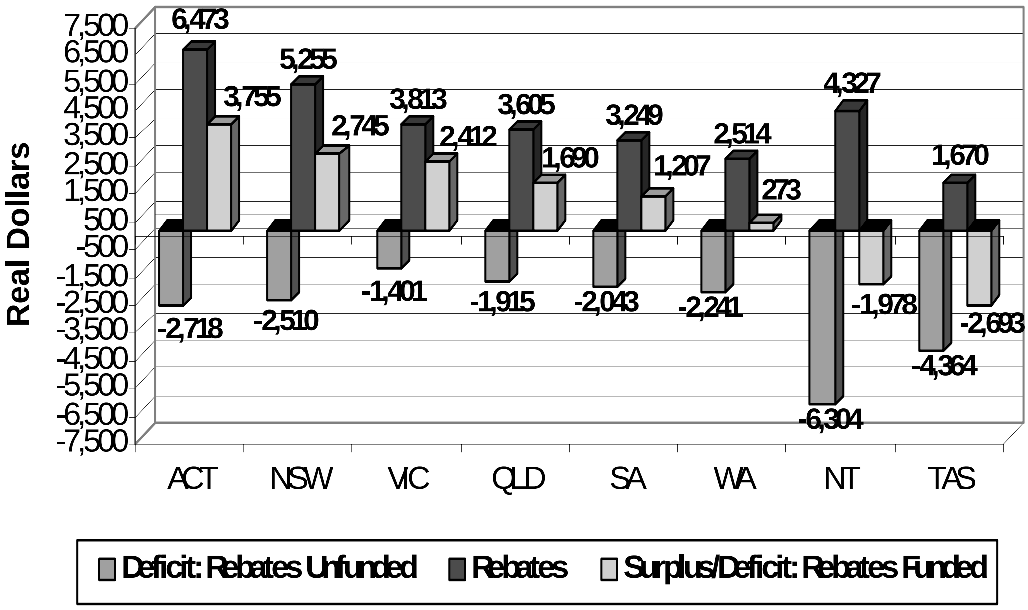


Figure 1.6 demonstrates that if the difference between market rent and concessional (rebated) rents was funded, the financial situation of the housing authorities would be placed on a commercially sound basis. *Funding the rebate would not only eliminate deficits in all authorities except the Northern Territory and Tasmania, but it would also provide a basis for longer-term financial stability for housing authorities.*

It will not be sufficient for housing authorities to eliminate current deficits. If deficits are not to worsen, housing authorities must also achieve some real net income growth.

Our analysis of rebate growth indicates that, for almost all housing authorities, market rents grow in real terms at about the same rate as average weekly earnings (AWE) (i.e. at around or just less than 1 per cent above inflation). It can be anticipated that a financial solution based on fully funding the rebate will enable net incomes to at least keep pace with efficiently managed cost structures.

Some system options

We conclude that, based on the analysis in this study, if the current policy focus is maintained, Australian public housing will not remain viable. While STHAs have made major efforts to improve revenues and reduce unnecessary expenditure, for all except two agencies the operating position has continued to deteriorate (after net interest and depreciation). For the two that have improved, the revenue gain from increasing rents is unlikely to be repeatable. *It is difficult to see how the revenue effort pursued by the majority of STHAs could be substantially improved upon. The drive towards expenditure efficiency has also been sustained, and any further gains in this area are likely to be modest.*

In the future, if the affordability benchmark of 25 per cent of assessable income in rent is maintained, changes to rent charging will not be an available tool to relieve growing deficits. Even if real revenue decline is arrested, the best that STHAs can hope for is that net income keeps pace with inflation. In addition, continuing to seek improvements in housing stock and continuous improvements in client services cannot be achieved without an acceleration in the rate of real cost increases. In a context where:

1. the funding of public housing is disconnected from its community service obligations,
2. the affordability benchmark of 25 per cent of assessable income is maintained, and
3. the emphasis on continuous service improvement is enforced

then incomes per unit will only stay stable, real expenditures per unit will increase and operating deficits will continue to grow.

Future directions

The 2004 report made a number of suggestions, as set out below.

> On the basis of the study findings, summarised above, the following implications for policy are suggested;
>
> 1. A Working Party of Commonwealth and State Housing Officials be established to:
>
> → examine ways in which the CSO experienced by Australian Housing Authorities can be fully funded (i.e. the difference between market and income related rents), including changes to current funding arrangements;
>
> → prepare detailed forecasts of the likely Net Income of all Australian Housing Authorities given no change to targeting policy;
>
> → examine other options by which Net Incomes for Housing Authorities can grow in real terms, including;
>
> - → relaxation of affordability benchmarks and abolition of current Productivity Commission targeting indicators;
> - → abandonment of current targeting policies;
> - → growing the housing stock to diversify the income base;
> - → other relevant options.
>
> 2. A similar mechanism could be used to examine in detail the current Productivity Commission efficiency indicators with a view to developing a financial reporting system which makes more transparent the trends in the operations of public housing authorities, building upon the method and definitions used in this study.

3. In the absence of any changes to Commonwealth policy, Australian State Housing Authorities could establish an in-depth investigation of the quality and extent of services that existing public housing authorities can afford and, if necessary, seek abolition of the Productivity Commission continuous improvement indicators and replacement by independent service standards;
4. For many expenditure items there was great variability between Housing Authorities. A more detailed analysis of the lowest cost authorities could be instituted to establish how these positive outcomes have been achieved and how the other authorities could benefit from the resulting efficiencies.
5. A working party of Commonwealth and State Chief Financial Officers and State Treasury Officials could examine and develop alternatives to the current treatment of Depreciation in Public Housing Authorities.

With the exception of the examination of the second point in suggestion 1, these suggestions remain valid.

In response to questions about the way forward, the overwhelming response from STHAs was:

1. fund the CSO; and
2. develop client profiles with a much higher proportion of households in receipt of incomes sourced from other than pension and benefits.

Another option would be for the Australian government to fund the operating deficits and require state matching funds to be applied to asset revitalisation and new construction. This option would not necessitate any change to targeting but would impose a considerably higher cost than Option 1.

If public housing is to remain viable and vibrant, the structure of financial support for public housing in Australia requires fundamental reform, whatever combination of options is pursued.

1 INTRODUCTION

1.1 Background

Government-assisted or sponsored public housing represents a key component of affordable housing in Australia, yet at end of the 2005/06 financial year the total stock of public housing has again fallen well below that which applied in 2000/01. The erosion in the level of public housing stock over this period is similar to that which occurred over the previous five-year period, recorded in our 2004 report, *"Operating Deficits and Public Housing: Policy Options for Reversing the Trend"*.

A key constraint on the continued provision of mainstream public housing in Australia is that the net incomes after rebates received by housing authorities should at least pay for their operational costs (net of interest paid or received). If this is not the case, any addition to stock expands the funding required to pay for the growing deficit. If funding is not forthcoming, the only option for reducing or freezing the additional funding requirement is to sell stock and therefore reduce the number of households provided with longer-term assistance (Donald, 2001). The evidence is now mounting that it is this latter scenario that is happening.

The rate at which these deficits are growing, and the time at which deficits outstrip current real levels of grant funding are matters of critical policy concern.

The 2004 report was based on information up to and including the 2000/01 financial year. Consequently that report is now five years out of date. Mindful of the difficult issues facing public housing in Australia, and in need of more current information on operating deficits, the Housing Ministers Advisory Committee (HMAC) requested that AHURI to seek cooperation from the authors to update the 2004 report.

1.2 Research aims and objectives

This project examines the trends in the financial performance of the eight STHAs, over the period 2001/02 to 2005/06, and compares these trends with those analysed in our earlier research. The report examines similarities and differences in trends between the current period and those applying to the 2004 report and discusses the reasons for any similarities or changes.

1.2.1 Aims

The aims of the project are to:

- clarify the impact of public housing operating deficits on the activities of STHAs in the period 2001/02 to 2005/06 and compare these outcomes with the analysis in the 2004 report;
- document STHA views on the policy options available to reverse the current real underlying trend to growing operating deficits.

1.2.2 Objectives

Related objectives are to:

- discuss and document the current public housing operating deficits;
- quantify trends in, and current levels of, the component line items that make up these deficits;
- elaborate on the reasons for the development of these deficits.

1.3 Scope of the work and structure of this report

This report sets out to:

- quantitatively analyse the trends in the main components of these deficits and the rate at which the various components are increasing or decreasing;
- identify the reasons for the development of these deficits and whether or not they are long-term structural outcomes or medium-term results that may revert at some point in the future.

Chapter 2 briefly outlines the methodology used for the research, which is identical to that used in the 2004 report and which is set out in detail in Attachment 1.

Chapter 3 discusses the analysis results by state and territory.

Chapter 4 draws out the principal conclusions and observations arising from the analysis and outlines possible directions that would, in light of the detailed research findings, reverse current (or prospective) trends towards growing operating deficits across the jurisdictions.

2 RESEARCH PROCESS AND METHOD

2.1 Research control and management

The 2004 project encompassed all Australian states and territories. In this study a process was established which;

- determined the appropriate definitions for establishing operating deficits;
- clarified and finalised the component research questions; and
- reviewed and finalised the questionnaire that was used for the Chief Financial Officers' (CFOs') interviews.

2.2 Analysis process

The 2004 report determined

- the basis of the construct for the analysis;
- the principles to be applied to the analysis;
- the unit of measurement to be applied to the line item analysis;
- the definitions and core line items to be included in the analysis; and
- the line items that would be added back into the analysis.

The HMAC agreed that this study would use the same definitions, line items and units of analysis as the 2004 study.

2.3 Analysis method and deficits defined

Attachment 1 sets out the agreed method used in the 2004 study, and Attachment 2 contains a list of the key definitions for the line items agreed to.

2.4 Public housing financial data

All STHAs in Australia provided spreadsheets for the period 2001/02 to 2005/06 inclusive. These spreadsheets are consistent with the previous analysis.

2.5 Clarification and unification

The actual amounts of revenue and expenditure for each year are identified in the spreadsheet returns in accordance with the principles, definitions, core items and add-back items agreed to. In this respect the clarification of community housing and its treatment for all authorities was agreed to.

Where community housing is completely off budget, and only supported by a grant or subsidy, then both the dwellings and revenues and costs have been removed from the analysis. Where any part of community housing is on budget, both the dwellings and revenues and expenditures have been included and subjected to any necessary pro rata adjustment.

For head-leased properties, the dwellings have been removed from the unit of measurement analysis and the revenues and costs have been excluded.

Housing authorities were also asked to provide details of the number of tenantable dwellings and all dwellings owned and head-leased for the years 2001/02 to 2005/06, which is consistent with the earlier data. For this reason we are using stock owned and operated but excluding any head-leased dwellings for each year from 1990/91 to 2005/06.

2.6 Quantification process

After obtaining all this information and making all the relevant adjustments, the actual amounts received and spent for the core items were calculated for each year for each STHA. The relevant number of dwellings was also incorporated. These amounts were then divided by the relevant dwelling number to obtain the per unit outcome.

All the per unit outcomes were then adjusted by the average Consumer Price Index (CPI) for all capital cities for Australia to bring all revenues and costs to 'real' June 2005/06 dollars. All the financial data from the 2004 report were also adjusted to June 2006 dollars. Attachment 3 contains a copy of the spreadsheet analysis for a housing authority.

2.7 Questionnaire support

These quantitative outcomes were supported by a questionnaire containing both qualitative and quantitative information returned by the CFO for all housing authorities in Australia. This questionnaire is the same as that used in the 2004 report. A copy of the agreed questionnaire is contained in Attachment 4.

3 ANALYSIS OF RESULTS

In this chapter we set out the detailed financial analysis for each Australian STHA. Comparisons are made between the period 1995/96 to 2000/01 and the period 2000/01 to 2005/06.

In the first instance we examine trends in real Net Rents and Net Incomes, and discuss quantitative factors that may be affecting Net Incomes. Next we examine expenditure priorities and expenditure trends. We look at the proportion of real operating expenditure absorbed by each functional item in 1990/91 and 2005/06. As a final part of the expenditure analysis we trace the real percentage change in the main recurrent expenditure items over the period 1990/91 to 2005/06.

In the subsequent sub-section we document quantitative trends in operating surpluses/deficits and look at the real percentage change in real net rents, operating incomes, expenditures and surpluses/deficits. Subsequent parts of the analysis examine the impact of:

- net interest and depreciation; and
- rebates.

In the 2004 research, the role of recurrent grants in supporting operations was examined. In the current research a number of STHAs were not able to separate the application of grant funds to recurrent and capital expenditure and for this reason the grant component of the previous analysis has not been repeated.

The next two parts of each state-based analysis discuss qualitative issues emerging from responses to our questionnaire. Conclusions are formed about the overall directions in operating deficits for that state or territory.

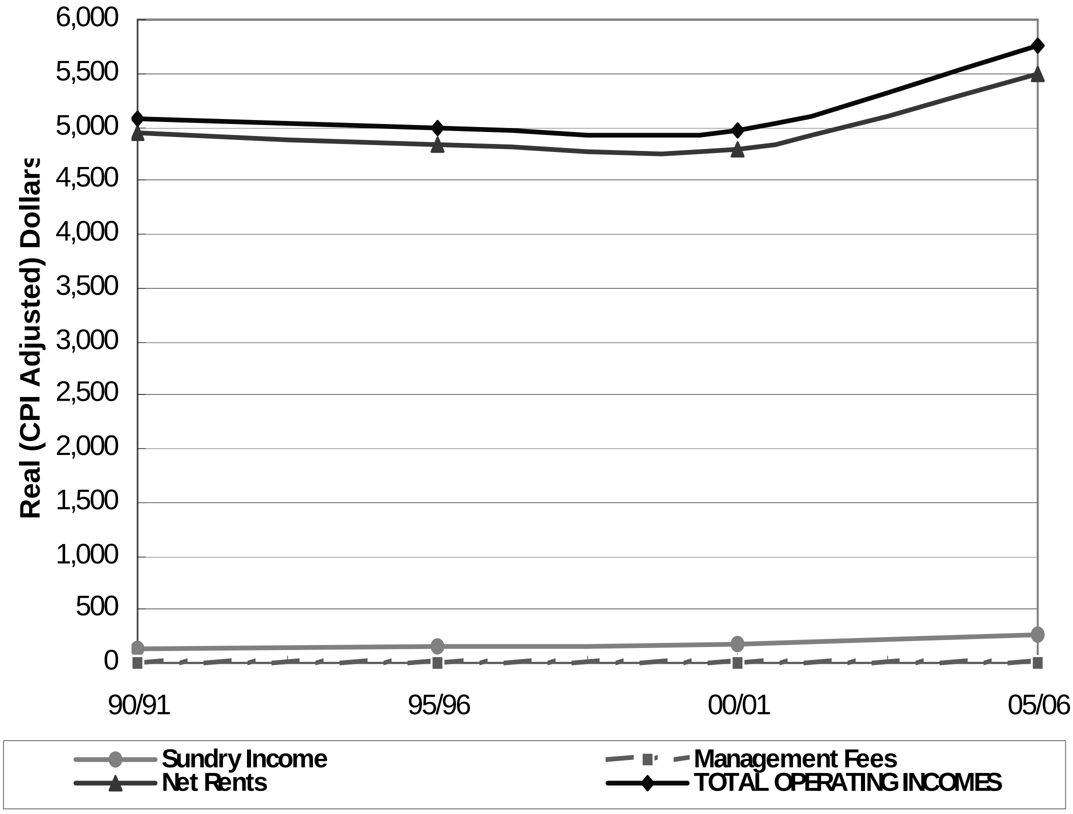
3.1 Australian Capital Territory

3.1.1 Quantitative

Changes in net incomes

Graph 3.1 traces real net income per dwelling unit over the period 1990/91 to 2005/06, in the Australian Capital Territory (ACT).

Graph 3.1: Real income per dwelling unit ($), ACT, 1990/91 to 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from ACT Housing to 2005/06 Operating Deficits Project

Note: Includes public community and Aboriginal housing owned and operated by the ACT but excludes any dwellings head-leased or leased from third parties.

Over the period 1990/91 to 2000/01, operating incomes actually fell in real terms from $5,081 to $4,961 or by $120 per dwelling. Net rents per dwelling fell by about 3 per cent. Since 2000/01 net real incomes have increased by nearly 15 per cent and real rents by 14.7 per cent. Real rents constituted more than 95 per cent of annual operating incomes throughout the 16-year analysis period.

Quantitative factors affecting operating incomes

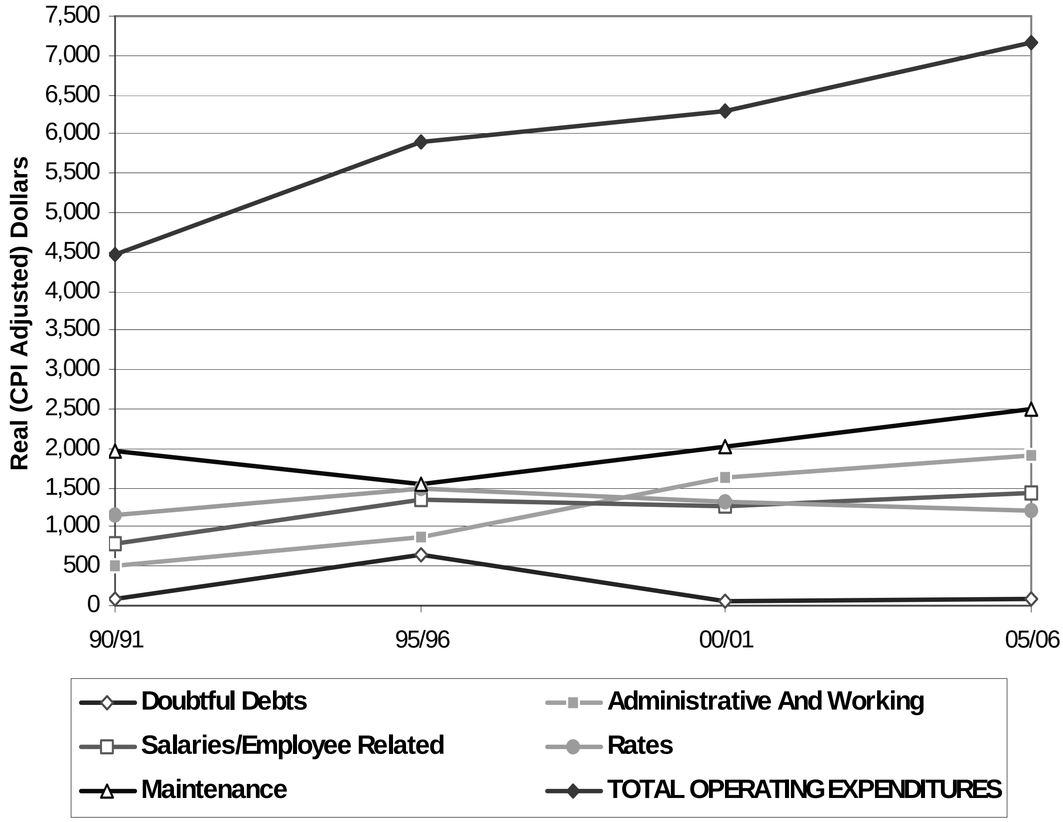
Between 1990/91 and 2000/01, rebated tenants increased from 78 per cent to 83 per cent of the total client households, but far more importantly, priority, crisis and emergency allocations increased from 35 per cent of all new allocations to 80 per cent, the second-highest of all Australian states. These households rely almost entirely on pension and benefit payments.

Since 2000/01, rebated tenants as a proportion of the total have remained almost static, only increasing from 83 per cent to 84 per cent of the total, with allocations to priority crisis and emergency clients increasing from 80 per cent to 96 per cent. Of much greater importance, however, are changes to rent charging. These changes have substantially increased the average net rent per dwelling.

Expenditures and expenditure priorities

Graph 3.2 shows real net expenditure per dwelling unit over the period 1990/91 to 2005/06.

Graph 3.2: Real expenditure per dwelling unit ($), ACT, 1990/91 to 2005/06



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend, AHURI*; and return from ACT Housing to 2005/06 Operating Deficits Project

Graph 3.2 shows that, for the period 1990/91 to 2000/01, real operating expenditures per dwelling increased from $4,458 to $6,292.

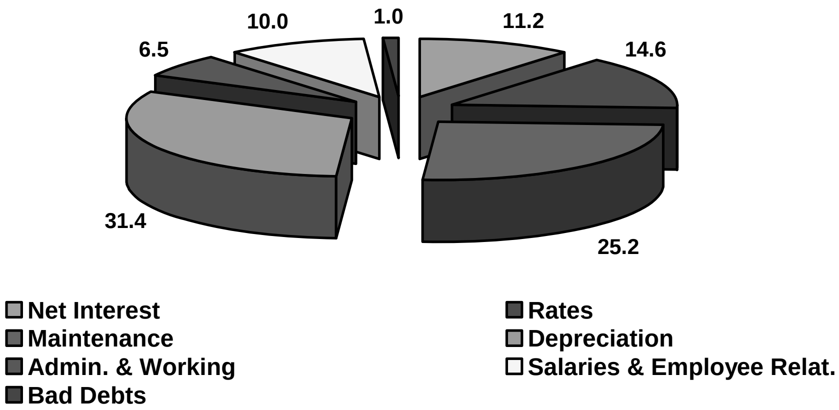
Real increases in rates outgoings increased by 30 per cent in the period 1990/91 to 1995/96, and have declined by 30 per cent in real terms since then. Real increases in maintenance outgoings has been moderate, with maintenance expenditure per dwelling actually decreasing by 20 per cent over the period 1990/91 to 1995/96 and then increasing by 30 per cent up to 2000/01 ($2,021) and again by 24 per cent between 2000/01 and 2005/06 ($2,509).

In the decade between 1990/91 and 2000/01, by far the most significant real increases in expenditure occurred in the 'salaries and employee related' and 'administrative and working' items (total overhead). Total overhead increased in real terms during this period by over 100 per cent from $1,283 to $2,885. Since 2000/01, however, the rate of growth of overhead expenditure substantially reduced, increasing by only 16.3 per cent or just slightly more than the rate of increase in net revenue.

As a result, growth in operating expenditure moderated between 2000/01 and 2005/06, increasing by 13.8 per cent to $7,163 per annum.

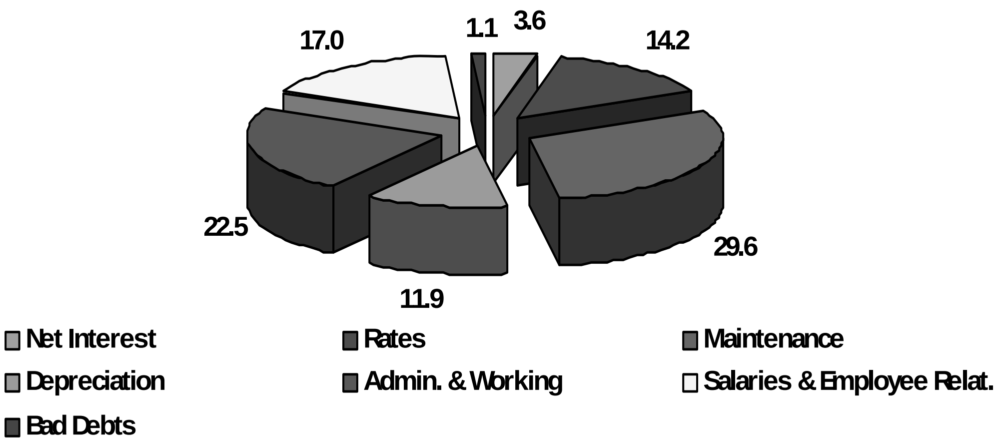
Reflecting these real changes in expenditure items, Graphs 3.3 and 3.4 set out the proportion of total operating expenditure occupied by each of the core expenditure items for the years 1990/91 and 2005/06.

Graph 3.3: Line items: percentage of real total public housing operating expenditure per dwelling (excluding rebates), ACT, 1990/91 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from ACT Housing to 2005/06 Operating Deficits Project

Graph 3.4: Line items: percentage of real total public housing operating expenditure per dwelling (excluding rebates), ACT, 2005/06 (June 2006 dollars)



Source: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from ACT Housing to 2005/06 Operating Deficits Project

The graphs show how the proportion of the ACT's total expenditure per dwelling for each item (including depreciation and net interest, the latter being interest received less interest paid) has changed over the period 1990/91 to 2005/06.

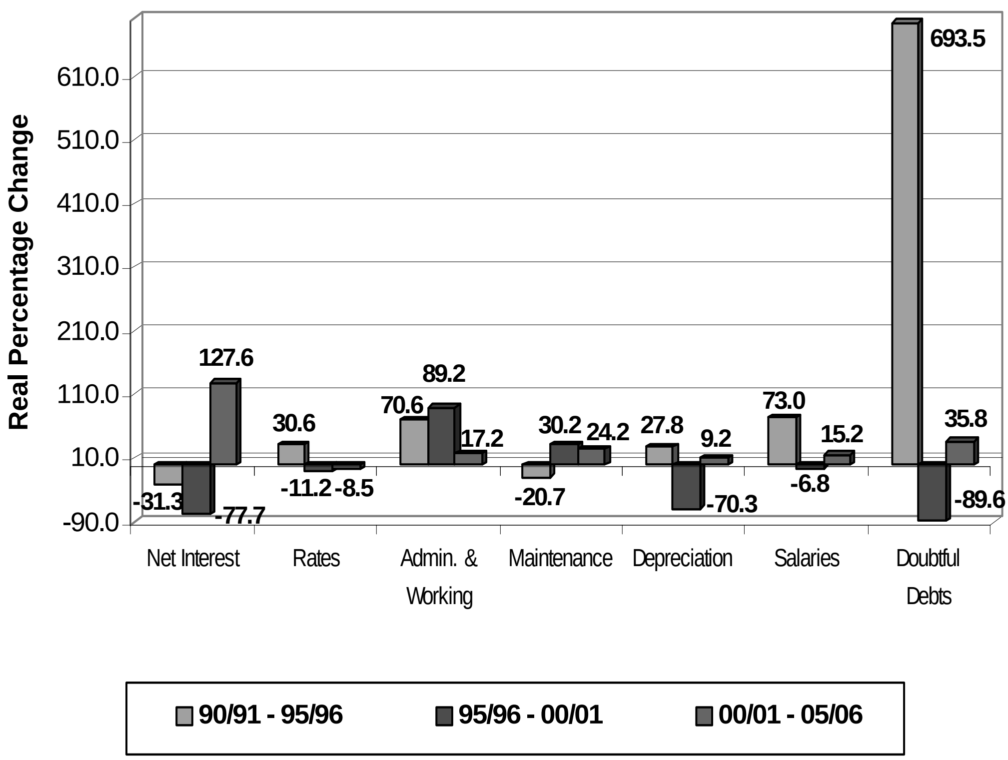
The proportion of total expenditure absorbed by both depreciation (down from 31.4 per cent to 11.9 per cent) and net interest (down from 11.2 per cent to 3.6 per cent) has declined dramatically.

Rates as a proportion of total expenditures has also declined, albeit slightly, from 14.6 per cent to 14.2 per cent while maintenance expenditure has increased slightly, from 25.2 per cent to 29.6 per cent.

As outlined in the analysis of expenditure item growth, by far the greatest change in proportions has occurred in salaries and salary-related expenses, and administrative and working items, for a combined overhead increase from 16.5 per cent to 39.5 per cent.

In 2005/06 total overhead absorbed just slightly less than the combined expenditures of maintenance and rates. Graph 3.5 sets out the real percentage change in the costs of key line items.

Graph 3.5: Real percentage change in key line items, ACT, 1990/91 to 2005/06



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from ACT Housing to 2005/06 Operating Deficits Project

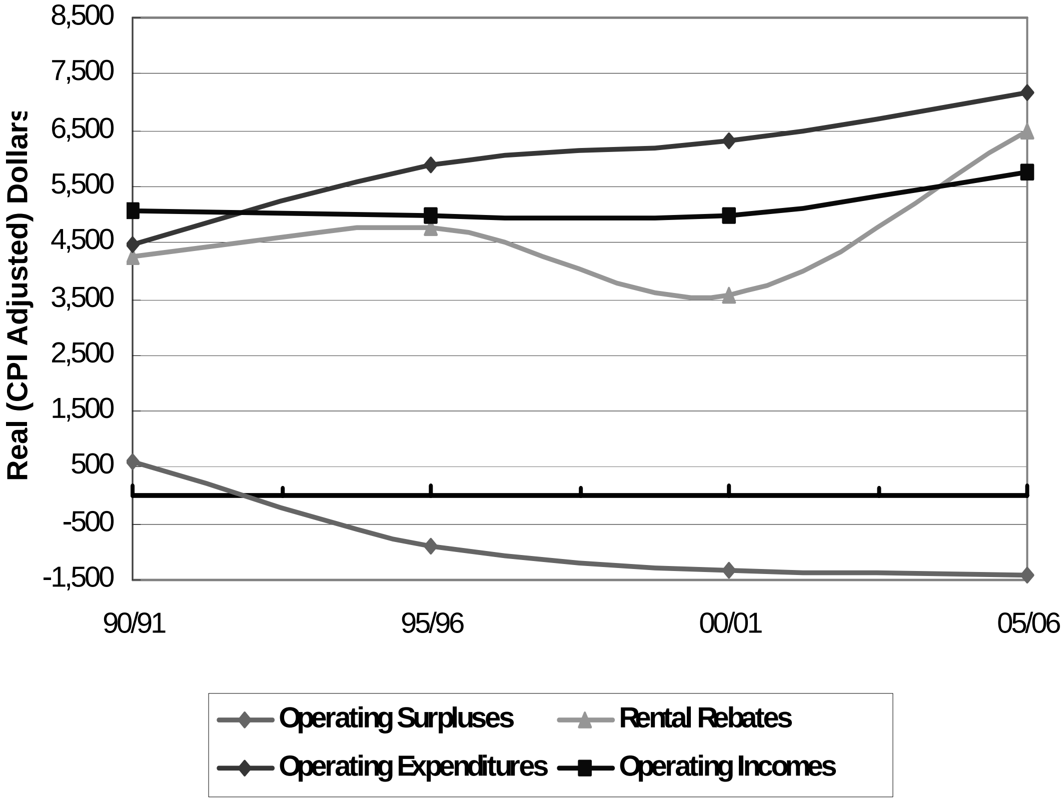
The graph reflects the findings outlined earlier; that over the period 1990/91 to 2000/01, there were very significant real declines in the cost per dwelling for net interest and depreciation, moderate changes in doubtful debts, maintenance and rates, and major real percentage increases in salaries etc, and administration and working.

Since 2000/01 only rates expenditures have declined in real terms. With the exception of net interest, the rate of growth in the other main expenditure items has moderated substantially.

Operating income, expenditure and surplus/deficits

Graph 3.6 sets out the trends in operating surpluses/deficits excluding net interest and depreciation.

Graph 3.6: Real operating surpluses/deficits per dwelling, ACT, 1990/91 to 2005/06 (June 2006 dollars)

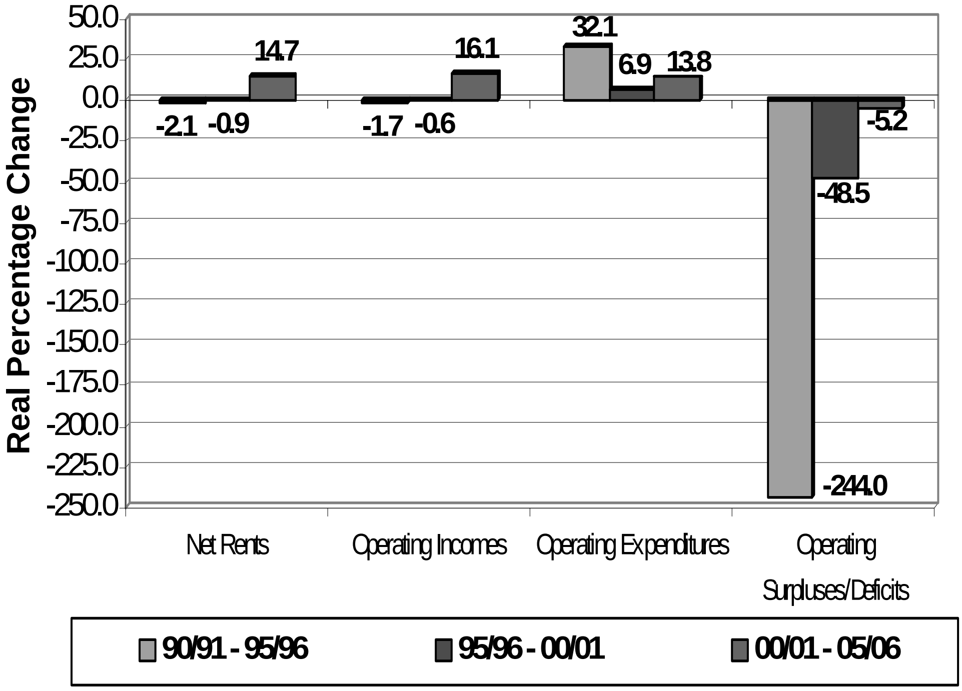


Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from ACT Housing to 2005/06 Operating Deficits Project

In 1990/91 the ACT produced a real surplus per dwelling (excluding net interest and depreciation) of $622, and between 1991/92 and 1993/94 some very small deficits were recorded. By 1995/96 operating deficits had increased dramatically, primarily as a result of real expenditures per dwelling increasing from $4,458 to $5,888, with deficits increasing to –$896 per dwelling. Thereafter, between 1995/96 and 2000/01 deficits again increased significantly to –$1,330.

Between 2000/01 and 2005/06, due to a significant tightening of real expenditure growth and a substantial increase in real income growth, deficits grew by only $65 per dwelling. Graph 3.7 sets out the real percentage change in net rent, operating incomes, expenditures and deficits.

Graph 3.7: Real percentage change in rents, incomes, expenditures and surpluses/deficits, ACT, 1990/91 to 2005/06



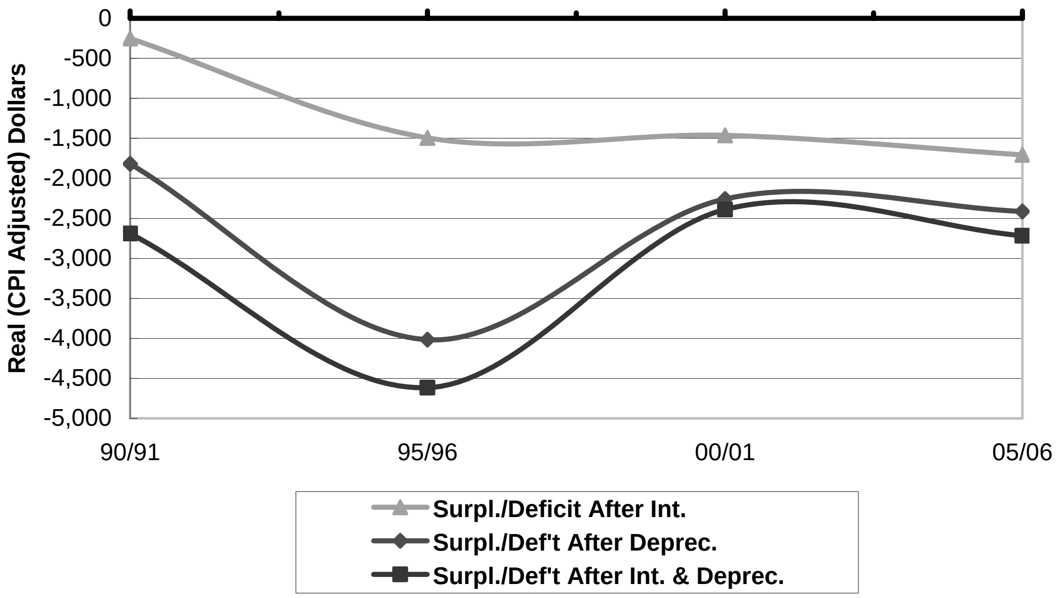
Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend, AHURI*; and return from ACT Housing to 2005/06 Operating Deficits Project

To summarise, over the 16-year period, real operating incomes per dwelling (net of grants and interest earned) only increased by less than one half of 1 per cent, while real operating expenditures per dwelling grew by 45 per cent, resulting in deficit growth per dwelling of 319 per cent.

Impact of net interest and depreciation

Graph 3.8 sets out the impact of net interest and depreciation on the operating surplus/deficit per dwelling.

Graph 3.8: Real surplus/deficit per dwelling after 'add backs' ($), ACT, 1990/91 to 2005/06



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from ACT Housing to 2005/06 Operating Deficits Project

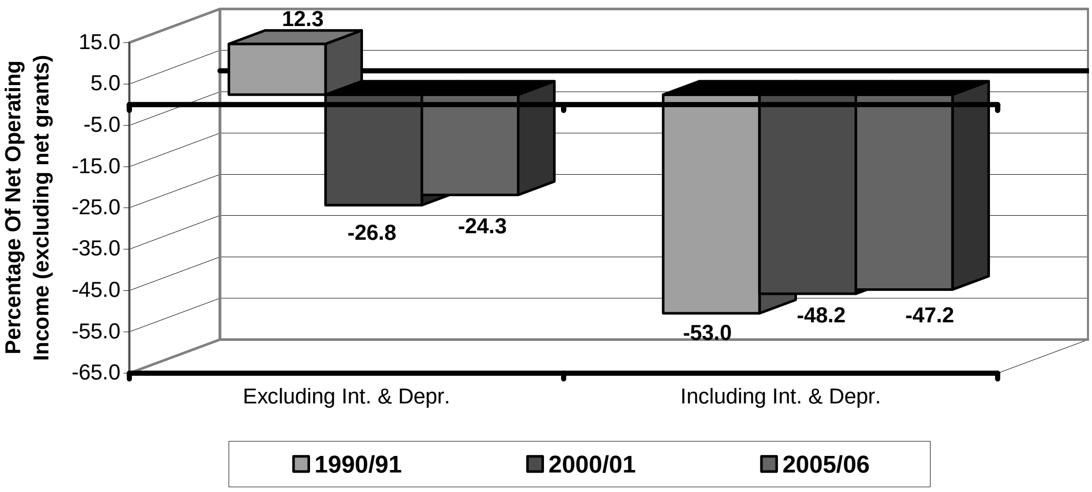
Over the period 1990/91 to 2005/06, the impact of interest costs and depreciation has declined substantially.

In 1990/91 net interest moved the real operating result from surplus to deficit by approximately $900 per dwelling. Depreciation added a further –$2440 to the deficit, increasing it after interest from –$250 to –$2,691 per dwelling. In 2000/01, however, net interest added only $134 to the expenditure line, and depreciation some $927, increasing the operating deficit from –$1,330 to –$2,372 or by less than half that which occurred a decade earlier.

Since 2000/01 the impact of these two items has stabilised in 2005/06, adding approximately the same to the deficit as in 2000/01.

Graph 3.9 sets out the operating deficits as a proportion of net income 'before' and 'after' net interest and depreciation.

Graph 3.9: Real public housing operating surpluses/deficits as percentage of net income before grants, ACT, 1990/91 to 2000/01 and 2005/06 (June 2006 dollars)



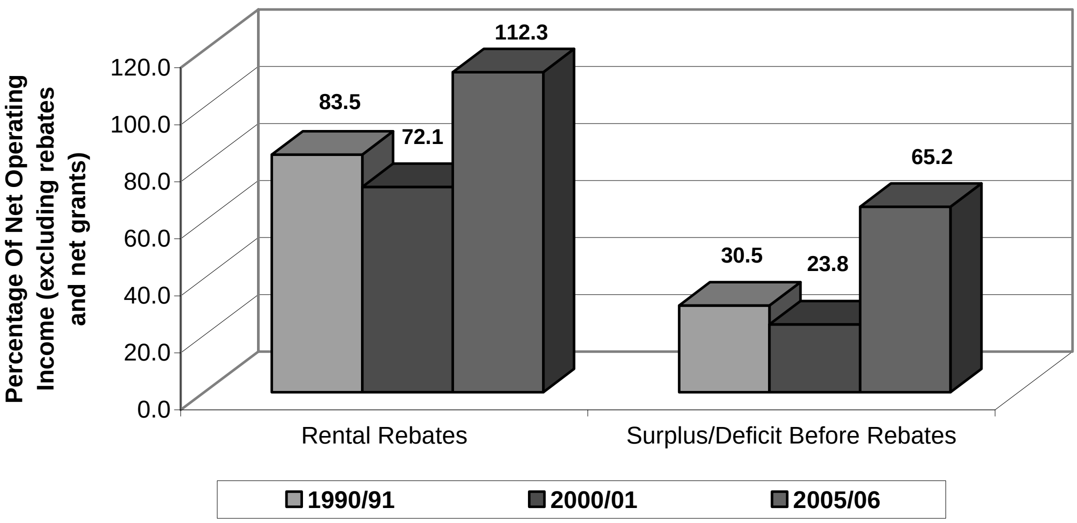
Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from ACT Housing to 2005/06 Operating Deficits Project

These results reinforce the earlier comments on the impact of net interest and depreciation. While these expenditure components are still important (as a percentage of net income), in 1990/91 they had a four-fold impact on the operating deficit but in 2005/06 they 'merely' added about 95 per cent to the deficit.

The importance of rebates

Graph 3.10 sets out rental rebates as a proportion of net income before grants.

Graph 3.10: Real public housing rental rebates as percentage of net income before rebates, ACT, 1990/91, 2000/01 and 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from ACT Housing to 2005/06 Operating Deficits Project

Between 1990/91 and 2000/01, real average rental rebates per dwelling declined significantly from $3,598 per dwelling to $3,120 in 2000/01. Between 2000/01 and

2005/06, average real rebates per dwelling almost doubled, increasing to $6,473 per annum.

Of most importance is that if the ACT received a commercial return based on market rents it would be financially robust and provide an appropriate operating rental return of about 3 per cent net per annum. Combined with the capital gain, this would provide a respectable double digit annual rate of return.

In the case of the ACT, recognising the real cost of the CSO and providing a cash payment for rebates would ensure the continued viability of the sector.

3.1.2 Qualitative

Key responses from the operational deficits questionnaire, 1990/91 to 2000/01, 2004 study

"The ACT respondent was unequivocal that tighter targeting and changes in household composition were leading to a steady decline in the real net rent received per dwelling as higher income, and multiple income households moved out and are replaced by lower income and more numerous single income households. It was anticipated, however that as a result of the changes to the rent setting policy in 2000/01 and an increase in rent payable as a proportion of income to 25% (up from 20% in 1992), the erosion of actual income from rents received may be halted for a short while.

The number and scale of older multi-unit properties built in the 1950s to 1970's to house public servants, and the lack of previous proper planned maintenance now means there are considerable maintenance backlogs (yet to be fully costed). The ACT has embarked on a substantial program of asset reconstruction and asset improvement, but the scope of the program was still being assessed in March 2003.

The long term failure to adequately maintain the properties means that, in many cases, the most economic option is for redevelopment, rather than upgrade-refurbishment.

The de-instutionalisation of many in society with mental and physical disabilities has meant that many of the costs of housing these people have fallen on housing authorities and the dwellings housing these households have required substantial modification and have high repair needs.

The call upon resources to fund more intensive tenancy management has continued to grow and increased targeting to those most in need with multiple and complex problems has meant that more effort is being devoted to ensure linkages with appropriate support services. To this end, five specialist housing managers have been employed at an additional cost of $0.6M per annum and an additional $500,000 linkages funding has been provided. There have, however, been no significant increases in salary and wages costs in the last decade.

Because of the smaller scale of the ACT overhead costs such as IT, finance, and policy are spread across a smaller property base and therefore, on a per dwelling basis, absorb a much higher proportion of the costs.

ACT Housing is of the view that a more holistic approach to tenancy management and the increasing number of clients requiring non-housing related assistance is the major contributor to the growth in administration costs."

Key responses from the operational deficits questionnaire, 2005/06

> "In the ACT, the structure of the portfolio has a bigger impact on maintenance and administrative costs than any locational factors. For instance, with the acquisition of properties in body corporates, there is the added cost of body corporate levies and associated administration of the property holdings in body corporates.
>
> Larger multi-units also tend to have higher costs largely related to ground maintenance, common area cleaning and graffiti removal and the costs associated with concentration of disadvantage, particularly if [tenants] belong to the same socio-economic class and have mental health and drug or alcohol dependencies/problems etc.
>
> An increasing amount of the budget is being directed towards providing support and assistance to tenants with high and complex needs, including the employment of specialist housing managers, providing financial and budget counselling and providing modifications or major works to enable those aged tenants and those with mobility impairments or disabilities etc. The actual cost is hard to extract as these are embedded into general operations, but would be in excess of $3 million per annum or 3 per cent and growing.
>
> In the 2006/07 [Federal] Budget, the government imposed expenditure savings of $14.4 million as well as introducing the cost of water consumption from tenants, which is expected to raise a further $0.900 million.
>
> The only long-term option is to seek to increase revenues through expanding public housing into a more affordable housing model with a proportion of tenants paying higher rents and some paying market rents at the median rental level."

ACT housing: conclusions

The 2004 report stated:

"In the last decade ACT Housing has embraced tighter targeting through the introduction of segmented waiting lists, engaged in a simultaneous effort to restructure its portfolio of dwellings and to improve its services to its clients, and has focused on reducing debt servicing required by the organisation.

These priorities have been reflected in:

- a long term decline in real rents per dwelling and hence Net Income per dwelling. Whilst this decline was recently arrested by changes to rent policy it can be expected to resume until such time as any trend to smaller households is completed and the proportion of rebated tenants and priority allocations reach saturation;
- almost stable real maintenance per dwelling; although it is now estimated that ACT Housing has a maintenance backlog of somewhere between $80million and $120million (the final liability will be determined after the current asset analysis);
- a rapid reduction in the amount of depreciation provisioning required per dwelling as asset restructuring and market developments act to reduce the average value per dwelling unit;
- significant improvements in tenants ranking of both their satisfaction with the service provided and the quality of their dwelling;
- a major increase in the real cost of managing the ACT Housing Stock to the point where the total overhead cost per dwelling is greater than the expenditure on either maintenance or rates and is the highest in Australia and New Zealand;

→ near elimination of any debt servicing burden, to the point where the debt/servicing ratio (Net Interest to Net Income) has fallen to 2.7%.

Notwithstanding the above, it would appear that the majority of any cost savings which can be accrued from asset restructuring (through lower maintenance) and debt reduction have already been achieved. With the likely future trends in Net Income, the anticipated maintenance backlog, and the current trends in overhead costs, it is probable that without any change to the distribution of tenant incomes, funding parameters and processes, the business will soon reach a point where untied grants will not be sufficient to fund operating deficits. Either additional funding will need to be provided or ACT Housing will have to 'cannibalise' (i.e. sell a proportion of) its dwellings to fund its operating shortfalls.

It is clear that were the ACT able to achieve the average Overhead cost for all authorities it would almost eliminate the existing Operating Deficit (under $100 per dwelling would remain).

It is also clear however, that if the full cost of the ACT's community service obligation (i.e. the difference between market rents and income related rents was fully funded) was fully recognised, ACT Housing's Operating Deficit would become an equivalent surplus. If funding was maintained on that basis, ACT Housing would likely operate at a profit for the foreseeable future."

Since 2000/01 the ACT has reversed the decline in real rents, and increased net rents and net incomes substantially. At the same time the housing authority has reined in the growth in operating expenditures to the extent that any difference in the growth of incomes and expenditures is almost entirely due to a greater maintenance effort.

As a consequence, backlogs in the preservation of the real asset value have declined and real operating deficits have remained almost static. Even though the decline in unrebated tenants has been arrested, it is unlikely that the real revenue growth of the past five years can be repeated, as this has largely been achieved by rent charging policy changes, which are now bumping up against the 25 per cent of income in repayment affordability barrier.

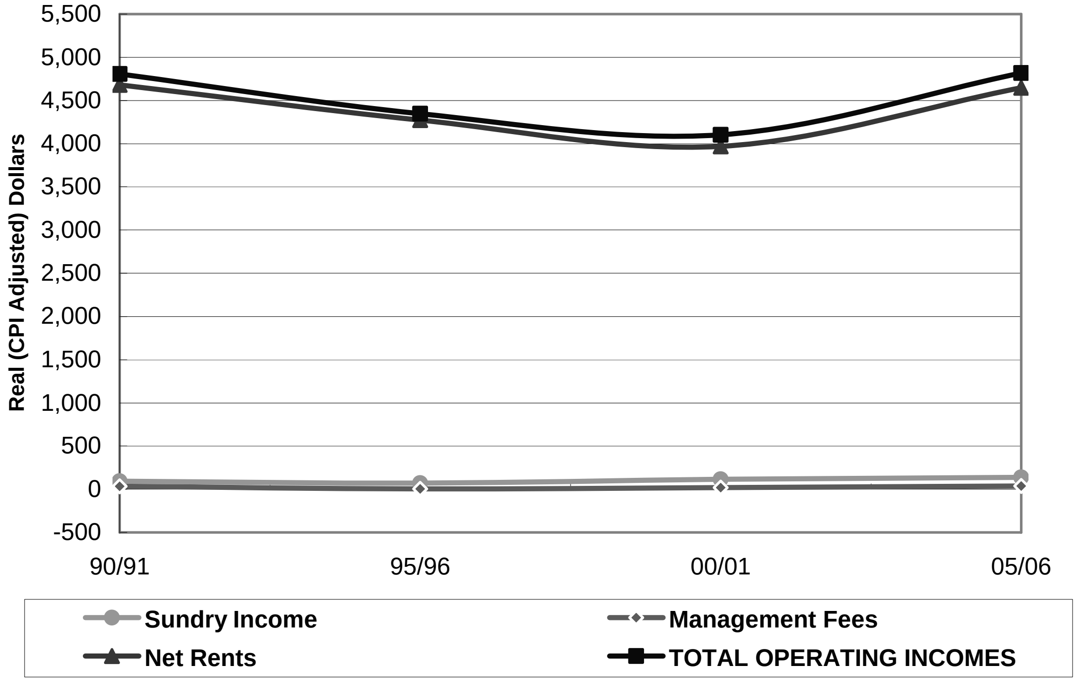
3.2 New South Wales

3.2.1 Quantitative

Changes in net incomes

Graph 3.11 traces real net income per dwelling unit over the period 1990/91 to 2005/06, in New South Wales (NSW).

Graph 3.11: Real incomes per dwelling unit ($), NSW, 1990/91 to 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from NSW Housing to 2005/06 Operating Deficits Project

Note: Includes public, community and Aboriginal housing owned and operated by NSW but excludes any dwellings head-leased or leased from third parties.

Over the period 1990/91 to 2000/01, net rents fell in real terms by the greatest proportions of all housing authorities from $4,680 to $3,968 or by approximately $700 per dwelling, nearly 16 per cent. Net real incomes per dwelling fell from $4,808 to $4,102. Real rents constituted more than 97 per cent of annual operating incomes throughout the decade.

Since 2000/01, however, real rents per dwelling have increased dramatically, rising from $3,968 to $4,646 or by approximately the same proportion as they fell during the preceding decade. This 17 per cent increase in real rents flowed on to net incomes, which grew from $4,102 to $4,818 or slightly more than $700 and by 17.5 per cent.

Quantitative factors affecting operating incomes

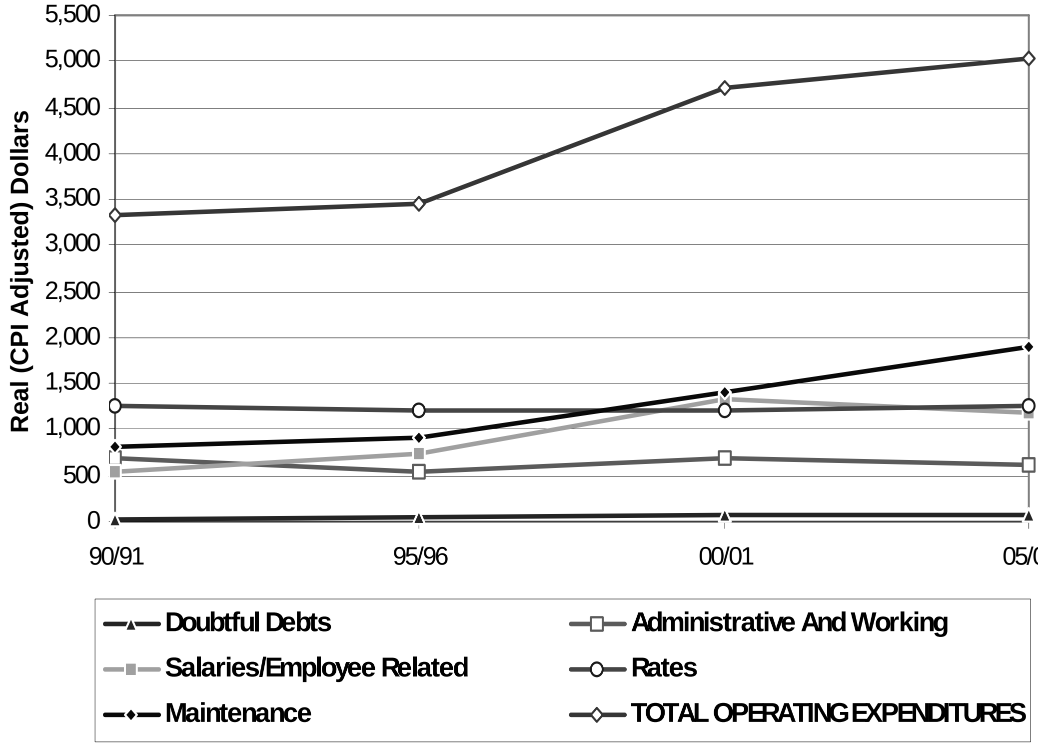
Over the period 1990/91 to 2000/01, rebated tenants increased from 85 per cent to 90 per cent of the total, but (more importantly) priority crisis and emergency allocations increased from 20 per cent of all new allocations to 40 per cent.

In the period 2000/01 to 2005/06, these trends reversed slightly. The number of rebated tenants only grew very marginally to 90.1 per cent of the total, while the proportion of allocations to priority, emergency and crisis cases fell substantially, from 39.5 per cent to 29 per cent.

Expenditures and expenditure priorities

Graph 3.12 sets out real net expenditure per dwelling unit over the period 1990/91 to 2005/06.

Graph 3.12: Real expenditures per dwelling unit ($), NSW, 1990/91 to 2005/06

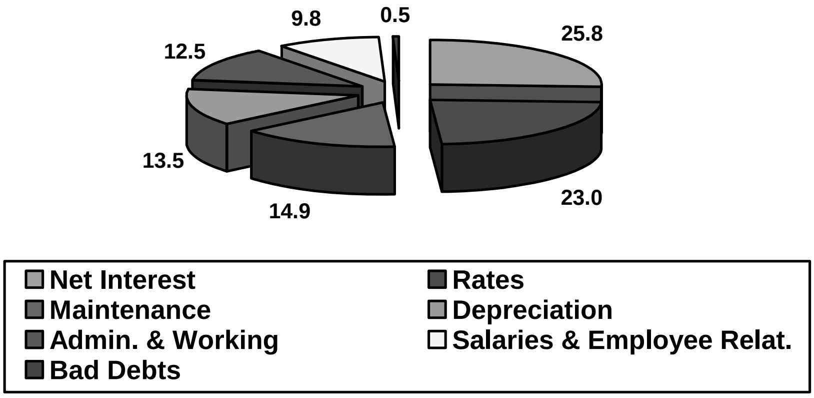


Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from NSW Housing to 2005/06 Operating Deficits Project

For the period 1990/01 to 2000/01, real operating expenditures per dwelling increased from $3,329 to $4,710. Real net interest payments fell substantially from $1,415 to $474 (–66.5 per cent), while real rates fell marginally from $1,261 to $1,212. Real administration and working expenses remained almost flat, increasing from $686 to $692 (or by just $7). Leaving aside doubtful debts (because these are such a small proportion of expenditure), all other items increased dramatically, with real maintenance increasing from $819 to $1,410, depreciation from $737 to $1,569 and salaries from $537 to $1,331. Total overhead increased in real terms from $1,223 to $2,023 or by approximately 65 per cent.

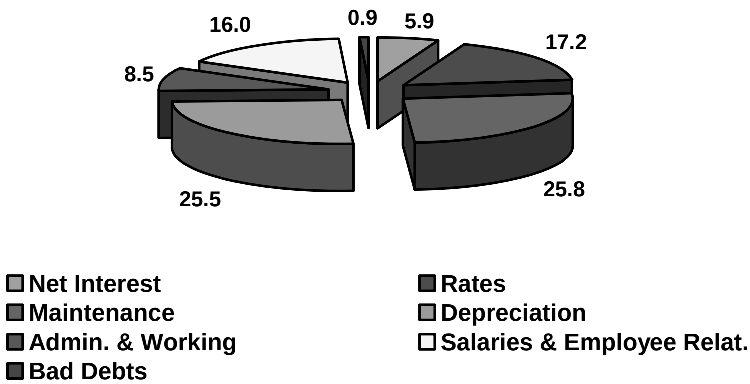
Since 2000/01, and similar to the ACT, there has be a dramatic change in these trends. Real operating expenditures have grown by just 6.6 per cent or just slightly more than 1 per cent per annum, only increasing by approximately $300 per dwelling per year. Reflecting these real changes in expenditure items, Graphs 3.13 and 3.14 set out the proportion of total operating expenditure occupied by each of the core expenditure items for the years 1990/91 and 2005/06.

Graph 3.13: Line items: percentage of real total public housing operating expenditure per dwelling (excluding rebates), NSW, 1990/91 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from NSW Housing to 2005/06 Operating Deficits Project

Graph 3.14: Line items: percentage of real total public housing operating expenditure per dwelling (excluding rebates), NSW, 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from NSW Housing to 2005/06 Operating Deficits Project

The graphs show how in NSW the proportion of total expenditure per dwelling for each item (including depreciation and net interest) has changed over the period 1990/91 to 2005/06.

The proportion of total expenditure absorbed by net interest has declined dramatically (from 25.8 per cent to 5.9 per cent).

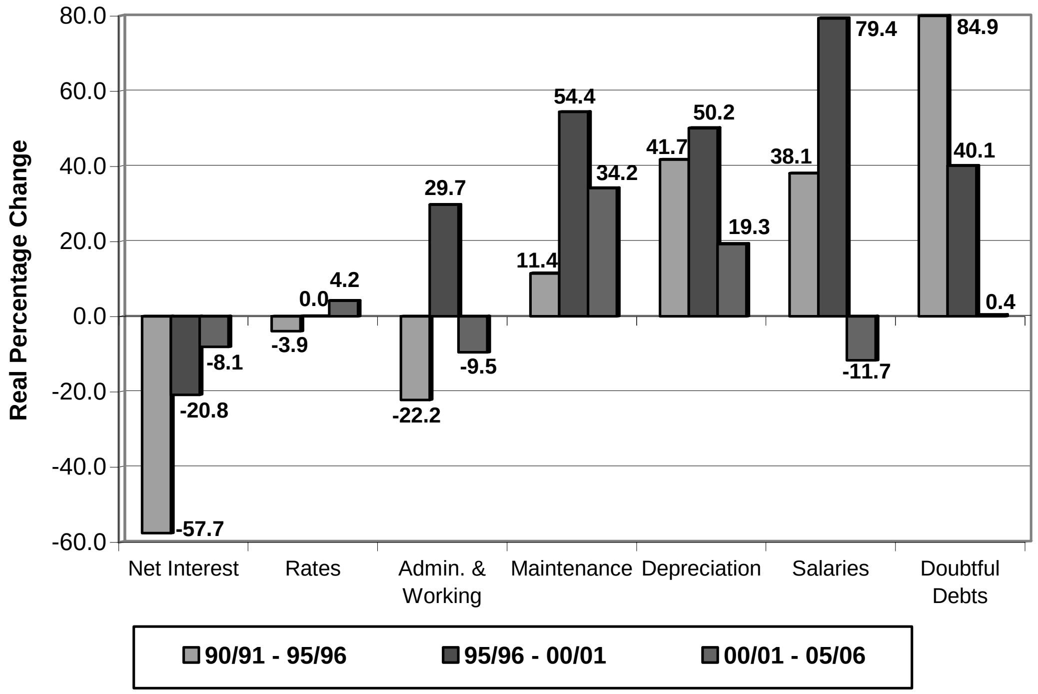
Both rates and administration and working items have declined moderately as a proportion of total operating expenditure, with the former falling from 23 per cent in 1990/91 to 17.2 per cent in 2005/06 and the latter from 12.5 per cent to 8.5 per cent over the same period.

As outlined in the analysis of expenditure item growth, by far the greatest change has occurred in maintenance, depreciation and salaries and related expenses, with maintenance increasing from 14.9 per cent to 25.8 per cent of total operating expenditures. Depreciation almost doubled, increasing from 13.5 per cent to 25.5 per cent, and salaries and related expenses increasing by approximately two-thirds, from

9.8 per cent to 16 per cent. NSW spends slightly less on salaries etc. than on rates, with total overhead absorbing just slightly less than the expenditure of maintenance.

Graph 3.15 sets out the real percentage change in the costs of key line items.

Graph 3.15: Real percentage change in key line items, NSW, 1990/91 to 2005/06



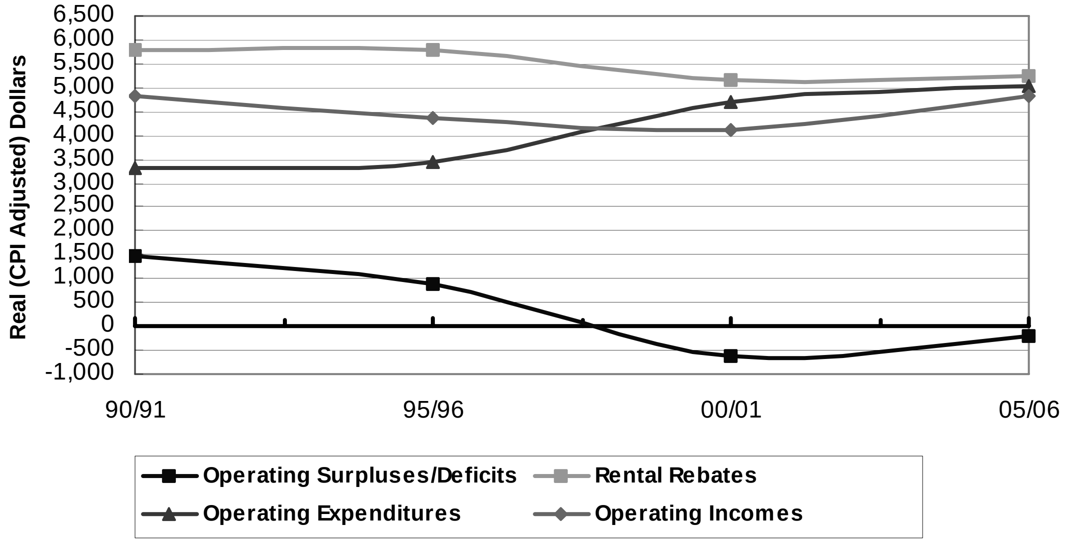
Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from NSW Housing to 2005/06 Operating Deficits Project

The graph reflects the findings outlined earlier – a very significant real decline in the cost per dwelling for net interest, a small decline in rates, a minor change in administration and working items, and major real increases in maintenance and depreciation. While salaries and employee-related expenses increased substantially in the period 1995/96 to 2000/01, since that time they have declined moderately (11.7 per cent).

Net operating income, expenditure and surplus/deficits

Graph 3.16 sets out the trends in operating surpluses/deficits excluding net interest and depreciation.

Graph 3.16: Real operating surpluses/deficits per dwelling ($), NSW, 1990/91 to 2005/06



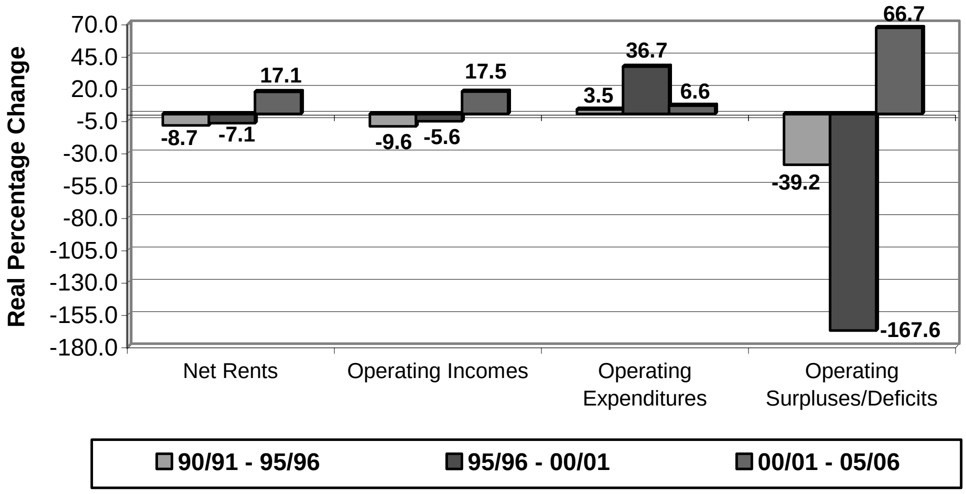
Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from NSW Housing to 2005/06 Operating Deficits Project

In 1990/91 NSW produced a real surplus per dwelling (excluding net interest and depreciation) of $1,479, the second-largest of all the housing authorities.

Thereafter, the surplus declined steadily until 1998/99. After 1998/99 the deficit grew rapidly until 2000/01, whereupon it reached –$608 per dwelling. After 2000/01 the deficit was reined in, reducing sharply to –$203 in 2005/06.

Graph 3.17 sets out the real percentage change in net rents, operating incomes, expenditures and surpluses/deficits.

Graph 3.17: Real percentage change in net rents, incomes, expenditures and surpluses/deficits, NSW, 1990/91 to 2005/06



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from NSW Housing to 2005/06 Operating Deficits Project

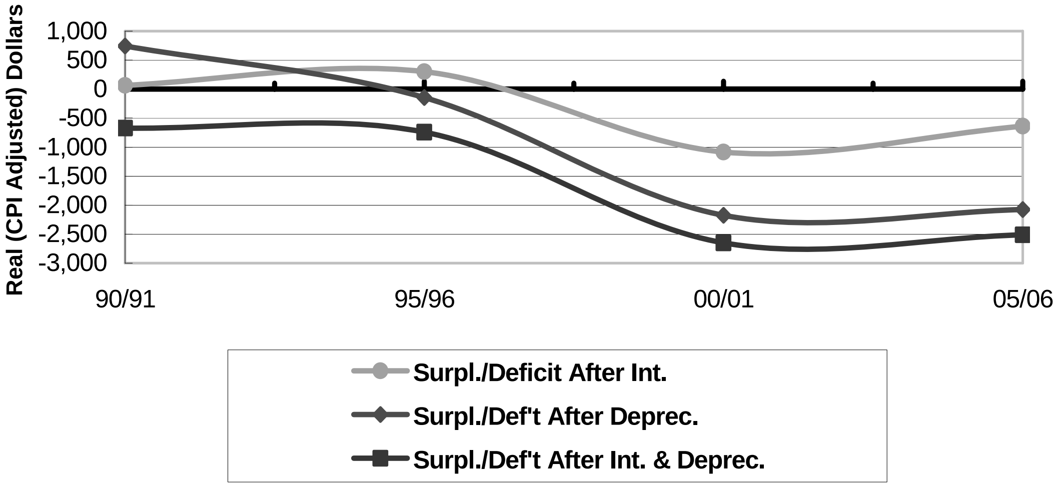
To summarise, two distinct and opposite trends can be identified. Over the period 1990/91 to 2000/01, real net rents and real operating incomes (net of grants and interest earned) fell by 15.2 per cent and 14.7 per cent respectively, while real operating expenditures grew by 41 per cent, resulting in a deficit growth of 141 per cent.

Since 2000/01 net rents and operating incomes have grown much faster (17.1 per cent and 17.5 per cent) than operating expenditures (6.6 per cent), resulting in an almost two-thirds improvement in the real deficit per dwelling.

Impact of net interest and depreciation

Graph 3.18 shows the impact of net interest and depreciation on the operating surplus/deficit.

Graph 3.18: Real surplus/deficit per dwelling after 'add backs' ($), NSW, 1990/91 to 2005/06

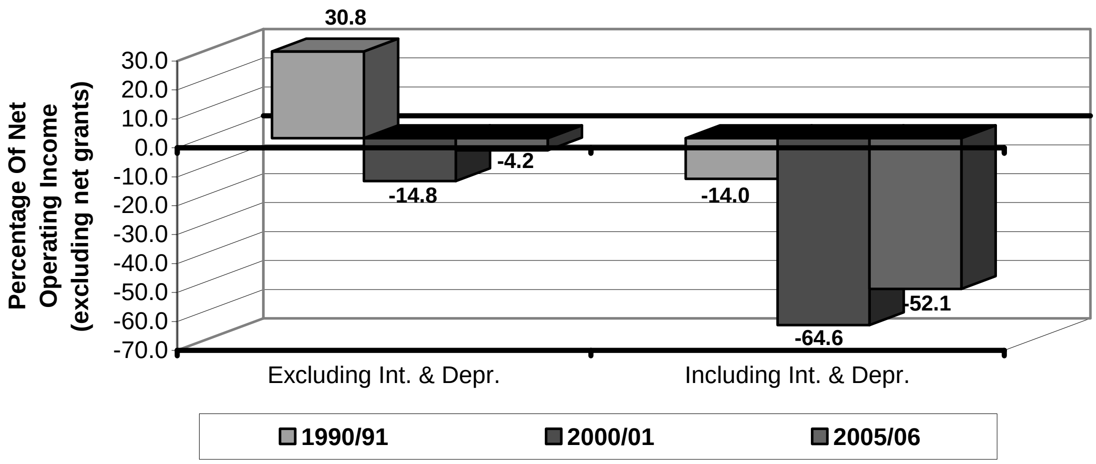


Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from NSW Housing to 2005/06 Operating Deficits Project

Since 2000/01 the impact of net interest and depreciation in absolute terms has only declined very slightly, from approximately –$1,800 per dwelling to –$1,700. Net interest and depreciation moved the operating result from a surplus of $1,479 to a deficit of –$671 in 1990/91, a net change of approximately $2,100; in 2005/06 the same items moved the deficit from –$203 to –$2,510, a net change of approximately $2,300 or just $200 more.

Graph 3.19 sets out the operating deficits as a proportion of net income before and after net interest and depreciation.

Graph 3.19: Real public housing operating surpluses/deficits as percentage of net income before grants, NSW, 1990/01, 2000/01 and 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from NSW Housing to 2005/06 Operating Deficits Project

These results reinforce the earlier comments on the impact of net interest and depreciation. These expenditure components had a three-fold impact on the operating deficit in 1990/91. In 2005/06 the impact was even greater, primarily as a result of the very small deficit and the rapid growth of depreciation from a very high base. Depreciation is now the second-largest expenditure item, just behind maintenance.

The importance of rebates

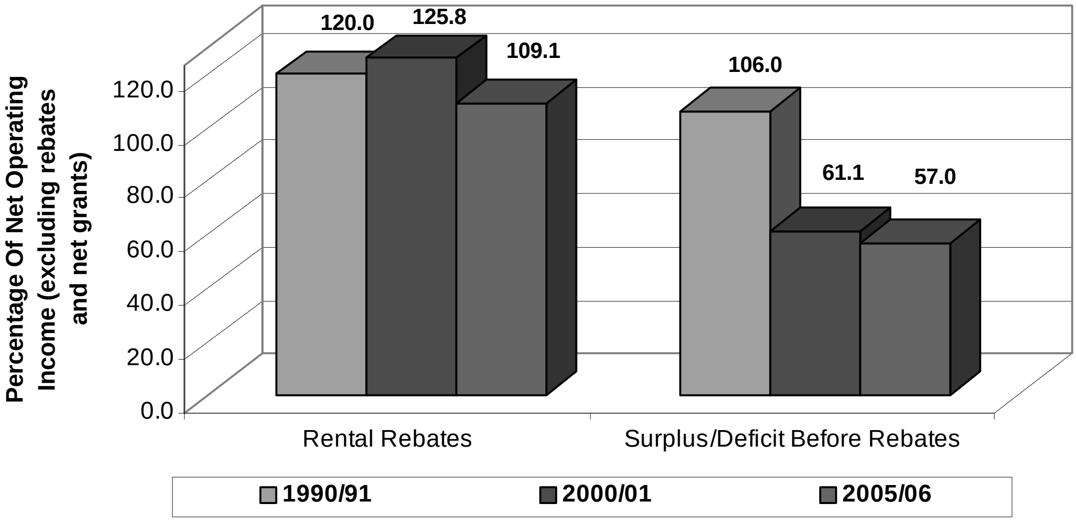
Over the period 1990/91 to 2000/01, real average rental rebates per dwelling declined significantly from $5,769 to $5,159, but as a result of changing rent-charging policies have since increased to $5,255.

Graph 3.20 sets out rental rebates as a proportion of net income before grants.

The graph clearly shows that although the impact of rental rebates relative to net incomes before rebates has declined slightly since 1990/91, they still remain very significant. Of most importance is that if NSW Housing received a commercial return based on market rents it would be financially robust and provide an appropriate operating rental return net per annum. Combined with the capital gain, this would provide a respectable double digit annual rate of return.

In NSW, recognising the real cost of the CSO and providing a cash payment for rebates would ensure the continued viability of the sector.

Graph 3.20: Real public housing rental rebates as percentage of net income before rebates, NSW, 1990/91, 2000/01 and 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from NSW Housing to 2005/06 Operating Deficits Project

3.2.2 Qualitative

Key responses from the operational deficits questionnaire 1990/91 to 2000/01, 2004 study

The 2004 study stated:

"The NSW respondent, in spite of the quantitative evidence, was equivocal about the impact of tighter targeting on Net Rent Income, and was unsure about the impact of changes to income growth on Net Rents.

There have been significant changes to rent setting policies in the last three years. With regards to rents charged, the policy has moved from charging 20% of household income to 25% for tenants on a subsidy.

The rate of 25% applies to all new tenants who entered public housing after April 2000, while rents for existing tenancies (as at April 2000) have increased by 1% a year and are currently charged at 24% (these annual increases will stop at 25% in 2004).

The diversity and dispersed nature of the property portfolio has meant that maintenance costs are higher than would be the case if the portfolio was a single concentrated entity of a homogenous type and construction. Premiums are paid for maintenance on country or more complex building type properties.

Recent initiatives under a maintenance improvement project have moved the Department from using single trade contractors to multi-trade contractors.

This is partly in response to increasing occupational health and safety requirements and the desire to deliver a total, seamless maintenance service to our customers without the Department becoming a building contractor coordinating single trades. This has been associated with cost increases. The maintenance backlog is currently estimated at over $600m, although large segments of the portfolio (70%) approach the 'maintained benchmark'. The backlog has been reduced by some $150m in the last few years.

Non planned maintenance has increased substantially in the last few years. Reasons for the continued growth in responsive maintenance expenditure includes:

- the introduction of a call centre in the late 1990s helped clients more easily register maintenance concerns, particularly those requiring an immediate or priority response; and
- increasing community and client expectations.

The Department is currently investigating ways of re-invigorating the portfolio to better align with service needs and reduce overheads such as maintenance costs. This includes looking to alliances and partnerships with private capital investment funds to transform the portfolio and eliminate the stigma associated with many areas of public housing.

Council and Water Rates are a very significant cost and in 2003 represented 30.5% of Net Rental Income.

Salaries and salary related costs have increased very significantly in the last decade.

In 1999/00 the Department transferred $250m of debt to the NSW Treasury.

The Department estimated on its accounting method a Deficit of $245m in 2000/01. Based on the analysis method agreed to in this analysis the Deficit would be about $300m for the same year."

Key responses from the operational deficits questionnaire: 2001/02 to 2005/06

"The Department [of Housing] has increasingly focused its targeting of products to those sectors with the greatest need. As a result the proportion of new allocations to priority/crisis cases has increased from almost 18 percent in 1997/98 to over 29 percent in 2005/06 (excluding priority re-housing transfers). The Department is in the process of implementing further refinement to its targeting processes that will further increase the proportion of new allocations to the target groups.

The Department is focused on implementing its purpose of building a stronger community by providing housing solutions for people in need. Accordingly, the Department has been concentrating on managing a sustainable level of liabilities in achieving its purpose rather than on restructuring or reducing its liabilities per se.

The Department has been estimating the maintenance backlog since 2000 using information from the Property Assessment Survey (PAS). From an estimate of $850 million in 2000 the backlog has been reduced to approximately $646 million in 2006.

The Maintenance Reform Program has been modelled on the basis of "normal" maintenance costs of $240 million a year, rising to $270 million a year over 10 years; and four years of activity (following the pilot phases) to clear the maintenance backlog.

The following factors significantly affect the operating environment for the NSW Department of Housing:

- The Department has a relatively high proportion of its housing stock (around 35 per cent) on estates. This configuration of the housing stock involves higher tenancy management and maintenance costs.
- The Department has embarked on a 10-year long-term asset planning process, which involves the replacement of around 10 per cent of the housing stock over the period. A significant proportion of grant funding is being devoted to this activity.

- → High housing costs in NSW affect the costs of stock replacement, particularly where the objective is to de-concentrate housing stock by reducing holdings on estates.
- → NSW has high levels of rent rebates, given [the] high market rents.
- → Significant upward pressure on private sector rents is increasing demand for social housing, at a time when the number of lettings in social housing is diminishing.

The Department of Housing devotes the majority of its income (rent and grants) to operating costs (including maintenance), and upgrading and realignment of the housing portfolio.

Net growth in the social housing stock is largely confined to the community housing sector, with growth running at around 200 dwellings a year.

Consequently the size of the social housing portfolio is not keeping pace with the growth in population or in the number of households in NSW."

NSW Housing conclusions

The 2004 study stated:

"In the last decade NSW Housing has embraced tighter targeting through the introduction of segmented waiting lists, focused heavily on improving the quality of its estates and its asset management; and sought to more closely align its portfolio with the types of households requiring assistance. It has also sought to substantially improve the overall quality of service and support provided to its clients. NSW was, however, very late to institute changes to rent charging policies that other States had introduced much earlier.

These priorities have been reflected in:

- → a long term decline in real rents per dwelling and hence Net Income per dwelling. Whilst this decline was recently arrested by changes to rent policy, an analysis of the 2001/02 accounts indicates that the changes to rent charging instituted in 2001, will fall well short of eliminating the 'core' (before Net Interest and Depreciation) Operating Deficit. Furthermore NSW is not, as yet, near saturation when it comes to Priority Allocations. Until such time as any trend to smaller households is completed and the proportion of rebated tenants and priority allocations reach saturation, the downward movement in Net Rents per dwelling can be expected to resume after 2004;
- → a major reduction in the impact of Net Interest, as the debt reduction and restructuring initiatives take effect;
- → rapidly rising real maintenance per dwelling, although NSW Housing estimates it has a maintenance backlog of something in excess of $600million;
- → a very rapid increase in the impact of Depreciation on the operating result, as the effect of the rapid rise in Sydney values finds it's way to the bottom line;
- → very high increases in Salaries and Related Expenditures as the additional and improved services add to the cost base;
- → because of the Sydney housing market NSW is the State where Rebates have their greatest effect and are the greatest burden on the Operating result;
- → significant improvements in tenants' ranking of both their satisfaction with the service provided and the quality of their dwelling;

It needs to be noted that NSW has moved from being the Housing Authority with the second largest Operating Surplus in 1990/91, to one where the Operating Deficit is now the third worst in the group examined. Whilst Operating Expenditure growth was just above the average of 38% real for all Authorities it has occurred in a context where Net Income has been the second hardest hit.

Notwithstanding the above, it would appear that the majority of any cost savings which can be accrued from debt reduction has already been achieved. With the anticipated maintenance backlog it is difficult to forecast how any significant cost savings will accrue from this core function in the immediate future. The same is true of Rates. With the likely future trends in Net Income, the anticipated maintenance backlog, and the current trends in overhead costs, it is probable without any change to the distribution of tenant incomes, funding parameters and cost structures, the business will soon reach a point where untied grants will not be sufficient to fund future operating deficits.

Either additional funding will need to be provided or NSW Housing will have to progressively 'sell off its assets in order to fund its operating shortfalls.

It is also clear, however, that if the full cost of the NSW's community service obligation was fully recognised (i.e. the difference between market rents and income related rents was fully paid for), NSW Housing would be a very profitable business and the rate of return would exceed that obtained by many purely for profit businesses."

Notwithstanding adjustment of stock numbers (to allow for the transfer of 2,181 stock to community housing in the intervening period), restructuring of the portfolio has resulted in slight stock losses of the order of 700 compared to the 2004 study.

However, major improvements have been made in reversing the direction of the operating deficit, primarily as a result of changes in rent-charging policy. These changes have produced a net real growth in rents of $55 m per annum net of stock reductions.

Furthermore, over the period 2000/01 to 2005/06, operating expenditures only just exceed operating incomes (before interest and depreciation), even with the major emphasis on the maintenance reform program, which has resulted in a growth in maintenance expenditures of 34 per cent. The operating result before net interest and depreciation may therefore return to balance in the next couple of years.

With nearly all tenants now paying 25 per cent of income in rent, however, and rental charging running up against affordability barriers, further net rental growth per dwelling unit is very unlikely. Similarly, although rebated tenants as a proportion of the total have stabilised, as time passes, increasing proportions of allocations will be to very low income priority cases. With no further changes to rental policy, real rental revenue may decline somewhat. Costs are likely to increase faster than revenues and the current improvement in operating deficits may therefore prove temporary.

3.3 Northern Territory (Territory Housing)

3.3.1 Quantitative

Changes in net incomes

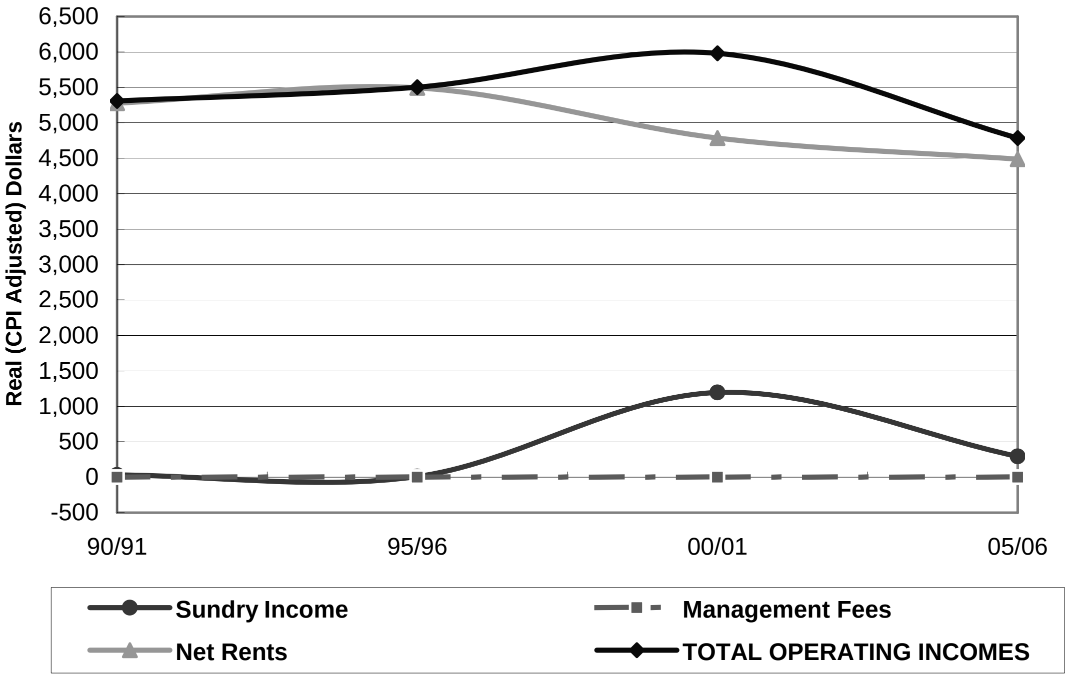
Graph 3.21 traces real Net Income per dwelling unit over the period 1990/91 to 2005/06.

Over the period 1990/91 to 2000/01, operating incomes increased in real terms from $5,307 to $5,979 or 12.6 per cent.

However, net rents per dwelling fell by 9.3 per cent, much more than the average for all authorities of 4.96 per cent or less than one half of 1 per cent per annum. The large majority of the increase was due to a substantial rise in sundry incomes, which although a recurrent item, in the case of Territory Housing includes receipts from excess water use, transfer fees, valuations, processing settlement fees and gifts.

As would be expected, this sundry income was not repeated in the period 2000/01 to 2005/06. Real rents constituted more than 95 per cent of annual operating incomes until 2000/01, when they fell to 80 per cent due to the impact of the rapid growth of sundry incomes.

Graph 3.21: Real incomes per dwelling unit ($), NT, 1990/91 to 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Territory Housing to 2005/06 Operating Deficits Project

Note: Includes public, community and, for part of the period, Aboriginal housing owned and operated by Territory Housing but excludes any dwellings head-leased or leased from third parties.

Since 2000/01 real rents per dwelling have fallen moderately from $4,783 per dwelling to $4,488 or over 6 per cent. When combined with elimination of the one-off sundry income effect, real operating incomes per dwelling have fallen by almost $1,200 or approximately 20 per cent.

Quantitative factors affecting operating incomes

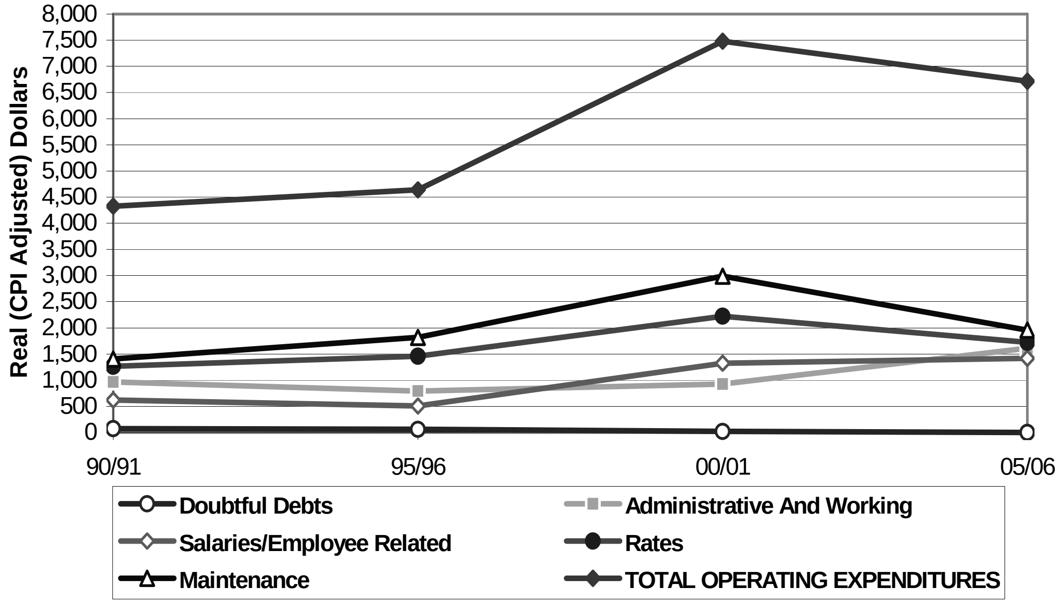
Over the period 1990/91 to 2000/01, rebated tenants increased from 43 per cent to 80 per cent of the total, and priority crisis and emergency allocations increased from 10 per cent of all new allocations to 47 per cent, the third-highest of all Australian states.

These trends have continued, albeit at a slower pace, in the period 2000/01 to 2005/06 and in 2005/06 rebated tenants constituted 84.2 per cent of the total, while priority applications have fallen from 47 per cent to 28 per cent of all new allocations.

Expenditures and expenditure priorities

Graph 3.22 sets out real net expenditure per dwelling unit over the period 1990/91 to 2005/06. The graph shows that real operating expenditures per dwelling increased from $4,326 in 1990/91 to $7,483 in 2000/01. Real increases in maintenance and rates outgoings has been severe, with maintenance expenditure per dwelling increasing from $1,405 to $2,986 (113 per cent), and rates from $1,268 to $2,222 (75 per cent). The most significant real increases in expenditure occurred in the 'salaries and employee-related item', increasing from $616 per dwelling to $1,328 (or 116 per cent). Total overhead (defined as salary and administrative/working costs) increased in real terms from $1,582 to $2,255 or approximately 43 per cent.

Graph 3.22: Real expenditures per dwelling unit ($), NT, 1990/91 to 2005/06

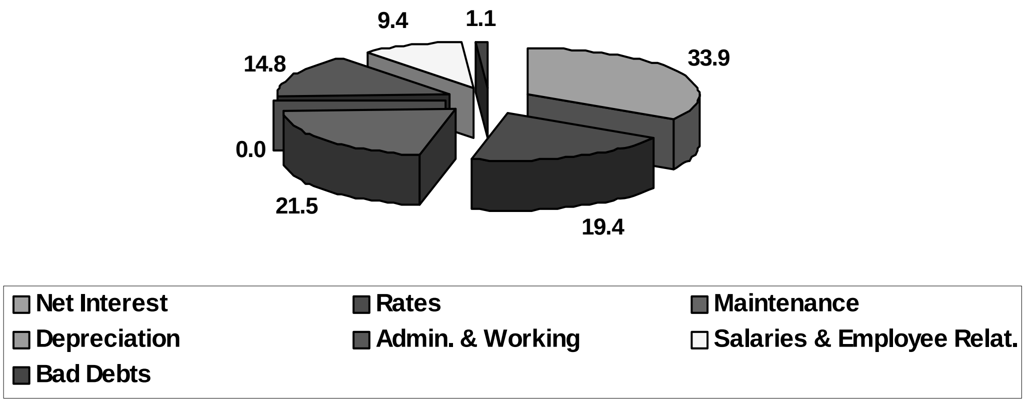


Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Territory Housing to 2005/06 Operating Deficits Project

Since 2000/01, however, real expenditure on both maintenance and rates per dwelling has significantly declined, falling approximately $1,000 per dwelling for the former and by more than $500 for the latter. Similarly, salaries and employee-related expenses only increased by less than $100 per dwelling, and administrative and working expenses grew by 73.8 per cent. Total overhead growth per dwelling was much slower than in the decade before 2000/01. Consequently total real operating expenditure per dwelling fell substantially from $7,483 to $6,713 or $770 per dwelling.

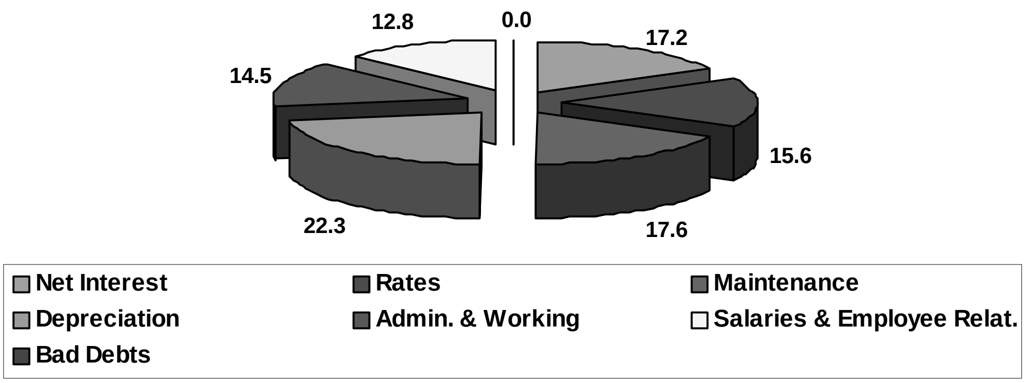
Reflecting these real changes in expenditure items, Graphs 3.23 and 3.24 set out the proportion of total operating expenditure occupied by each of the core expenditure items for the years 1990/91 and 2005/06.

Graph 3.23: Line items: percentage of real total public housing operating expenditure per dwelling (excluding rebates), NT, 1990/91 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Territory Housing to 2005/06 Operating Deficits Project

Graph 3.24: Line items: percentage of real total public housing operating expenditure per dwelling (excluding rebates), NT, 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Territory Housing to 2005/06 Operating Deficits Project

The graphs show how the proportion of the total expenditure per dwelling for each item (including depreciation and net interest) has changed over the decade. It should be noted that NT Housing has only been provisioning for depreciation since the financial year 2000/01, so results are somewhat distorted by this factor.

The proportion of total expenditure absorbed by net interest (down from 33.9 per cent to 17.2 per cent) has declined dramatically. This is also true of bad debts, which have fallen from 1.1 per cent to 0.1 per cent of total expenditure.

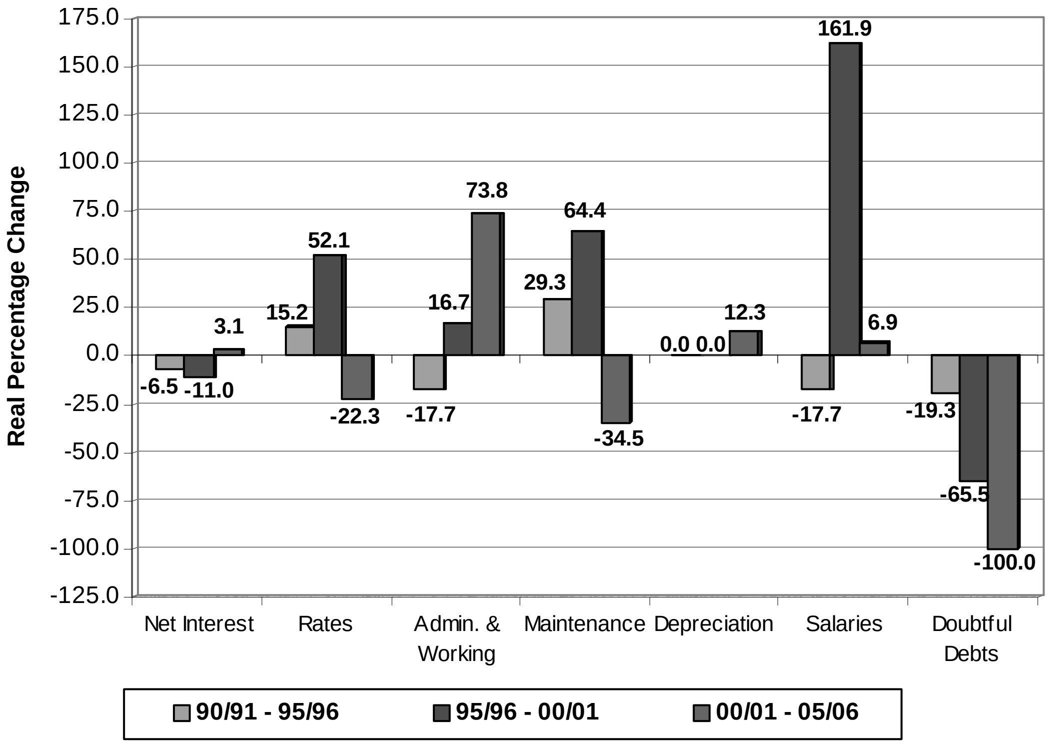
The proportion of total expenditure spent on maintenance has also declined moderately (down from 21.5 per cent to 17.6 per cent), as have rates, which fell from 19.4 per cent to 15.6 per cent.

Most other items have remained relatively constant as a proportion of total expenditure, although the real amount per dwelling spent on most items (with the exception of administration and working items) has grown rapidly. Salaries and employee-related expenses have increased moderately from 9.4 per cent to 12.8 per cent of the total.

Depreciation is by far the largest item of expenditure, followed by maintenance and net interest.

Graph 3.25 reflects the findings outlined earlier – that is, very significant real declines in the cost per dwelling for doubtful debts and net interest, and major real percentage increases in maintenance, rates and salaries etc.

Graph 3.25: Real percentage change in key line items, NT, 1990/91 to 2005/06

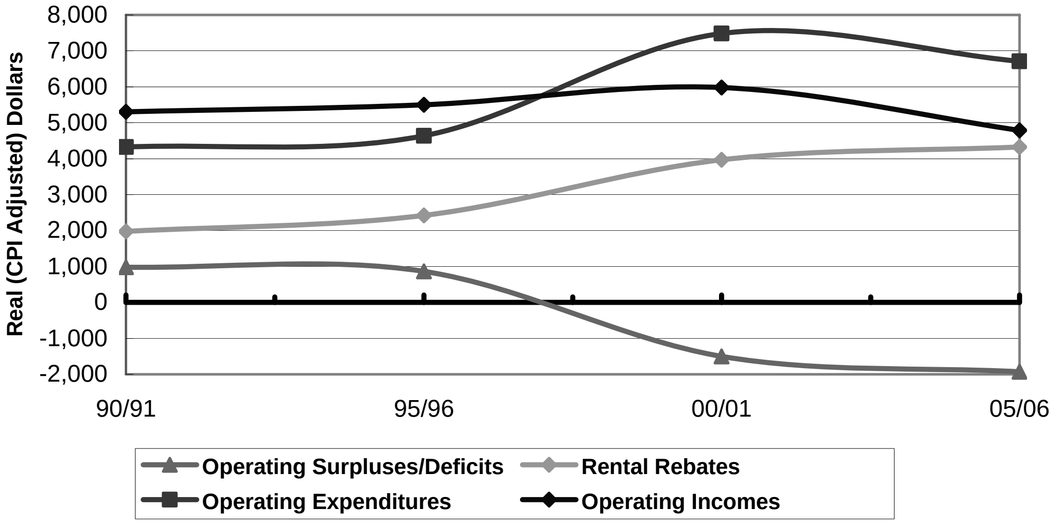


Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Territory Housing to 2005/06 Operating Deficits Project

Net operating income, expenditure and surplus/deficits

Graph 3.26 sets out the trends in operating surpluses/deficits excluding net interest and depreciation.

Graph 3.26: Real operating surpluses/deficits per dwelling ($), NT, 1990/91 to 2005/06



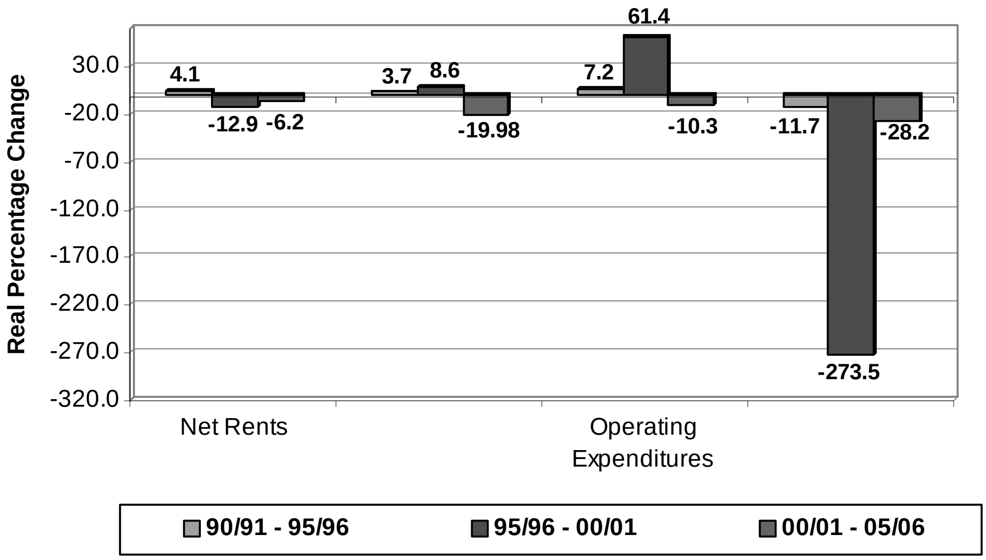
Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Territory Housing to 2005/06 Operating Deficits Project

In 1990/91 the Northern Territory produced a real surplus per dwelling (excluding net interest and depreciation) of $981, and between 1990/91 and 2000/01 this fell to a deficit of –$1,504. Between 1990/91 and 2000/01 real expenditures increased rapidly (from $4,326 to $7,483), while real incomes only increased moderately (from $5,307 to $5,979)

Since 2000/01 real net rents have fallen from $4,783 per dwelling to $4,488 and real operating incomes from $5,979 to $4,784 (due to the impact of a large one-off sundry income item in 2000/01). Real expenditures per dwelling have also fallen since 2000/01 but by a far more modest amount, from $7,483 to $6,713. As a result these deficits increased to –$1,929 per dwelling.

Graph 3.27 sets out the real percentage change in net rents, operating incomes, expenditures and surpluses/deficits.

Graph 3.27: Real percentage change in net rents, incomes, expenditures and surpluses/deficits, NT, 1990/91 to 2005/06



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Territory Housing to 2005/06 Operating Deficits Project

To summarise over the full period, real operating incomes per dwelling (net of grants and interest earned) fell by 9.9 per cent, but real operating expenditures grew by 55 per cent, resulting in deficit growth of 297 per cent.

Impact of net interest and depreciation

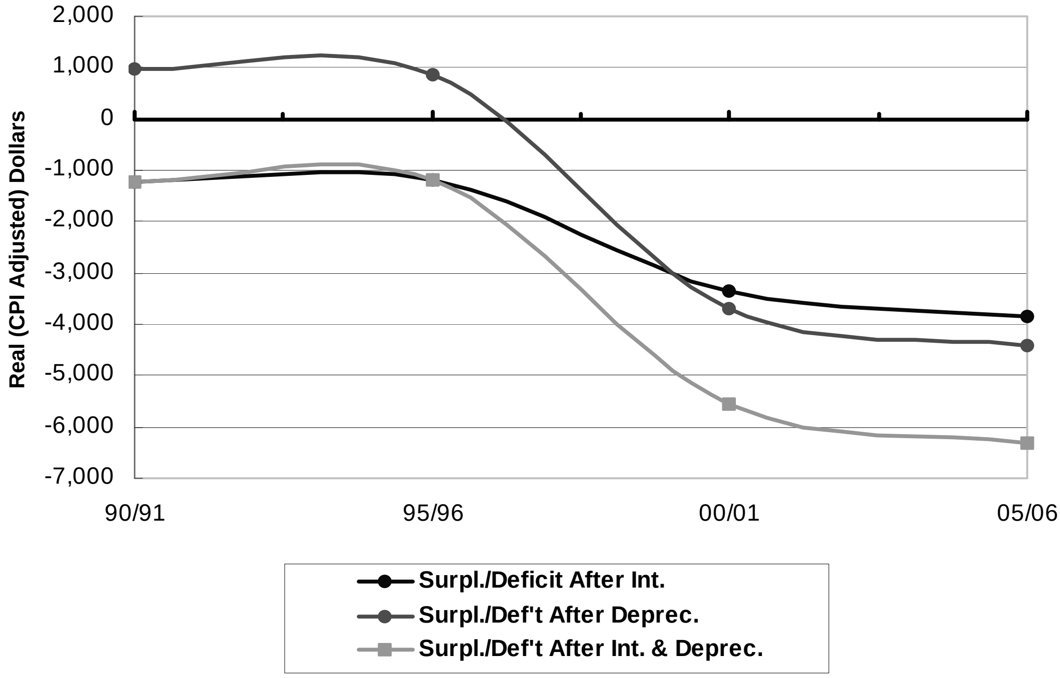
Graph 3.3.8 sets out the impact of net interest and depreciation on the operating surplus/deficit, with depreciation being first provisioned in 2000/01.

If the impact of depreciation is left out of the analysis, the impact of interest costs have declined moderately over the period. In 1990/91 real net interest moved the real operating result from surplus to deficit by $2,300 per dwelling.

In 2000/01, however, real net interest added $1,846 to the expenditure line, affecting the deficit outcome somewhat less.

Depreciation is now the largest single item of expenditure, and net interest and depreciation effectively almost triple the size of the operating deficit per dwelling.

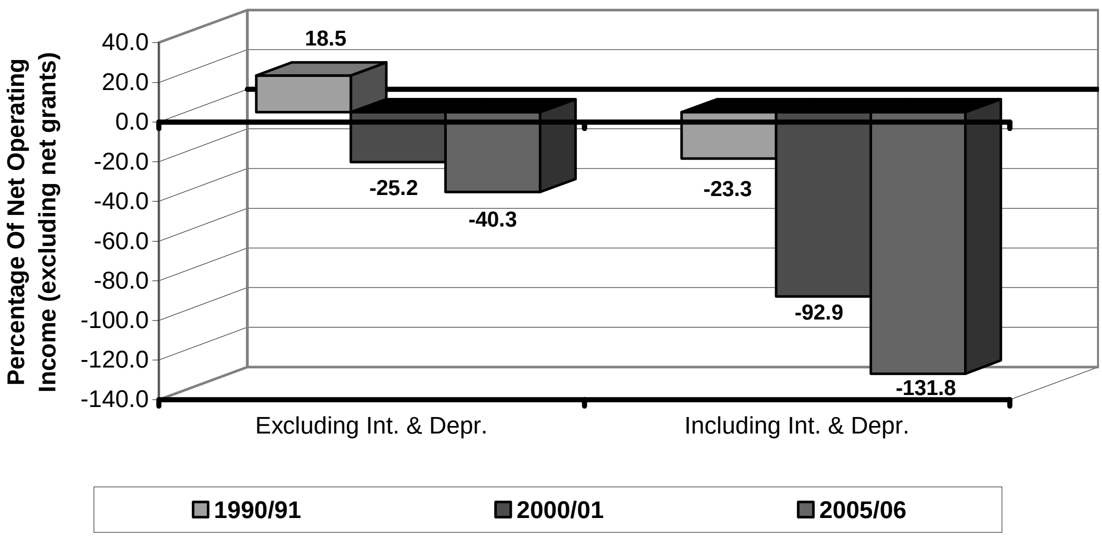
Graph 3.28: Real surplus/deficit per dwelling after 'add backs' ($), NT, 1990/91 to 2005/06



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Territory Housing to 2005/06 Operating Deficits Project

Graph 3.29 sets out the operating deficits as a proportion of net income before and after net interest and depreciation.

Graph 3.29: Real public housing operating surpluses/deficits as percentage of net income before grants, NT, 1990/91, 2000/01 and 2005/06 (June 2006 dollars)



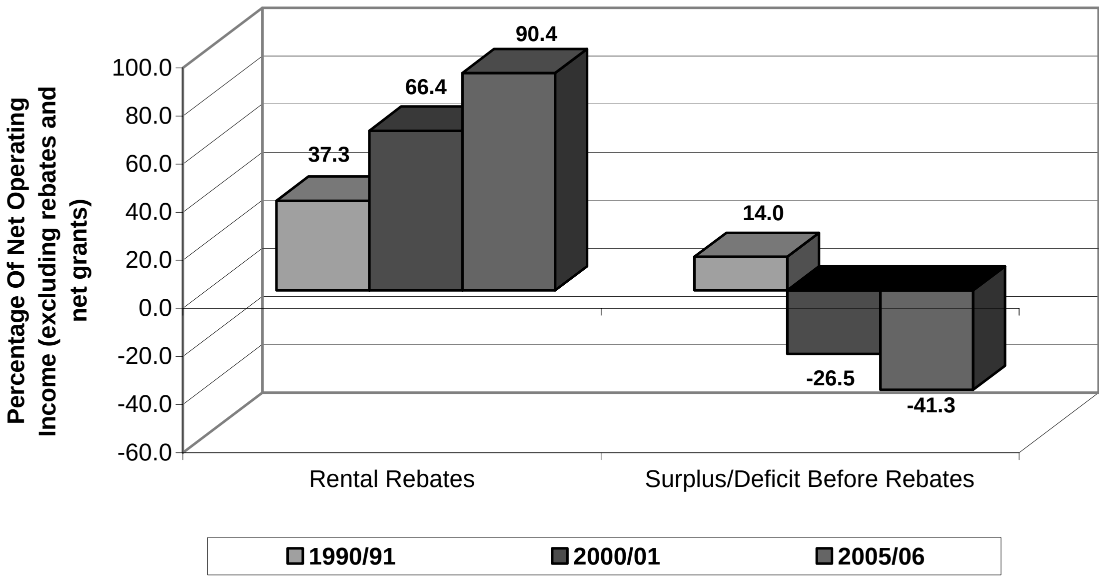
Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Territory Housing to 2005/06 Operating Deficits Project

The impact of net interest and depreciation is very significant, with the real public housing operating deficit after interest and depreciation being more than three times that excluding interest and depreciation in 2005/06.

The importance of rebates

Real average rental rebates per dwelling grew significantly from $1,979 in 1990/91 to $4,327 in 2005/06. The 1990/91 real average rental rebate per dwelling figure is relatively low, as a significant number of government employees in Territory Housing at this time could not be excluded from the data. The incomes of these government employees would have been such that they would not have received a rebate, therefore on average lowering the per dwelling rental rebate.

Graph 3.30 sets out rental rebates as a proportion of net income before grants.



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Territory Housing to 2005/06 Operating Deficits Project

The graph clearly shows that the impact of rental rebates has increased substantially and is now equivalent to more than 90 per cent of net operating incomes. Even after adding back net interest and with the recent introduction of depreciation, if rebates were received as a cash payment, Territory Housing would be left with an operating deficit similar to that which applies before net interest and depreciation.

In the Northern Territory, recognising the real cost of the CSO, plus eliminating net interest, would ensure the continued viability of the sector.

3.3.2 Qualitative

Key responses from the operational deficits questionnaire, 1990/91 to 2000/01: 2004 study

> "The Northern Territory respondent indicated that the Territory did not move to a strict targeted based approach until the later part of the decade (1998). This was primarily due to Territory Housing's role in providing accommodation for public servants. However, the respondent indicated average household incomes had declined in recent years and that aged and single households were increasing rapidly, thereby reducing the net rents received.

The Territory has been through two major changes to rent setting policies in the decade each of which progressively moved tenants towards paying 25% of their income in rent. These changes coincided with the significant rise in net rents from 1998/99 on.

Territory Housing is intent on restructuring both geographically and by dwelling type the asset base to more closely reflect the changes in demand patterns which have emerged.

From 1998 on, Maintenance requirements were outsourced to the Northern Territory Department of Transport and Works and Territory Housing had no effective control of expenditure for this item until the end of 2001 when the function was returned. The difficulty of obtaining skilled contractors in many areas and the high cost of obtaining materials means a strong competitive tender process for maintenance work is almost impossible to achieve, with the consequent impact on maintenance costs. Because a large part of the stock was completely rebuilt after the hurricane in 1975, only responsive maintenance was conducted for much of the 1990s. Cyclical maintenance programs have only been reintroduced in recent times.

Rates are seen as a very significant cost which is increasing rapidly in both nominal and real terms.

Of great concern to the Territory respondents was the continuing burden of Net Interest payments, which in 2000/01 approximated 26.3% of Net Income. At the time of the interview in March 2003, officers were engaged in an extensive exercise examining options for restructuring the debt.

The call upon resources to fund more intensive tenancy management has continued to grow and increased targeting to those most in need has meant that more effort is being devoted to ensure linkages with appropriate support services. In the last decade there has been significant increases in Salary and Related expenses, and Administration and Working costs.

It is anticipated that whilst the Territory has arrested the rise in Operational Deficits through recent changes in rent charging policy if real rates of cost growth continue, these deficits will grow substantially in the foreseeable future."

Key responses to the operating deficits questionnaire 2005/06

"Territory Housing has recently undertaken a restructure including the establishment of a dedicated finance unit [that] had been outsourced to the Department of Corporate and Information Services. Since the restructure the unit has specifically focused on financial management and the entity's capital structure. Liabilities are a high priority for the 2006/07 financial year.

Due to the significant increase in infrastructure activity in 2004/05, no attempt has been made to escalate the pay down of existing debt. The Territory carries approximately 4–5 times the average interest servicing cost per public housing dwelling compared to other state housing entities. This contributes to the higher operating cost base and clouds comparisons with other jurisdictions.

The geographical nature and age of the portfolio influence maintenance costs significantly. Industry capacity and contractor availability in small towns also influences maintenance costs.

There has been limited programmed maintenance undertaken over a considerable period on the housing stock assets to maintain condition, resulting in a major backlog to bring assets to acceptable condition standard.

More than 60 per cent of the stock is over 20 years old, which is accentuating the increasing magnitude of the backlog and the ultimate cost to bring all stock up to required standards.

The overall asset condition and amenity problem has been identified and a program commenced in 2003 to improve the overall condition of public housing assets. A conservative estimate places the total program requirement at around $180 million.

From a public housing perspective, Territory Housing is still experiencing substantial operating deficits. These are relatively stable and no real growth is expected over the next few years (bar any change in government policy surrounding the delivery of public housing)."

Territory Housing: conclusions

The 2004 study stated:

"Similar to the ACT, in the last decade Territory Housing has embraced tighter targeting through the introduction of segmented waiting lists, engaged in a simultaneous effort to restructure its portfolio of dwellings and to improve its services to its clients, and has focused on reducing debt servicing required by the organisation. One substantial difference is the focus on rent charging policy in the last five years. These priorities have been reflected in the following outcomes:

- there has been a substantial real increase in Net Rents received per dwelling with almost all of the 13.5% real increase occurring in the last three years since the major change to rent charging policy;
- similar to the ACT, however, the decline in Net Rents per dwelling can be expected to resume until such time as any trend to smaller households is completed and the proportion of rebated tenants and priority allocations reach saturation;
- an increase has occurred in Sundry Income, and it is uncertain if the income from the individual items which make up Sundry Income can be maintained in the future;
- as a consequence, it is very probable that the rate of growth of Territory Housing's Net Incomes (currently the fastest in Australia) will slow considerably over the next five years;
- whilst the very high and rapidly growing Maintenance expenditure per dwelling is partially due to the special geographic, labour market, and demand characteristics in the Northern Territory, it may also be partially due to the outsourcing arrangement that persisted until the end of 2001, and since this arrangement has been reversed, it is possible that the rate of Maintenance expenditure per dwelling may not grow in the future as rapidly as the recent past;
- significant improvements have occurred in tenants' ranking of both their satisfaction with the service provided and the quality of their dwelling;
- whilst the relative importance of interest payments as a component of expenditure has halved in the last decade, it still represents a very substantial cost.

With the likely future trends in Net Income, current trends in Maintenance, Rates and Overhead similar to the ACT, it is probable without any change to the distribution of tenant incomes, funding parameters and cost structures, the business will soon reach a point where untied grants will not be sufficient to fund operating deficits. Either additional funding will need to be provided or Territory Housing will have to sell stock ('cannibalise' its assets) to fund its operating shortfalls.

Two developments would ensure the longer term viability of Territory Housing. If the full cost of the Territory Housing's community service obligation was fully recognised (i.e. the difference between market rents and income related rents was fully funded), and the Net Interest bill was reduced by about 35%, Territory Housing's Operating Deficit would become an equivalent surplus. If funding was maintained on that basis, Territory Housing would likely operate at a profit for the foreseeable future."

Since 2000/01 the financial position of Northern Territory public housing has continued to deteriorate, due primarily to a moderate real fall in net rents received per dwelling, and a fall of 20 per cent in operating incomes. Consequently, even though operating expenditures have been reined in, the deficit per dwelling (before net interest and depreciation) is 28.2 per cent higher than it was in 2000/01. This has also been accompanied by significant stock losses, with stock falling by more than 600 dwellings or nearly 10 per cent.

In order for Northern Territory's public housing operating result to be restored to surpluses, all the rebate would need to be funded and all debt servicing liabilities discharged.

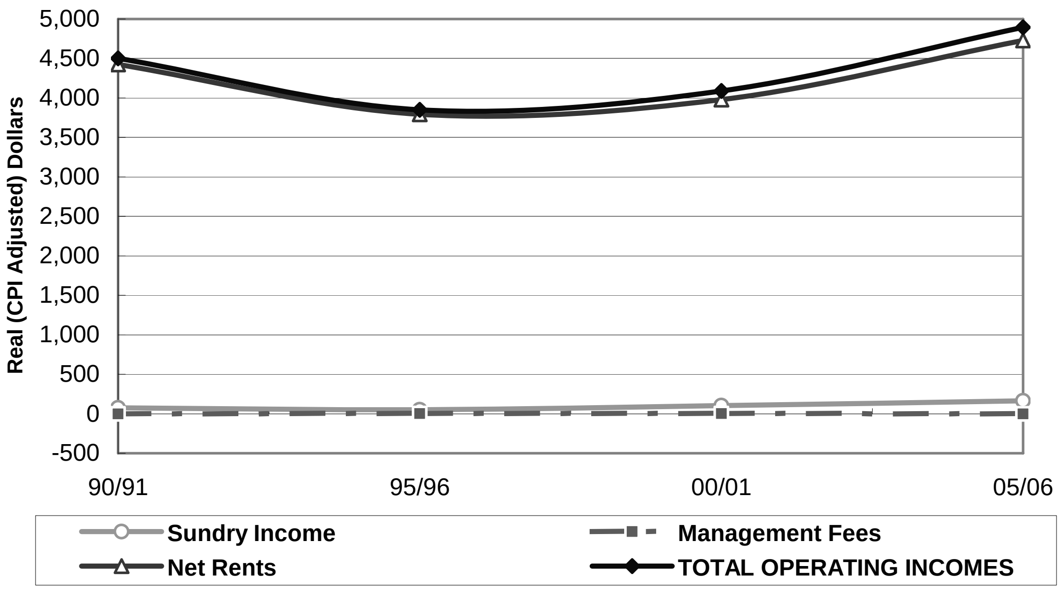
3.4 Queensland

3.4.1 Quantitative

Changes in net incomes

Graph 3.30 traces real net income per dwelling unit over the period 1990/91 to 2005/06, in Queensland (Qld).

Graph 3.30: Real incomes per dwelling unit ($), Qld, 1990/91 to 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Queensland Housing to 2005/06 Operating Deficits Project

Note: Includes public and Aboriginal housing owned and operated by the QDH but excludes any dwellings head-leased or leased from third parties.

Over the period 1990/91 to 2000/01, operating incomes fell substantially in real terms from $4,502 to $4,089 or approximately $400 per dwelling. Net rents per dwelling fell by a significant 10 per cent. Real rents constituted approximately 98 per cent of annual operating incomes throughout the decade.

The shift in trend evident in the late 1990s, however, continued between 2000/01 and 2005/06. In this period operating incomes increased in real terms by more than $800 per dwelling, from $4,089 to $4,894, or 19.7 per cent. This result is almost entirely due to a 18.8 per cent increase in net rents per dwelling, from $3,981 to $4,729.

Quantitative factors affecting operating incomes

Before 1994/95, Queensland operated a rent-charging policy whereby three rates of assessment were used at different income levels up to a maximum of 30 per cent of income, with a maximum rent of $200 per week.

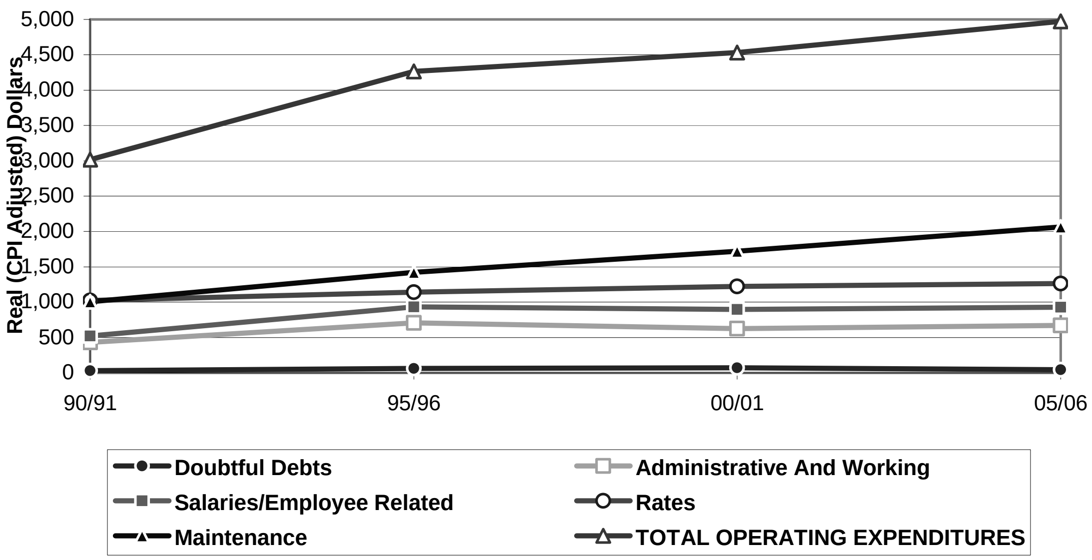
In August 1994, Queensland introduced a new policy that required payments of 21.5 per cent of income up to the first $300 income and then 26 per cent of income up to market rent. Although the new policy was revenue neutral, timing and systems issues in implementation had the effect of substantially reducing the rent paid in that year. Although no figures were kept on rebates prior to 1994, by 2000/01 Queensland had the highest proportion of tenants receiving rebates, with 9 out 10 tenants obtaining this concession.

Between 2000/01 and 2005/06, rebated tenants as a proportion of the total has virtually stabilised, only increasing from 90 per cent to 90.9 per cent (after subsidy removal). No historical data are available on priority and crisis allocations.

Expenditures and expenditure priorities

Graph 3.31 sets out real net expenditure per dwelling unit over the period 1990/91 to 2005/06.

Graph 3.31: Real expenditures per dwelling unit ($), Qld, 1990/91 to 2005/06

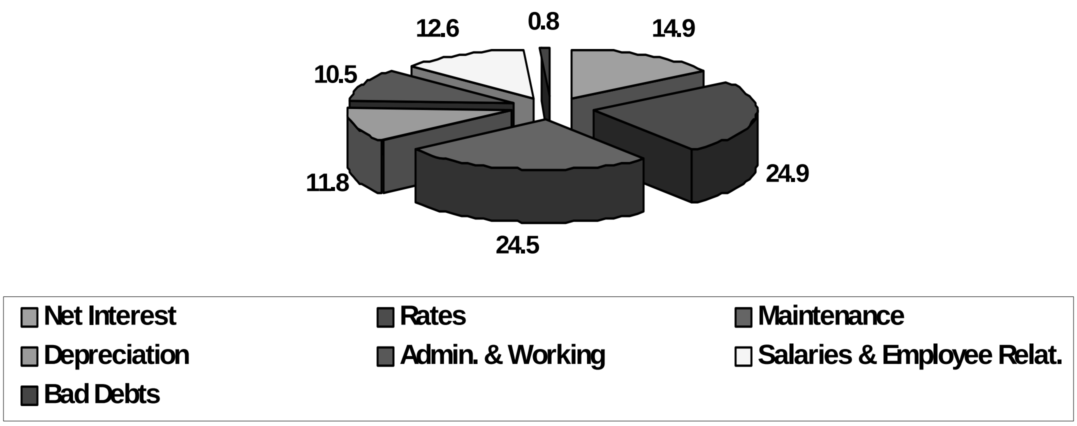


Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Queensland Housing to 2005/06 Operating Deficits Project

The graph shows that real operating expenditures per dwelling have increased from $3,016 in 1990/91 to $4,532 in 2000/01. Real increases in rates outgoings has been moderate, with rates expenditure per dwelling increasing from $1,026 to $1,224, (19 per cent). For the larger items, by far the most significant real increases in expenditure occurred in salaries and employee-related expenses and maintenance items, with salaries etc increasing from $519 to $894, or 72 per cent (although comparatively this was off a very low base figure). Maintenance increased from $1,008 to $1,720 (71 per cent). Total overhead increased in real terms from $951 to $1,517 or approximately 60 per cent.

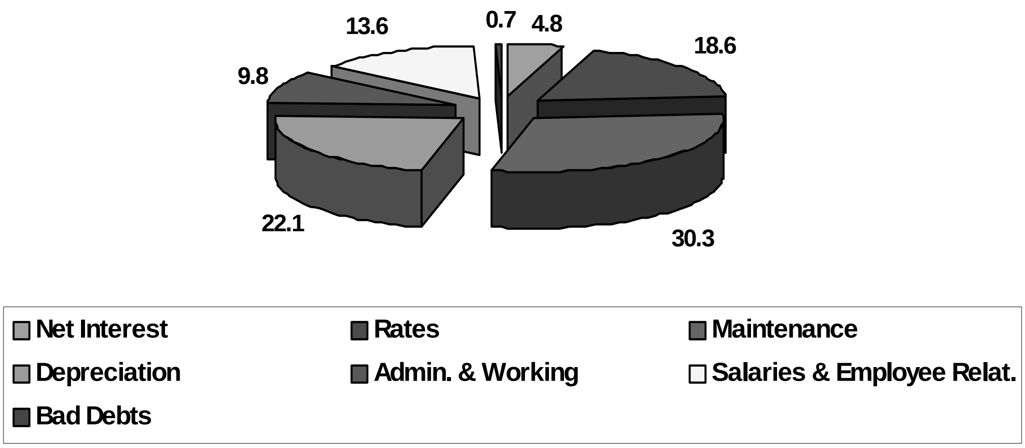
Reflecting these real changes in expenditure items, graphs 3.32 and 3.33 set out the proportion of total operating expenditure accounted for by each of the core expenditure items for the years 1990/91 and 2005/06.

Graph 3.32: Line items: percentage of real total public housing operating expenditure per dwelling (excluding rebates), Qld, 1990/91 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Queensland Housing to 2005/06 Operating Deficits Project

Graph 3.33: Line items: percentage of real total public housing operating expenditure per dwelling (excluding rebates), Qld, 2005/06 (June 2006 dollars)



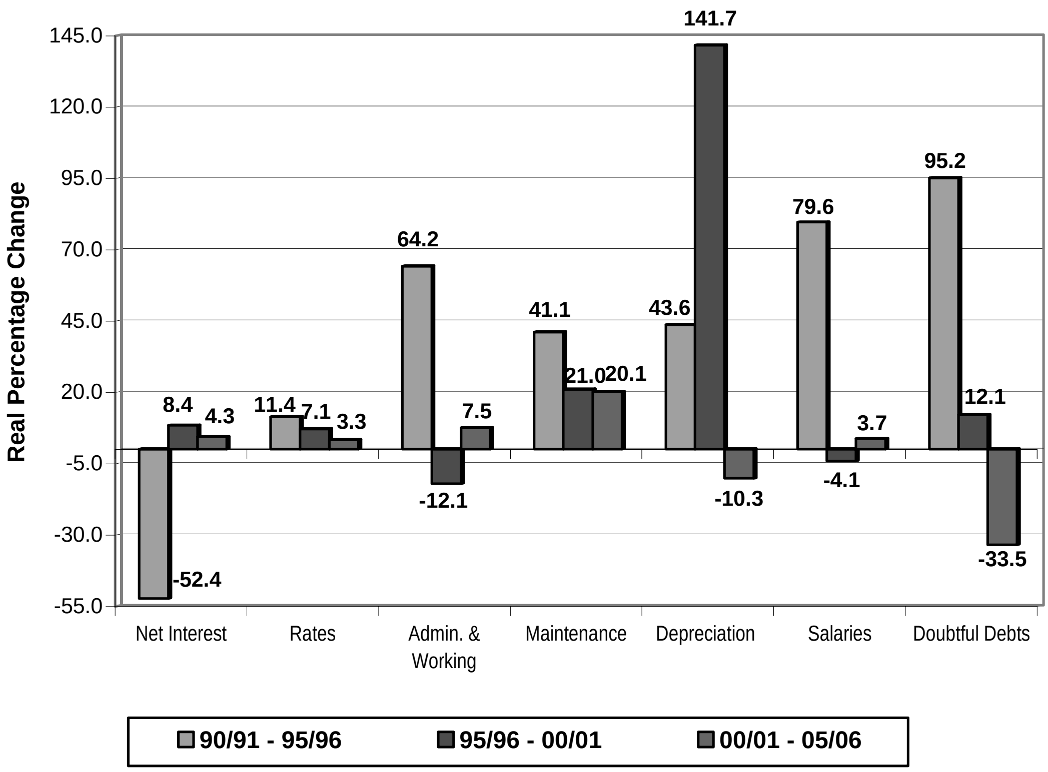
Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Queensland Housing to 2005/06 Operating Deficits Project

The graphs show how the proportion of the Queensland Department of Housing's (QDoH's) total expenditure per dwelling for each item (including depreciation and net interest) has changed over the period. The proportion of total expenditure absorbed by both net interest (down from 14.9 per cent to 4.8 per cent) and rates (down from 24.9 per cent to 18.6 per cent) has declined dramatically.

Administration and working expenditure has declined slightly (from 10.5 per cent to 9.8 per cent), as has bad debts (from 0.8 per cent to 0.7 per cent). By far the greatest change in proportions has occurred in depreciation, increasing from 11.8 per cent to 22.1 per cent of total operating expenditures. Salaries have only increased slightly in percentage terms from 12.6 per cent to 13.6 per cent. Maintenance now absorbs 30.3 per cent of QDoH's total expenditure on public housing, having increased from 24.5 per cent.

Graph 3.34 sets out the real percentage change in the costs of key line items.

Graph 3.34: Real percentage change in key line items, Qld, 1990/91 to 2005/06



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Queensland Housing to 2005/06 Operating Deficits Project

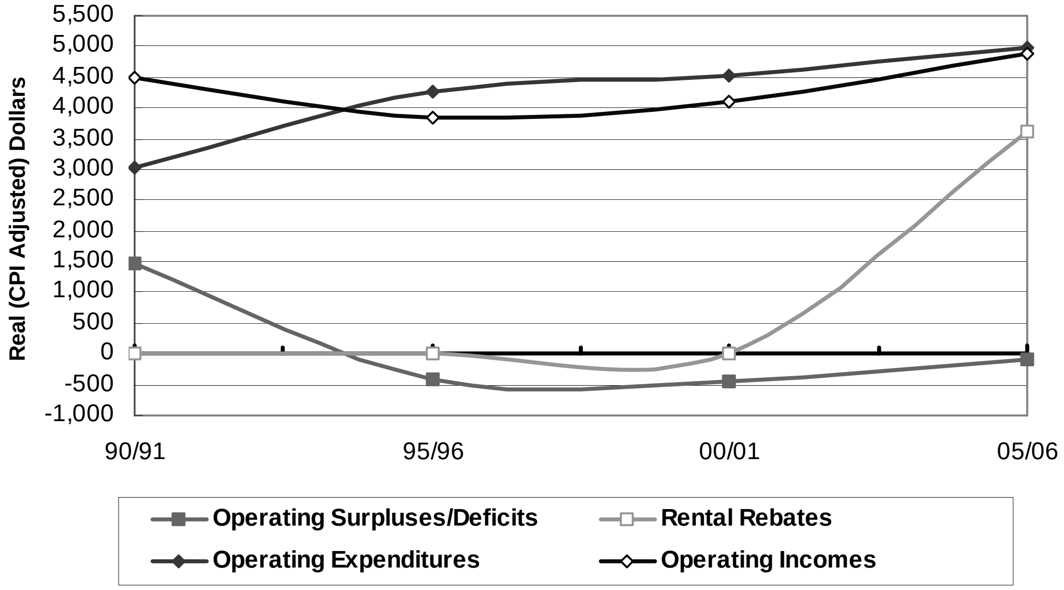
Over the period 1990/91 to 2000/01, there was a very significant real decline in the cost per dwelling for net interest, moderate changes in rates and administration and working items, and major real percentage increases in maintenance, salaries and related expenses, and depreciation.

Since 2000/01, with the exception of maintenance, growth in the remaining expenditure items has been modest, with all items growing by less than 10 per cent and depreciation falling by –10 per cent.

Operating income, expenditure and surplus/deficits

Graph 3.35 sets out the trends in operating surpluses/deficits excluding net interest and depreciation.

Graph 3.35: Real operating surpluses/deficit per dwelling ($), 1990/91 to 2005/06



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Queensland Housing to 2005/06 Operating Deficits Project

In 1990/91 the QDoH produced a real surplus per dwelling (excluding net interest and depreciation) of nearly $1,486, which fell steadily until 1994/95 when the first small deficit was recorded. Thereafter up to 2000/01 deficits were recorded, increasing to –$442 per dwelling.

In the same period, real expenditures increased substantially (from $3,016 to $4,532) and net incomes per dwelling fell steadily from $4,502 to $4,089.

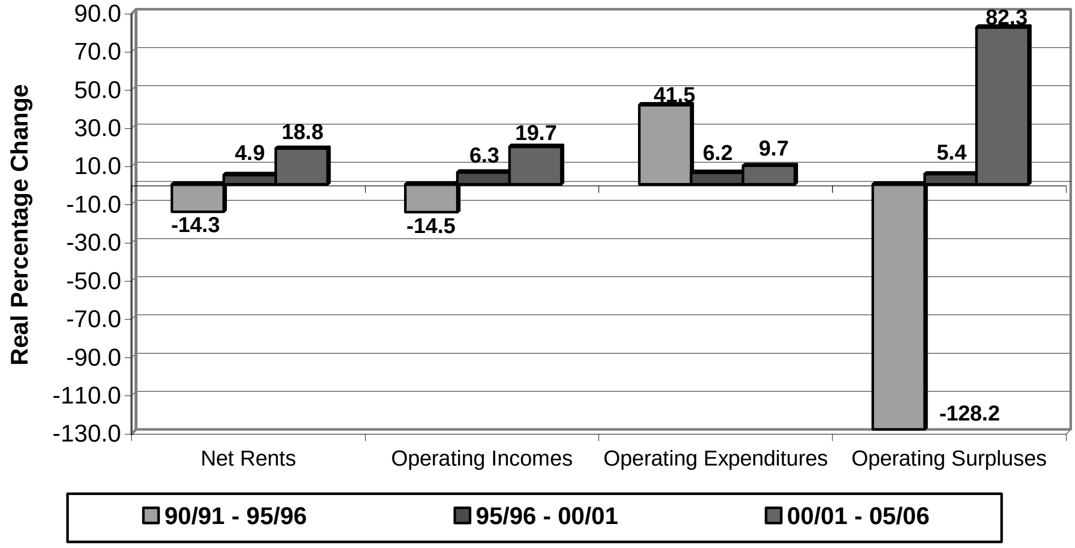
Since 2000/01, however, these trends have been dramatically reversed, with real expenditures only growing moderately to $4,973 per dwelling, while net incomes grew rapidly to $4,894, reducing the average deficit per dwelling to just –$78 in 2005/06.

Graph 3.36 sets out the real percentage change in net rents, operating incomes, expenditures and surpluses/deficits.

To summarise, over the period 1990/01 to 2000/01, real operating incomes (net of grants and interest earned) decreased by –9 per cent, while real operating expenditures grew by 50 per cent, resulting in a deficit growth of 130 per cent.

Since 2000/01, however, real net rents have increased by 18.8 per cent, real operating incomes by 19.9 per cent, and operating expenditures by a modest 9.7 per cent, while there has been an 82.3 per cent improvement in the deficit.

Graph 3.36: Real percentage change in net rents, incomes, expenditures and surpluses/deficits, Qld, 1990/91 to 2005/06

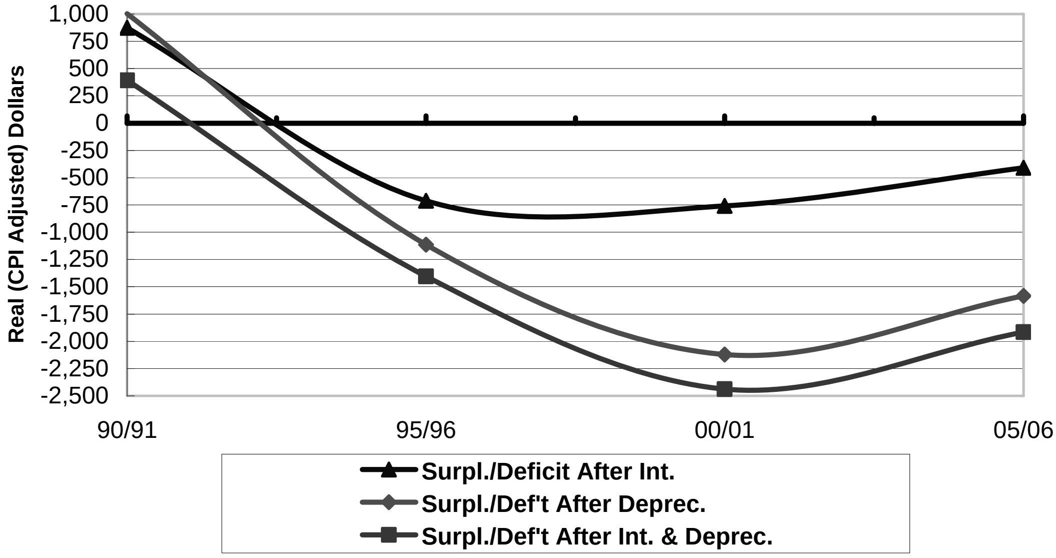


Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Queensland Housing to 2005/06 Operating Deficits Project

Impact of net interest and depreciation

Graph 3.37 sets out the impact of net interest and depreciation on the operating surplus/deficit.

Graph 3.37: Real surplus/deficit per dwelling after 'add backs' ($), Qld, 1990/91 to 2005/06



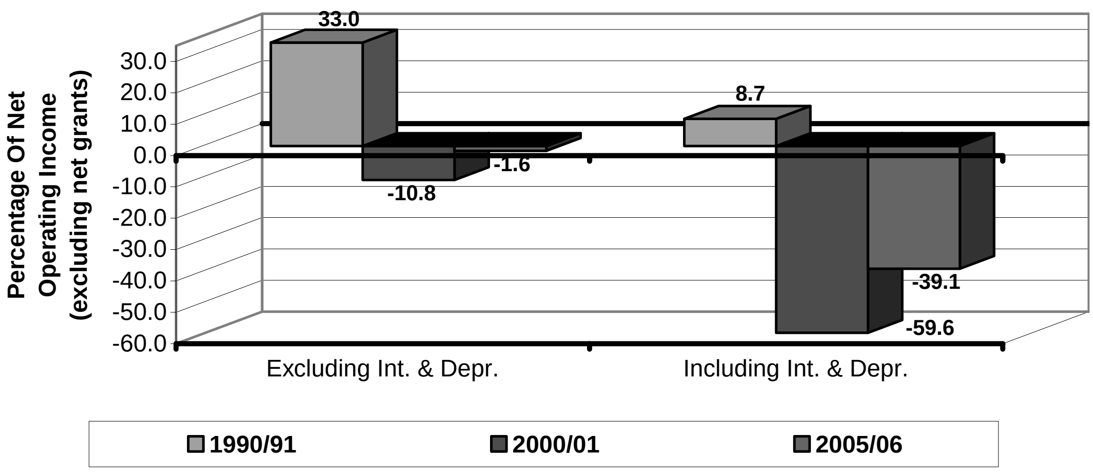
Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Queensland Housing to 2005/06 Operating Deficits Project

It is clear from Graph 3.37 that while the impact of net interest costs has declined to small proportions, until 2000/01 depreciation cost increases had more than offset the reduction in net interest. In 1990/91 net interest reduced the surplus by approximately

$611 per dwelling. Depreciation reduced the surplus by a further $484 to $1,002. In 2000/01, however, net interest added only $316 to the expenditure line, but depreciation of some $1,679 increased the operating deficit from –$442 to –$2,121 or by approximately –$1,679.

Graph 3.38 sets out the operating deficits as a proportion of net income before and after net interest and depreciation.

Graph 3.38: Real public housing operating surpluses/deficits as percentage of net income before grants, Qld, 1990/91, 2000/01 and 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Queensland Housing to 2005/06 Operating Deficits Project

These results reinforce the earlier comments on the impact of net interest and depreciation, which increased substantially until 2000/01, primarily due to depreciation. Since that time the impact of depreciation has been moderately reduced with net interest stable. In 1990/91 these expenditure components reduced the surplus by more than 25 per cent of net income, whilst in 2005/06 they added about 38 per cent to the deficit as a percentage of net income.

The importance of rebates

We were unable to analyse the impact of rental rebates due to the early data being unavailable.

3.4.2 Qualitative

Key responses from the operational deficits questionnaire, 1990/91 to 2000/01: 2004 study

> "The QDoH respondent indicated that tighter targeting and changes in household composition was leading to a steady decline in the real net rent received per dwelling as higher income, and multiple income households moved out and are replaced by lower income and more numerous single income households.
>
> During the decade there were two significant changes to rent setting policies. In 1994 a new policy was introduced where, for the first $300 of a tenants income rent was set at 21.5% of income and for any income in excess of $300, rent was set at 26%of the additional income up to market rent, (prior to this change rent was based on up to 30% of income until a maximum of $200 or market rent was reached). In 1997 maximum rent

was set at a flat 25% of income for all new tenants after the date of the policy was introduced, up until market rents were introduced.

The geographic structure of Queensland, and its climatic influences demand a regionalised structure for the administration of the public housing portfolio, and this makes some expenditure items more expensive.

The Department has commenced a major upgrading program, whereby it is spending $90m in 2002/2003 plus a similar amount in 2003/2004. Due to a new system based on property inspections and comprehensive condition information responsive maintenance has declined but regular cyclical maintenance has increased. Rates represent a significant component of outgoings' and have grown at a rate faster than inflation.

With the current Commonwealth policy settings, tight targeting and demand for improved quality of services, public housing is probably unsustainable if there is no change to the funding policies of the Commonwealth Government."

Key responses to the operating deficits questionnaire: 2005/06

"In 2005 a single rate of rent assessment of 25 per cent was introduced together with a redefining of a concessional rate of 10 per cent, which is now only applied to young household member[s] under 25 years of age. In 2006 rents are now being reviewed annually instead of twice a year.

The spread of public housing across the state including in rural and remote areas impacts on costs as the difficulty of access increase staff (time and travel) and material (transport costs, availability) costs.

Significant funds have been injected into maintenance and upgrades over the past few years to address asset degradation."

Queensland Housing: conclusions

The 2004 Report stated:

"In the last decade Queensland Housing has been most affected by the focus on tighter targeting and has focused heavily on improving the quality and management of its stock and on eliminating any debt servicing requirement. These priorities have been reflected in:

- the greatest increase in the proportion of rebated tenants of all Housing Authorities and a rapid and long term decline in real rents per dwelling and hence Net Income per dwelling. This decline has partly been reinforced by rent policy changes which capped rents at market, which in many places where Queensland Housing operates is very low. This decline in Real Income per dwelling can be expected to continue until such time as any trend to smaller households is completed and the proportion of rebated tenants and priority allocations reach saturation;
- rapid increases in real Maintenance per dwelling, as a result of asset improvement and management systems being introduced, although it can be anticipated that these increases will cease at some point in the near future as the large majority of the stock reach quality and inclusion control benchmarks;
- a commensurate increase in the amount of depreciation provisioning required per dwelling as asset restructuring and market developments act to improve the average value per dwelling unit;

- relatively high growth in both the Salaries and related expenses and Maintenance components of expenditures, being reflected in Operating Expenditure growing by 55% over the period;
- some improvements in tenants' ranking of both their satisfaction with the service provided and the quality of their dwelling;
- elimination of a significant amount of the debt servicing burden.

It would appear that the majority of any cost savings which can be accrued from debt reduction and asset restructuring (through lower maintenance), have been achieved.

It should be noted, however, that at 90% of rebated tenants Queensland cannot be far from the likely 'saturation point' for lower income entries and Net Rent can then be expected to stabilise. With the likely future short term trends in Net Income, and the current trends in some costs, it is probable that without any change to the distribution of tenant incomes and funding parameters, the business in the short term will continue to generate larger deficits. Either additional funding will need to be provided to Queensland Housing or some other solution will need to be found."

Since 2000/01 the operating position in Queensland has substantially improved, primarily as a result of two main management initiatives:

- changes in rent-charging policy that have substantially boosted real revenue per dwelling; and
- a bearing down on expenditure items such that total expenditure growth per dwelling has been kept within single digits.

Notwithstanding the above, there have been stock losses of the order of approximately 900 dwellings.

Although rebated tenants as a proportion of the total appear to have plateaued, priority and crisis allocations are still at relatively low levels. The current rent-charging initiatives are unlikely to be able to be repeated as payments are bumping up against affordability barriers, and with increasing proportions of allocations to priority and crisis clients with very low incomes it can be anticipated that real revenue per dwelling may decline somewhat.

While there may be a brief return to operating surpluses in the near future, this may not be sustained without other major policy interventions.

3.5 South Australia

3.5.1 Quantitative

Changes in net incomes

Graph 3.39 traces real net income per dwelling unit over the period 1990/91 to 2005/06[2] in South Australia (SA).

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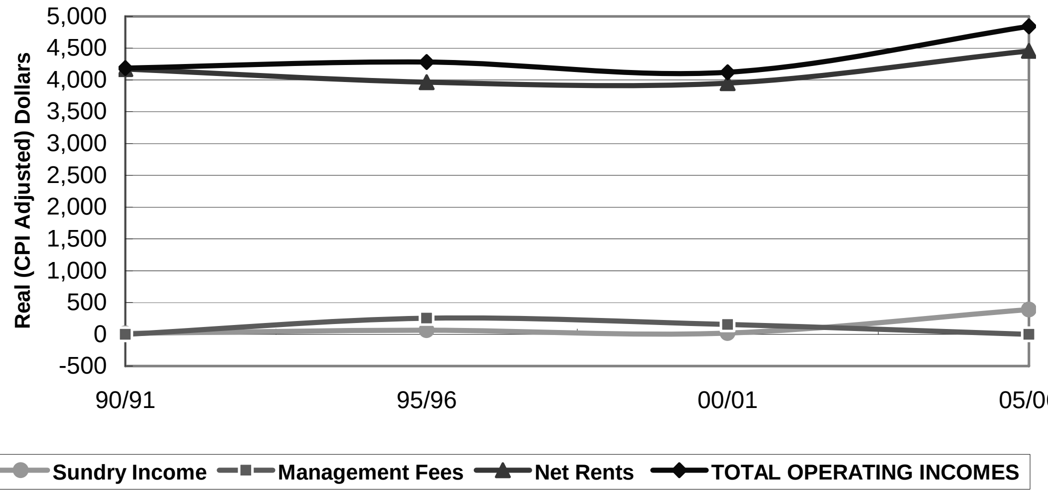
[2] Includes public community and Aboriginal housing owned and operated by the South Australian Housing Trust but excludes any dwellings head-leased or leased from third parties.

Graph 3.39: Real incomes per dwelling unit ($), SA, 1990/91 to 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from South Australian Housing Trust to 2005/06 Operating Deficits Project

Note: Incomes and expenditures have been adjusted to net out land tax costs and land tax reimbursements.

Over the period 1990/91 to 2000/01, operating incomes fell in real terms from $4,183 to $4,122 or by –$61 per dwelling. Net rents per dwelling fell by 5.3 per cent. Real rents constituted more than 93 per cent of annual operating incomes throughout the decade.

Since 2000/01 real operating incomes have increased more rapidly, growing to $4,845 or by 17.6 per cent. This reflects the real increase in net rents, which have increased up to $4,458 per dwelling or by 12.8 per cent. The difference is due to a one-off increase in sundry incomes.

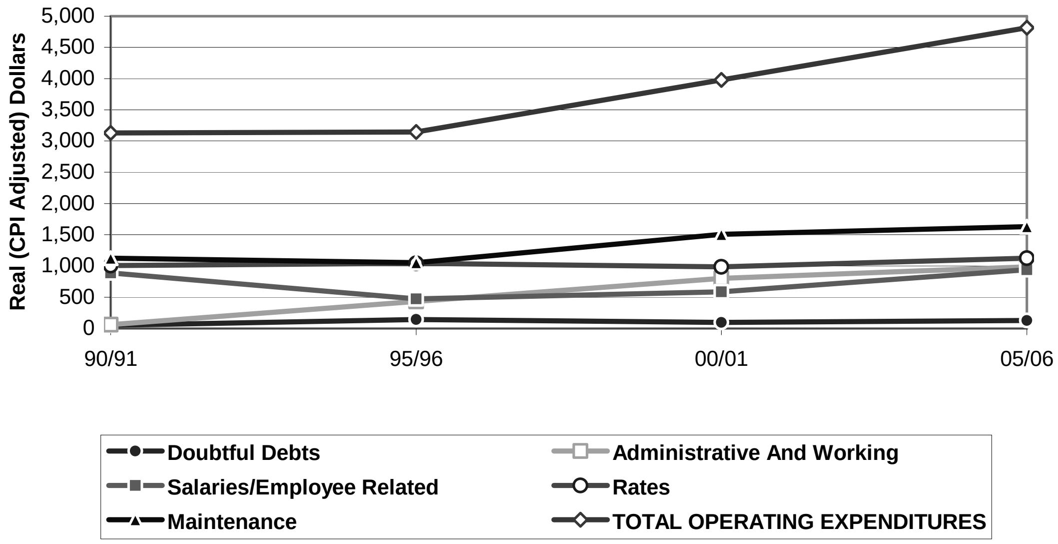
Quantitative factors affecting operating incomes

Over the period 1990/91 to 2000/01, rebated tenancies increased from 73 per cent to 85 per cent of the total and (more importantly) priority crisis and emergency allocations increased from 13 per cent of all new allocations to 50 per cent. Since 2000/01 rebated tenancies appeared to have stabilised at 85.1 per cent of the total, while priority allocations have fallen slightly to 46 per cent of all new allocations.

Expenditures and expenditure priorities

Graph 3.40 sets out real net expenditure per dwelling unit over the period 1990/91 to 2005/06.

Graph 3.40: Real expenditures per dwelling unit ($), SA, 1990/91 to 2005/06



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from South Australian Housing Trust to 2005/06 Operating Deficits Project

The graph shows that real operating expenditures per dwelling have increased from $3,130 in 1990/91 to $3,978 in 2000/01. There were substantial real decreases in both salaries and related expenses and net interest, with the former declining from $891 to $585, while the latter fell from $1,443 to $1,004.

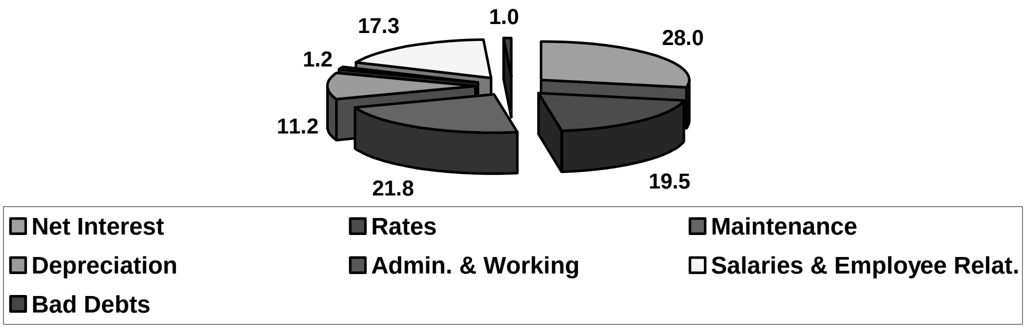
Real rates expenditures remained essentially flat throughout the decade, while real increases in maintenance outgoings were significant, with maintenance expenditure per dwelling increasing from $1,123 to $1,508 (up 34 per cent).

Leaving aside bad debts, which are a very small absolute amount, by far the most significant real increases in expenditure occurred in the depreciation and administrative and working items, with the former increasing from $577 per dwelling to $1,178 (or by 104 per cent) and the latter from $62 to $800 (or by 1,201 per cent). Total overhead increased in real terms from $953 to $1,386 or by approximately 45 per cent over the period.

Since 2000/01 net interest has continued to decline in real terms, falling from $1,004 to $783 per dwelling, and with the exception of depreciation and maintenance expenditure, growth in the other items has been substantial, with rates increasing 14.3 per cent, and administration and working 23.3 per cent, and salaries and employee-related from $585 to $942 or by 61 per cent.

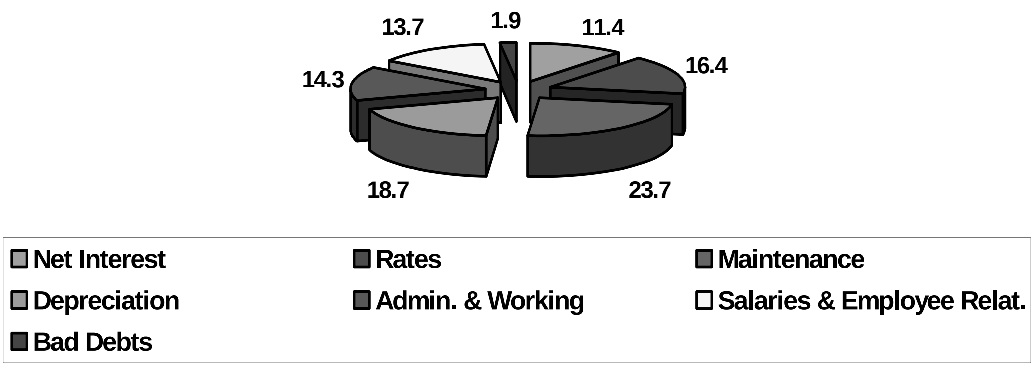
Depreciation, however, only increased from $1,178 to $1,290 or by 8 per cent, and maintenance by 8.1 per cent. Reflecting these real changes in expenditure items, graphs 3.41 and 3.42 set out the proportion of total operating expenditure occupied by each of the core expenditure items for the years 1990/91 and 2005/06.

Graph 3.41: Line items: percentage of real total public housing operating expenditure per dwelling (excluding rebates), SA, 1990/91 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from South Australian Housing Trust to 2005/06 Operating Deficits Project

Graph 3.42: Line items: percentage of real total public housing operating expenditure per dwelling (excluding rebates), SA, 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from South Australian Housing Trust to 2005/06 Operating Deficits Project

The graphs show how the proportion of the South Australian Housing Trust's (SAHT's) total expenditure per dwelling for each item (including depreciation and net interest) has changed over the period 1990/91 to 2005/06.

The proportion of total expenditure absorbed by net interest (down from 28 per cent to 11.4 per cent), and salaries and related expenses (down from 17.3 per cent to 13.7 per cent), has declined dramatically.

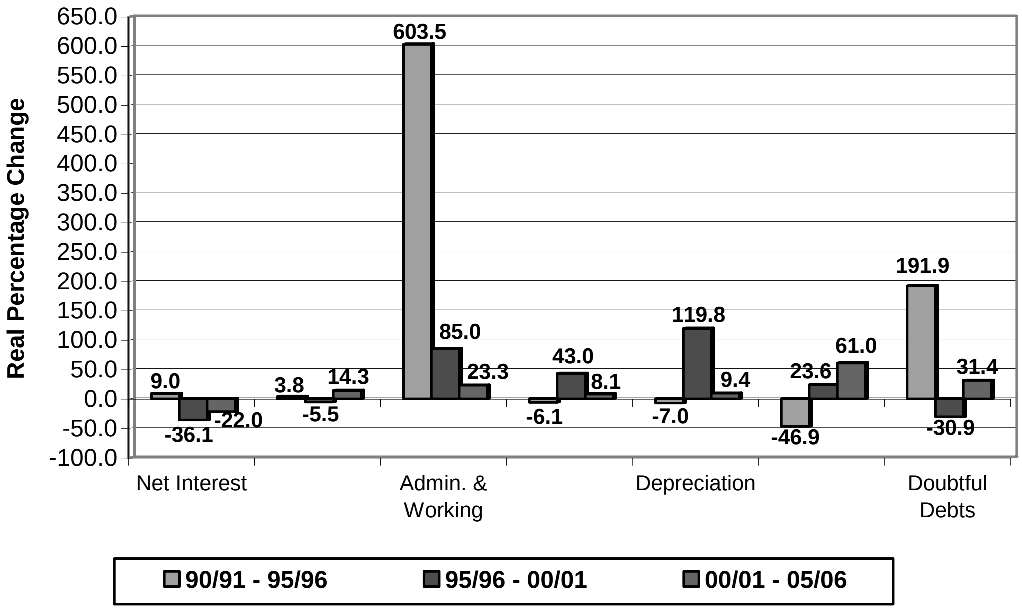
Rates expenditure has declined moderately, while maintenance expenditure has increased slightly as a proportion of total expenditures per dwelling, with the former decreasing from 19.5 per cent to 16.4 per cent and the latter increasing from 21.8 per cent to 23.7 per cent.

As outlined in the analysis of expenditure item growth, by far the greatest change in proportions has occurred in depreciation and administrative and working items, with the former increasing from 11.2 per cent to 18.7 per cent of total operating expenditures, and the later increasing from 1.2 per cent to 14.3 per cent.

In reality, the fall in salaries and increase in administrative and working items may reflect a shift from in-house supply to outsourcing, with fees replacing salaries.

Graph 3.43 sets out the real percentage change in the costs of key line items.

Graph 3.43: Real percentage change in key line items, SA, 1990/91 to 2005/06



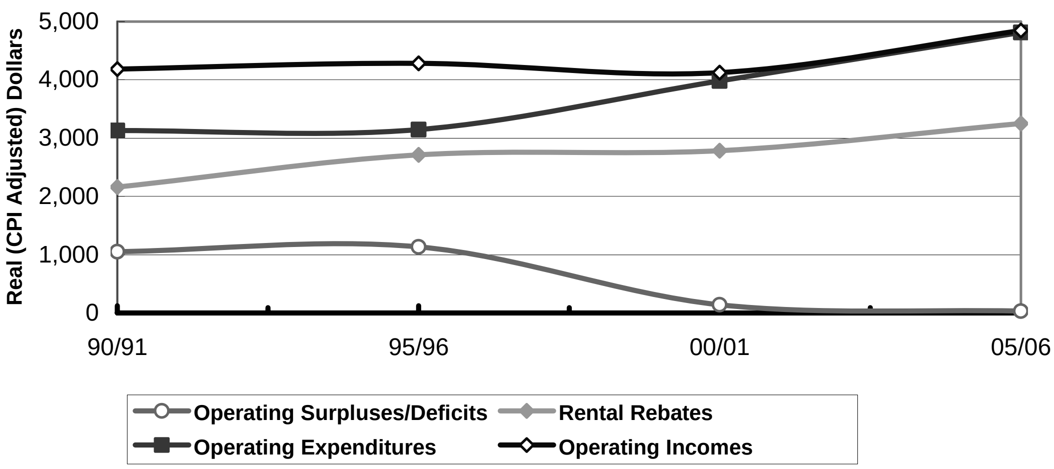
Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from South Australian Housing Trust to 2005/06 Operating Deficits Project

The graph reflects the findings outlined earlier – significant real declines in the cost per dwelling for net interest, significant changes in maintenance and major real percentage increases in doubtful debts, depreciation, and administration and working items.

Operating incomes, expenditure and surplus/deficits

Graph 3.44 sets out the trends in operating surpluses/deficits excluding net interest and depreciation.

Graph 3.44: Real operating surpluses/deficits per dwelling ($), SA, 1990/91 to 2005/06

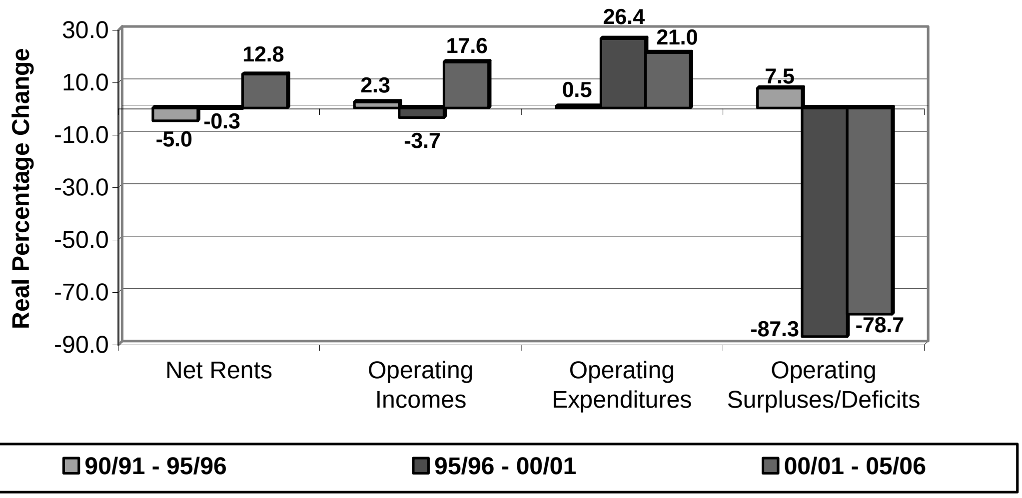


Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from South Australian Housing Trust to 2005/06 Operating Deficits Project

In 1990/91 the SAHT produced a real surplus per dwelling (excluding net interest and depreciation) of $1,054, and between 1990/91 and 2000/01 this declined steadily to $144. The graph clearly shows that these trends have continued post 2000/01, with operating surpluses all but eliminated in 2005/06 (down to $31 per dwelling) primarily as a result of the twin trends of slow revenue growth accompanied by faster expenditure growth.

In2005/06 operating incomes ($4,845) exceeded operating expenditures ($4,815) by just this $31 per dwelling. Graph 3.45 sets out the real percentage change in net rents, operating incomes, expenditures and deficits.

Graph 3.45: Real percentage change in net rents, incomes, expenditures and surpluses/deficits, SA, 1990/91 to 2005/06



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from South Australian Housing Trust to 2005/06 Operating Deficits Project

To summarise, over the period 1990/91 to 2000/01, real operating incomes (net of grants and interest earned) increased by only 15.8 per cent, while real operating expenditures grew by 53 per cent, resulting in a reduction of the operating surplus of approximately –97 per cent.

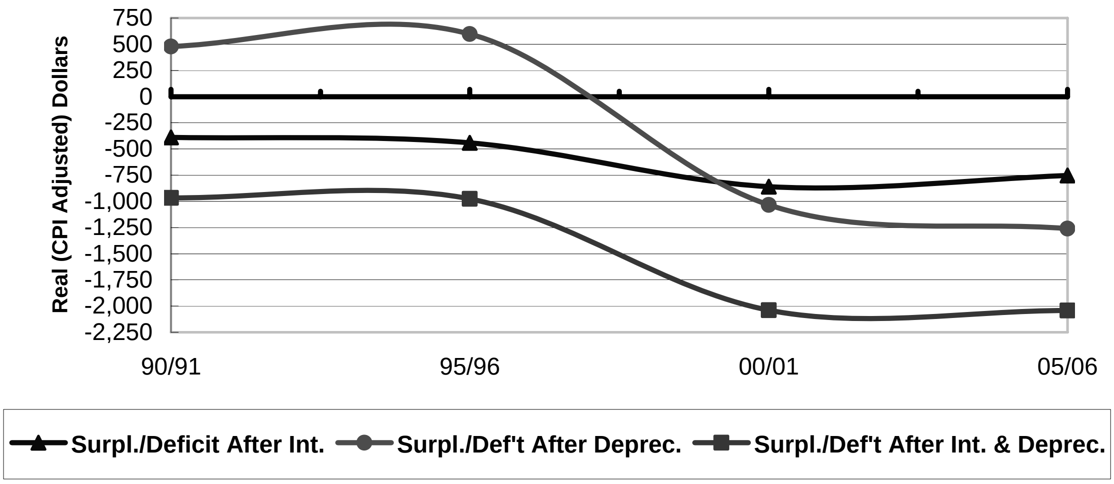
Since 2000/01 these trends have continued, albeit at a slower pace, with real operating incomes increasing by 17.6 per cent and real operating expenditures increasing by 21 per cent, with real operating surpluses falling by a further 79 per cent.

Impact of net interest and depreciation

Graph 3.46 sets out the impact of net interest and depreciation on the operating surplus/deficit.

It is clear from Graph 3.47 that the impact of net interest costs and depreciation has increased slightly over the period 1990/91 to 2000/01. In 1990/91 net interest moved the real operating result from surplus to deficit by approximately –$389 per dwelling. Depreciation added a further –$577 to the deficit, increasing it from –$389 to –$966 per dwelling. In 2000/01, however, net interest added –$1004 to the expenditure line, and depreciation some –$1178, turning the operating surplus from $193 to –$2,039 or approximately 50 per cent more per dwelling unit more than that which occurred a decade earlier. Since 2000/01 the impact of net interest and depreciation has stabilised, moving the deficit by only $5 more to –$2,043.

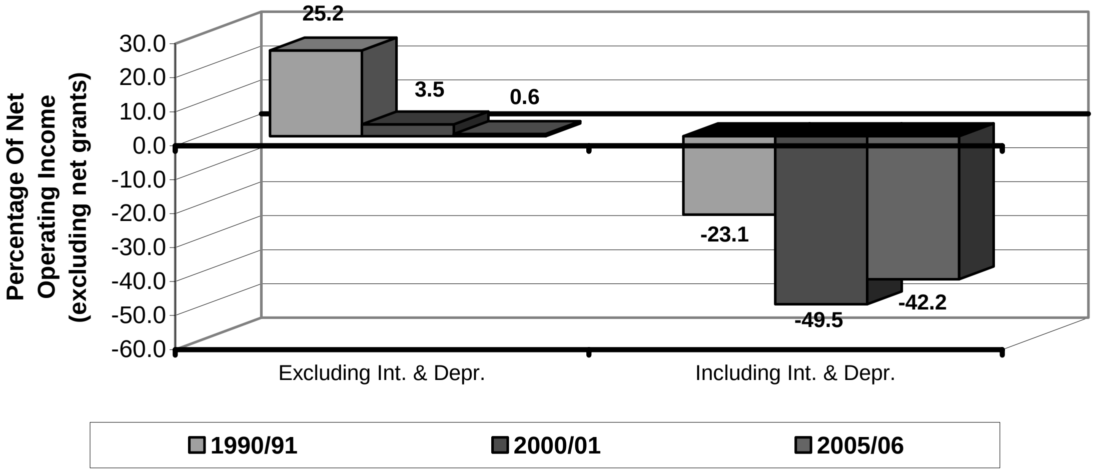
Graph 3.46: Real surplus/deficit per dwelling after 'add backs' ($), SA, 1990/91 to 2005/06



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from South Australian Housing Trust to 2005/06 Operating Deficits Project

Graph 3.47 sets out the operating deficits as a proportion of net income before and after net interest and depreciation.

Graph 3.47: Real public housing operating surpluses/deficits as percentage of net income before grants, SA, 1990/91, 2000/01 and 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from South Australian Housing Trust to 2005/06 Operating Deficits Project

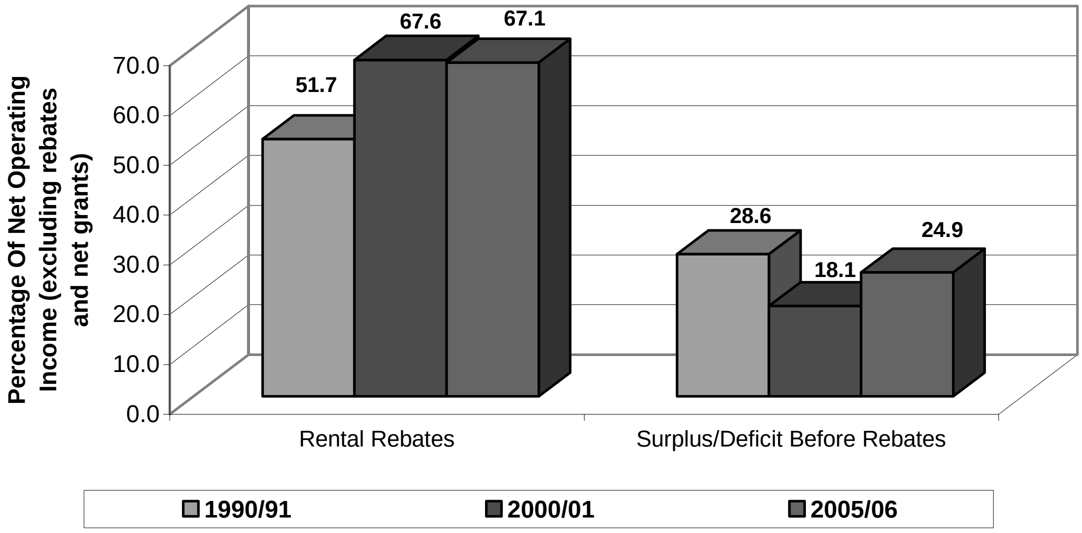
These results reinforce the earlier comments on the impact of net interest and depreciation. These expenditure components were still affecting the operating deficit in 2005/06 in nearly double the proportions of 1990/91.

The importance of rebates

Real average rental rebates per dwelling increased significantly from $2,161 in 1990/91 to $2,786 in 2000/01, and increased by a further 16.6 per cent to $3,249 in 2005/06.

Graph 3.48 sets out rental rebates as a proportion of net income before grants.

Graph 3.48: Real public housing rental rebates as percentage of net income before grants, SA, 1990/91, 2000/01 and 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from South Australian Housing Trust to 2005/06 Operating Deficits Project

The graph clearly shows that the impact of rental rebates relative to net incomes before rebates has increased by about 30 per cent over the period 1990/91 to 2000/01. Since that time the impact of rental rebates has declined slightly.

As with all states examined so far, with the exception the Northern Territory, and as in 2000/01, if the SAHT received a commercial return based on market rents it would be financially robust and provide an appropriate operating rental return of about 15 per cent net per annum. Combined with the capital gain, this would provide a very good double digit annual rate of return.

In the case of the SAHT, recognising the real cost of the CSO and providing a cash payment for rebates would ensure the continued viability of the sector.

3.5.2 Qualitative

Key responses from the operational deficits questionnaire 1990/91 to 2000/01: 2004 study

"The South Australian respondent made the following comments.

Whilst average rents charged to tenants have dropped minimally, the proportion of total households being single person households (and hence single versus double incomes and therefore much lower rents) has grown steadily from 46% in June 1996 to 66% in January 2003.

The rent charging policy has changed several times in the last decade, moving from a sliding scale to a flat 25% of household income for all the different types of households, with the exception of under 21's and the elderly.

The Trust has embarked on a process of debt restructuring and reduction by using the proceeds of asset sales to pay off all commercial loans. At the beginning of the decade these totalled $367m outstanding but had been fully prepaid by December 1999.

Maintenance backlogs have increased slightly over the years, but an asset restoration program has been ramped up during the last ten years, and over the last two years there has been a heavier focus on improving the amenity level of dwellings.

Salaries and Overhead costs have been reduced due to organisational restructurings.

Customer debt has increased slightly after March 2000 but new strategies to reduce evictions due to debt have been effective. The nature and extent of demand for Trust services by people with complex and multiple needs has impacted on tenancy management. The Trusts strategic directions of successful tenancies and sustainable communities underpin the service provided to customers. The Trust therefore places strong importance on early intervention to support customers at risk.

Operating deficits, (including Net Interest and Depreciation), effectively prevent the Trust from expanding and have doubled between 1999/00 and 20001/02. At the time of the interview a plan was being prepared for Cabinet setting out options to eliminate deficits."

Key responses from the operational deficits questionnaire: 2005/06

"In real terms, the income of households entering public housing has not changed significantly over time. While the proportion of new tenancies entering public housing on a rental subsidy since March 2000 has consistently been recorded [at] around 93 per cent, the proportion of existing tenancies receiving a rental subsidy has remained constant at 85 per cent.

The rent to income scale of 1999 was replaced with a flat rate system (17 per cent for bedsits, 19 per cent for cottage flats, 19.5 per cent for households earning less than the Centrelink Adult Allowee Rate, 25 per cent for all other households).

The release of the Housing Plan for South Australia in March 2005 included the announcement of a scheme to help social housing tenants into home ownership (the EquityStart scheme). Part of the proceeds from the sale of social housing assets under this scheme are reserved for the repayment of existing interest-bearing debt, in addition to scheduled repayments. Additional debt reduction for the most part depends on proceeds from asset sales.

Over the past 5 years SAHT urban renewal and redevelopment projects have restructured housing stock, removing from stock 2819 older properties that had reached the end of their serviceable life. This housing stock has been replaced with 1679 new properties, hence reducing responsive expenditure for that component of the older housing stock that was replaced.

The [SHAT's] Asset Condition Database currently reports that the average overall condition of the 44,529 residential assets surveyed is 3.56 of a total possible score of 5. This indicates that the overall condition of owned residential assets is fair.

Interest payments, and the associated Treasury Guarantee Fee, accounted for $41.7m of expenditure in 2005/06, which was 9.2 per cent of total operating expenses. This represents a substantial burden.

The 'Triennial Review of the South Australian Housing Trust', an independent report prepared by an external consulting firm in September 2005, estimated that approximately $5.7m per annum was being incurred as a result of providing non-housing related support services to tenants (with a further $9.0m attributable to non-tenant services). This is broadly consistent with internal estimates."

South Australian Housing Trust: conclusions

The 2004 report stated.

> "South Australia is probably the most advanced of all the States engaged in asset reconstruction and debt minimisation. In the last decade SAHT has sold over 10,000 dwellings, and has restructured the remaining portfolio, simultaneously engaging in a backlog maintenance program, embraced tighter targeting through the introduction of segmented waiting lists, provided significant tangible improvements to its services to its clients, and has focused on reducing debt servicing required by the organisation.
>
> These priorities have been reflected in:
>
> - a long term decline in real rents per dwelling and hence Net Income per dwelling. This decline was recently arrested by changes to rent policy, but because of comparatively low proportions of rebated tenants and priority allocations it can be expected to resume until such time as any trend to smaller households is completed and the proportion of rebated tenants and priority allocations reach saturation. In South Australia's case some considerable time may elapse before these conditions are reached;
> - a significant reduction in the cost of Salaries and Net Interest over the decade;
> - significant improvements in tenants' ranking of both their satisfaction with the service provided and the quality of their dwelling;
>
> Notwithstanding the above, it would appear that the majority of any cost savings which can be accrued from asset restructuring (through lower maintenance) and debt reduction have already been achieved. With the likely future trends in Net Income, and the current trends in costs, it is probable that without any change the business will require greater funding than that provided by untied grants. Either additional funding will need to be provided or SAHT will have to sell down or its assets in order to fund its operating shortfalls.
>
> What is most disturbing about the trends for SAHT is that they give the lie to the theory that focusing on asset management and reconstruction, minimising your debt servicing obligations and bearing down on the cost structure will be sufficient to maintain viability. Clearly it will not.
>
> It is also clear, however, that if the full cost of SAHT's community service obligation was correctly recognised (i.e. if the difference between market rents and income related rents was fully funded) SAHT's Operating Deficit would become an equivalent surplus. As with most other public housing authorities, if funding was maintained on that basis, SAHT would likely operate at a profit for the foreseeable future."

Since 2000/01 there have been further stock reductions of 5,796 or 12.8 per cent of the stock, and consistent with the Trusts strategy to reduce debt by repayments from asset sales, debt servicing costs have fallen by 20 per cent.

However, operating incomes, while growing faster than inflation, are still not keeping pace with the growth in operating expenditures, and as a result the operating position before interest and depreciation continues to deteriorate. With nearly all client categories paying 25 per cent of income, the capacity to further increase revenue from rent charging changes is likely to be minimal. It appears, however, that the proportion of total tenants who are receiving rebates has now plateaued and the proportion of new allocations going to priority and crisis cases has actually declined. Consequently it may be possible for net rent income to keep pace with inflation, even if, with current allocation priorities, there is little prospect of real revenue growth.

Meanwhile, expenditures continue to grow faster than revenues and are likely to continue to do so in the foreseeable future. Even with the repatriation of further debt, in the absence of substantial policy change, the operating position is likely to continue to deteriorate.

With significant asset improvement backlogs and an overall fair condition for the stock, the Trust is of the view that the only way in which appropriate asset refurbishment can be achieved is by supplementing capital grants with proceeds from the sale of dwellings.

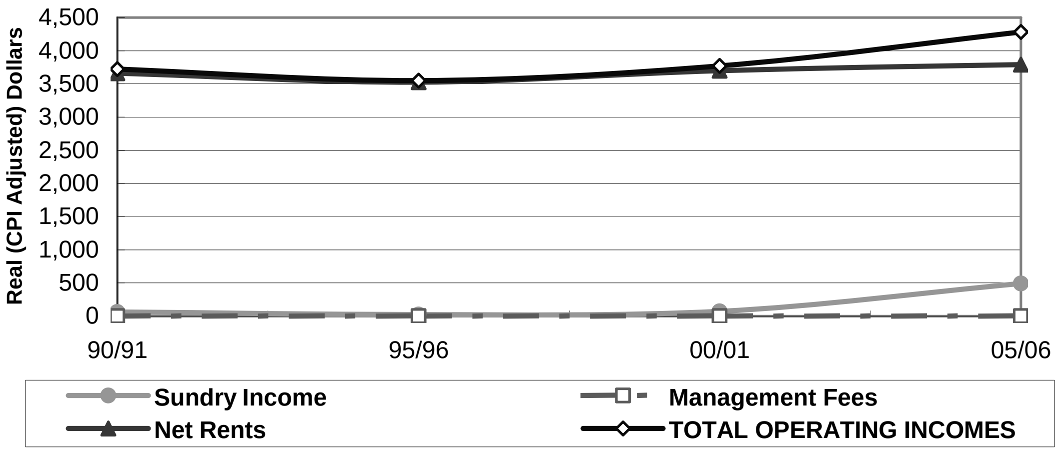
3.6 Tasmania

3.6.1 Quantitative

Changes in net incomes

Graph 3.49 sets out real net income per dwelling unit over the period 1990/91 to 2005/06 in Tasmania (Tas).

Graph 3.49: Real incomes per dwelling unit ($), Tas, 1990/91 to 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, Operating Deficits and Public Housing, Policy Options For Reversing The Trend, AHURI; and return from Housing Tasmania to 2005/06 Operating Deficits Project

Note: Includes public, community and Aboriginal housing owned and operated by the Housing Tasmania but excludes any dwellings head-leased or leased from third parties.

Over the period 1990/91 to 2000/01, total operating incomes per dwelling only increased slightly in real terms from $3,722 to $3,770 or by about $48. Net rents per dwelling increased by just 3.6 per cent. Real rents constituted more than 98 per cent of annual operating incomes throughout the decade.

Since 2000/01 real operating incomes per dwelling have increased by $514 to $4,284. However, $493 of the $514 is probably a once-off sundry income increase which is unlikely to be repeated. Without this once-off increase, real operating incomes per dwelling have increased by just $21 since 2000/01 or just over half of 1 per cent.

Quantitative factors affecting operating incomes

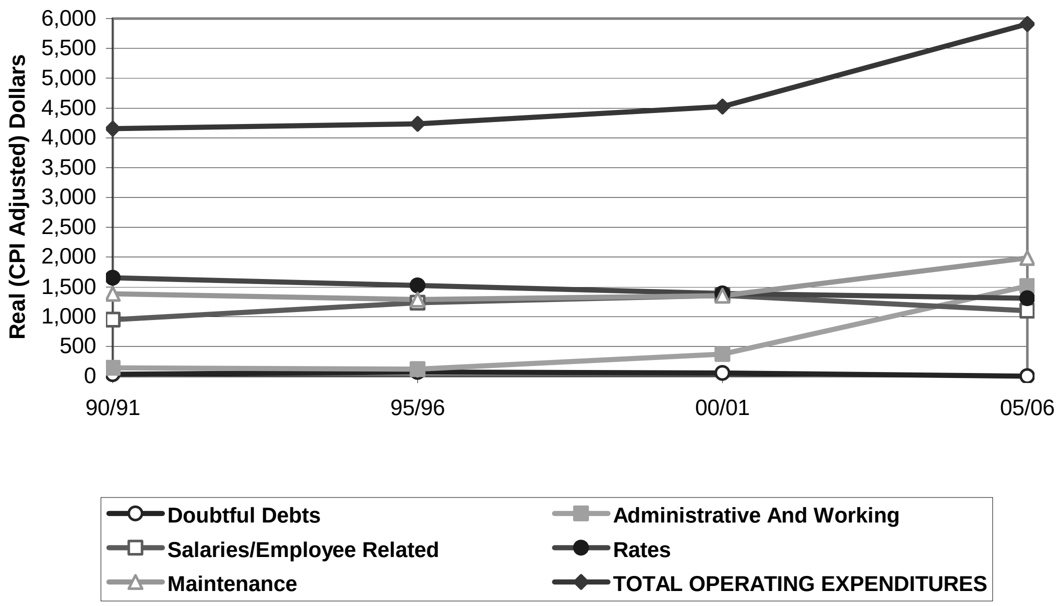
While rebated tenants remained the same proportionately throughout the period 1990/91 to 2000/01 (85 per cent of tenancies), priority crisis and emergency allocations increased from 35 per cent of all new allocations to 100 per cent, the highest of all Australian states. Changes to rent policy have partially offset the negative financial impact of increasing priority allocations.

Since 2000/01 rebated tenancies have fallen somewhat (78 per cent) but allocations to priority, crisis and emergency are still well in excess of 90 per cent of the total.

Expenditures and expenditure priorities

Graph 3.50 sets out real net operating expenditure per dwelling unit over the period 1990/91 to 2005/06.

Graph 3.50: Real expenditures per dwelling unit ($), Tas, 1990/91 to 2005/06



Sources: Hall J and Berry M, 2004, Operating Deficits and Public Housing, Policy Options For Reversing The Trend, AHURI; and return from Housing Tasmania to 2005/06 Operating Deficits Project

Real operating expenditures per dwelling increased from $4,156 in 1990/91 to $4,523 in 2000/01. There were significant real falls in both net interest and rates, the former decreasing from $1,730 per dwelling to $993, and the latter falling from $1,651 to $1,389.

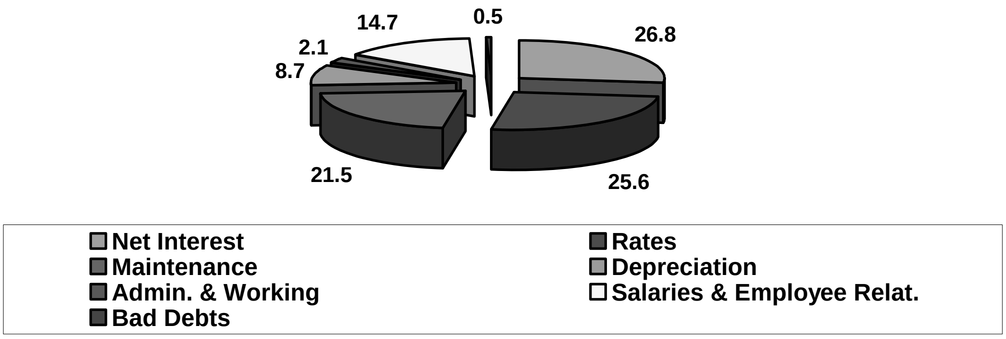
Maintenance expenditure per dwelling remained almost unchanged, while salaries and related expenses increased substantially from $949 to $1,358. Leaving aside doubtful debts (because of the very small size of the amounts), the largest increases occurred with respect to administration and working items, increasing from $139 to $370. Total overhead costs per dwelling increased dramatically (albeit off a small base), from $1,087 to $1,728.

Since 2000/01 both net interest and salaries and employee-related expenditures per dwelling have fallen nearly 20 per cent, with the former falling to $811 and the latter to $1,098.

Notwithstanding the above, real operating expenditures grew by almost 30 per cent to $5,906 (before net interest and depreciation), primarily on the back of major increases in administration and working expenses and maintenance, with the former growing to $1,515 and the latter to $1,984.

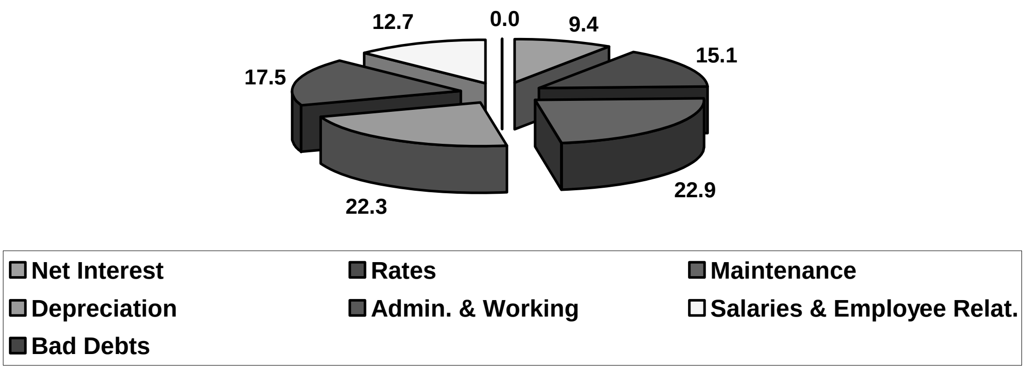
Reflecting these real changes in expenditure items, graphs 3.51 and 3.52 set out the proportion of total operating expenditure occupied by each of the core expenditure items for the years 1990/91 and 2005/06.

Graph 3.51: Line items: percentage of real total public housing operating expenditure per dwelling (excluding rebates), Tas, 1990/91 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, Operating Deficits and Public Housing, Policy Options For Reversing The Trend, AHURI; and return from Housing Tasmania to 2005/06 Operating Deficits Project

Graph 3.52: Line items: percentage of real total public housing operating expenditure per dwelling (excluding rebates), Tas, 2005/06 (June 2006 dollars)



Source: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI, and Return From Housing Tasmania To 2005/06 Operating Deficits Project

The graphs show how the proportion of Housing Tasmania's total expenditure per dwelling for each item (including depreciation and net interest) has changed over the period.

The proportions of total expenditure absorbed by both net interest (down from 26.8 per cent to 9.4 per cent) and rates (down from 25.6 per cent to 15.1 per cent) have declined dramatically.

Salaries and employee-related has fallen slightly from 14.7 per cent to 12.7 per cent

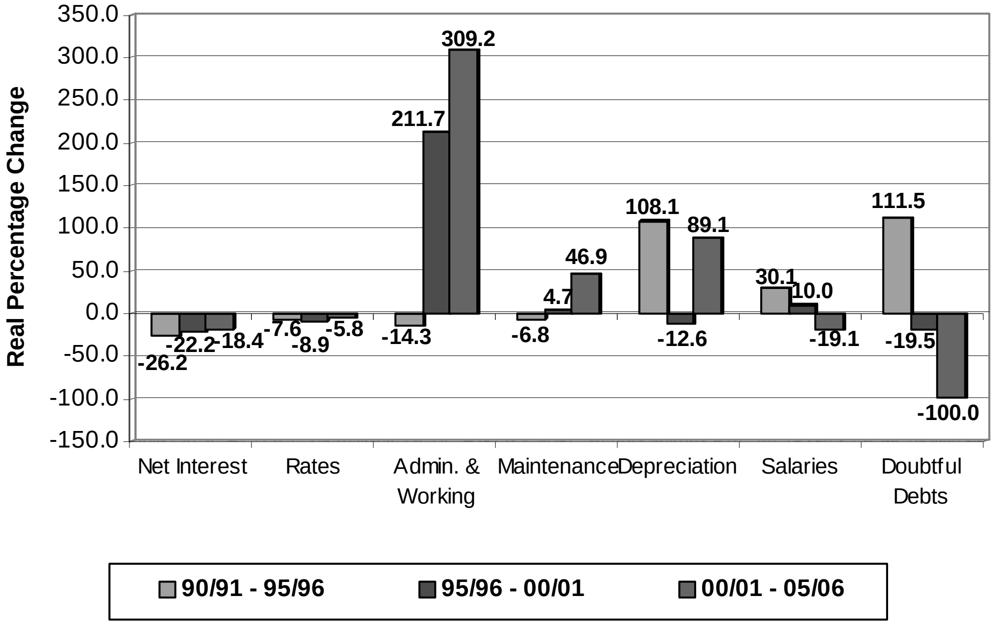
By far the greatest increase in proportions has occurred in depreciation and administrative and working items, with the former increasing from 8.7 per cent to 22.3 per cent of total operating expenditures, and the latter increasing from 2.1 per cent to 17.5 per cent.

Total overhead increased from 16.8 per cent to 30.2 per cent. Housing Tasmania spends more on overheads than either maintenance or rates.

Maintenance expenditure has remained almost the same as a proportion of total expenditures, increasing only slightly (21.5 per cent to 22.9 per cent).

Graph 3.53 sets out the real percentage change in the costs of key line items.

Graph 3.53: Real percentage change in key line items, Tas, 1990/91 to 2005/06



: Hall J and Berry M, 2004, Operating Deficits and Public Housing, Policy Options For Reversing The Trend, AHURI; and return from Housing Tasmania to 2005/06 Operating Deficits Project

The graph reflects the findings outlined earlier – very significant real declines in the cost per dwelling for net interest and rates, no significant change in salaries and employee-related, and major real percentage increases in depreciation, administration and working and maintenance expenditures.

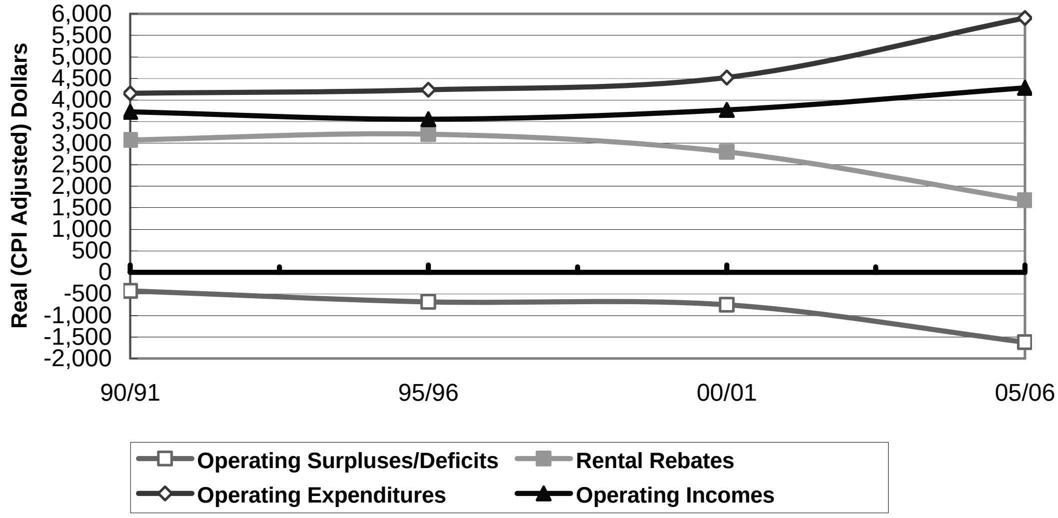
Operating income, expenditure and surplus/deficits

Graph 3.54 sets out the trends in operating surpluses/deficits, excluding net interest and depreciation.

In 1990/91 Housing Tasmania produced a real deficit per dwelling (excluding net interest and depreciation) of –$433 and this increased to –$753 in 2000/01.

Since 2000/01 operating expenditures (excluding net interest and depreciation) grew at almost three times the rate of operating incomes and this deficit per dwelling has now increased to –$1,622.

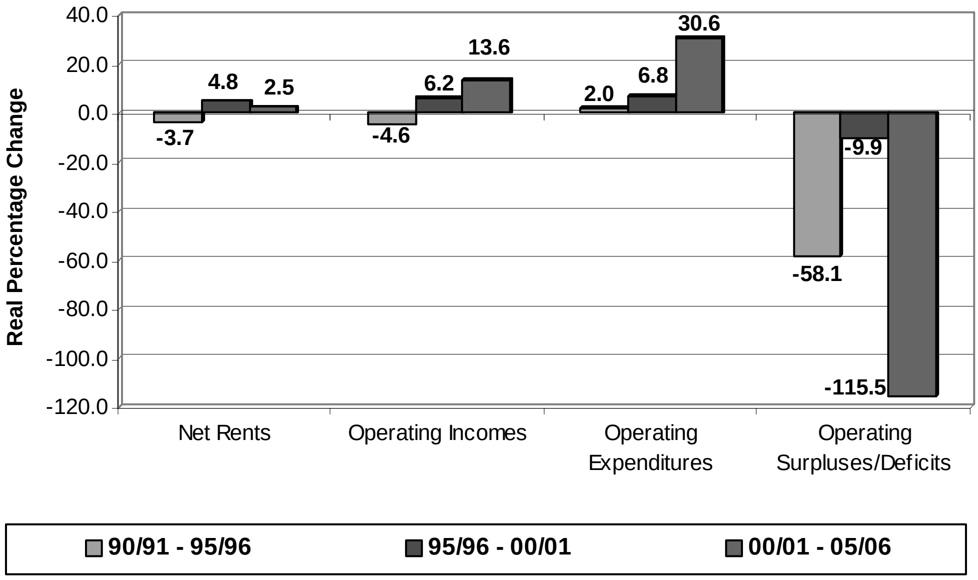
Graph 3.54: Real operating surpluses/deficits per dwelling ($), Tas, 1990/91 to 2005/06



Sources: Hall J and Berry M, 2004, Operating Deficits and Public Housing, Policy Options For Reversing The Trend, AHURI; and return from Housing Tasmania to 2005/06 Operating Deficits Project

Graph 3.55 sets out the real percentage change in net rents, operating incomes, expenditures and surpluses/deficits.

Graph 3.55: Real percentage change in net rents, incomes, expenditures and surpluses/deficits, Tas, 1990/91 to 2005/06



Sources: Hall J and Berry M, 2004, Operating Deficits and Public Housing, Policy Options For Reversing The Trend, AHURI; and return from Housing Tasmania to 2005/06 Operating Deficits Project

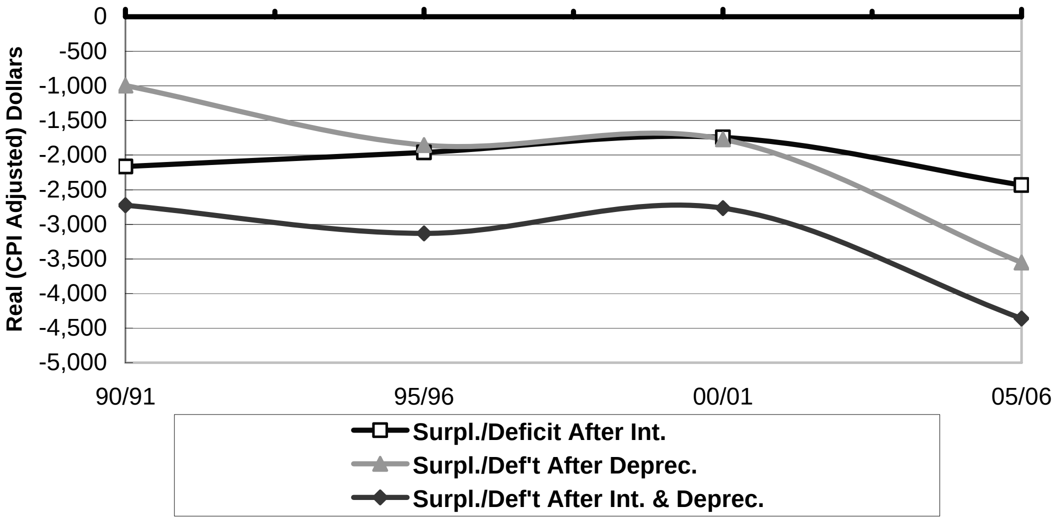
To summarise, over the period 1990/91 to 2000/01, real operating incomes (net of grants and interest earned) increased by only l per cent, as did net rents, while real operating expenditures grew by 9 per cent, resulting in deficit growth of 74 per cent.

Since 2000/01, while real operating incomes have grown by 13.6 per cent, net rents have only increased by 2.5 per cent (almost all the increase due to a one-off sundry income adjustment). Real operating expenditures have grown by nearly 31 per cent, resulting in a 115 per cent increase in the operating deficit per dwelling.

Impact of net interest and depreciation

Graph 3.56 sets out the impact of net interest and depreciation on the operating surplus/deficit.

Graph 3.56: Real surplus/deficit per dwelling after 'add backs' ($), Tas, 1990/91 to 2005/06



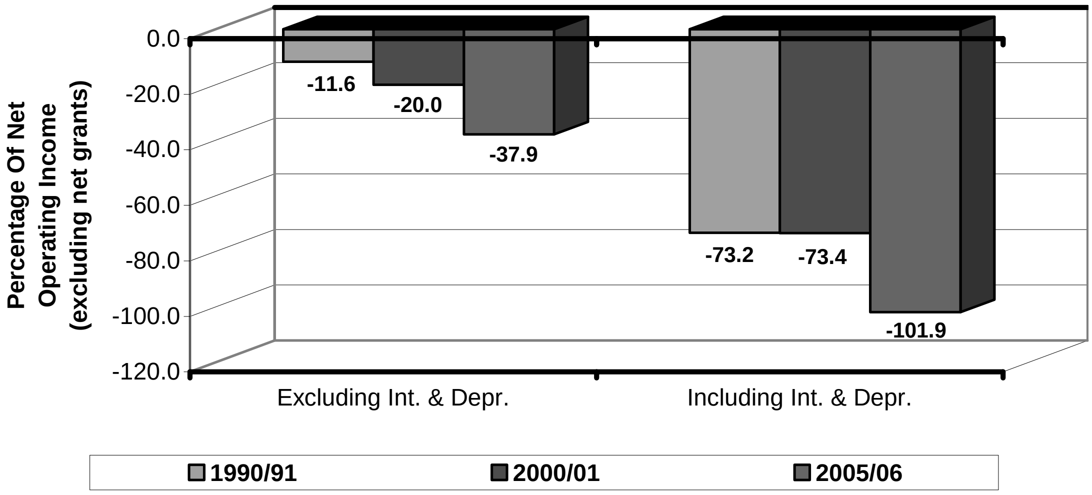
Sources: Hall J and Berry M, 2004, Operating Deficits and Public Housing, Policy Options For Reversing The Trend, AHURI; and return from Housing Tasmania to 2005/06 Operating Deficits Project

The impact of net interest costs and depreciation has declined slightly over the period 1990/91 to 2000/01, with the decline in net interest being offset somewhat by the increase in depreciation. In 1990/91 net interest increased the deficit by –$1,730 per dwelling. Depreciation added a further –$562 to the deficit, increasing it after interest from –$2,164 to –$2,725 per dwelling. In 2000/01, however, net interest added only $993 to the expenditure line, and depreciation some $1,1021, increasing the operating deficit from –$753 to –$2,767 or by slightly less than a decade earlier.

Since 2000/01, while there has been a 20 per cent decline in the impact of net interest (to $811), depreciation has almost doubled per dwelling (up to $1,903), so that the operating deficit before interest and depreciation (–$1,622) more than doubles to –$4,364.

Graph 3.57 sets out the operating deficits as a proportion of net operating income before and after net interest and depreciation.

Graph 3.57: Real public housing operating surpluses/deficits as percentage of net income before grants, Tas, 1990/91, 2000/01 and 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, Operating Deficits and Public Housing, Policy Options For Reversing The Trend, AHURI; and return from Housing Tasmania to 2005/06 Operating Deficits Project

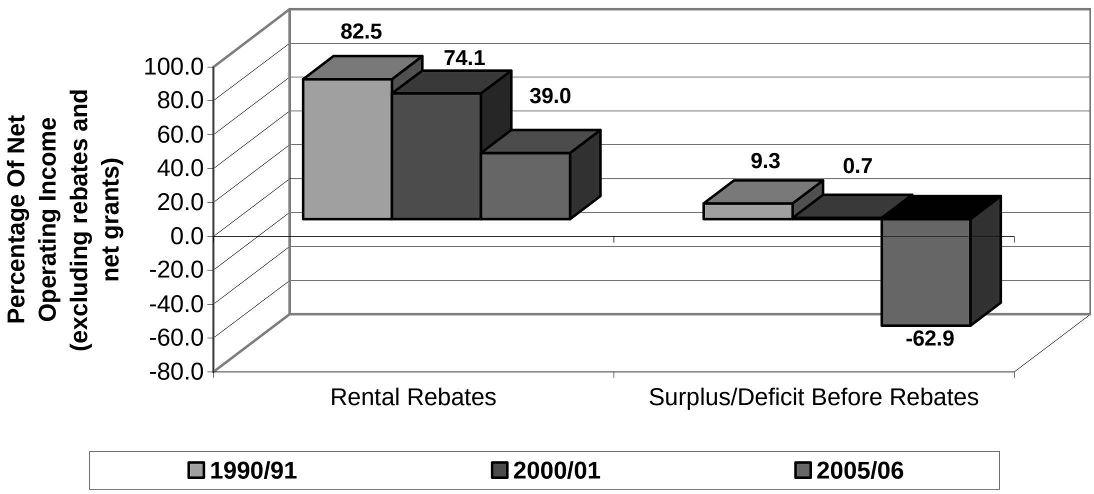
These results reinforce the earlier comments on the impact of net interest and depreciation. In 1990/91 they increased the deficit by over 60 per cent of net operating income, while in 2000/01 they only increased it by about 53 per cent of net operating income.

Since 2000/01, however, the impact has escalated sharply, so they now add in excess of 60 per cent of net operating income.

The importance of rebates

Graph 3.58 sets out rental rebates and grants as a proportion of net income before grants.

Graph 3.58: Real public housing rental rebates as percentage of net income before rebates and grants, Tas, 1990/91, 2000/01 and 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, Operating Deficits and Public Housing, Policy Options For Reversing The Trend, AHURI; and return from Housing Tasmania to 2005/06 Operating Deficits Project

Over the period 1990/91 to 2000/01, real average rental rebates per dwelling have actually declined slightly from $3,072 to $2,795. Since 2000/01 they have fallen dramatically to $1,670 per dwelling.

The impact of rental rebates relative to net incomes before rebates has declined but they still remain very significant. In 2000/01, if Housing Tasmania had received a commercial return based on market rents it would have generated a small surplus.

Since 2000/01, however, a substantial deterioration has occurred. To return to operating surpluses per dwelling, Housing Tasmania would now need to receive a cash payment for rebates, eliminate all debt and find a solution to the high depreciation.

3.6.2 Qualitative

Key responses to the operational deficits questionnaire, 1990/91 to 2000/01: 2004 study

The 2004 study stated:

> "The Tasmanian respondents were unequivocal that both tighter targeting and greater and greater proportions of single income households were having a depressive effect on Net Rental Income. Priority allocations now represent 100% of new tenancies and single person households represent 48% of existing tenancies and 66% of households on the waiting list.
>
> The nature of the Tasmania housing market and distribution of a significant proportion of the stock into small towns and rural locations means stock outside Hobart has been expensive to maintain. There is some maintenance backlog but it is relatively small as the worst stock has been sold out as it is identified.
>
> However, the average age of the stock is 23 years and increasing and it can be anticipated therefore that real Maintenance costs will grow.
>
> Housing Tasmania is undertaking a program of restructuring its asset base whereby 3,500 sales over three years have been earmarked. It is intended to buy some 1,000 dwellings and use the remaining proceeds for debt reduction. At the current time the only debt remaining is the 4.5% concessional loans from the Commonwealth."

Key responses to the operational deficits questionnaire: 2005/06

> "The focus now is very much on special needs, priority and crisis accommodation. It represents a significant proportion of placements. The focus is considerably different [from] a decade ago.
>
> Maintenance backlogs is a very important issue for [Housing Tasmania]. To a large degree the costs have not yet "hit home". It is forecast to create financial tensions in the next few years as the portfolio ages. Therefore increased maintenance is a priority when funding is allocated.
>
> The "hidden" cost of not undertaking essential maintenance will begin to [have an] impact over the next three to five years.
>
> Modelling is currently being completed to determine the levels of funding required to adequately maintain the portfolio and, [while] not complete, indicative figures show that many millions of dollars will be required annually."

Housing Tasmania: conclusions

The 2004 study stated:

"Housing Tasmania's main priorities have been to restructure its assets and eliminate any commercial debt. In addition, it has focused upon improving the quality of the services it provides to its clients, and tighter targeting,

These priorities have been reflected in:

- almost flat Net Rents and hence Net Income per dwelling;
- substantial increases in both Salaries and Administration and Working expenditures as improvements in service quality and the extension of support services find their way into the bottom line;
- significant improvements in tenants, ranking of both their satisfaction with the service provided and the quality of their dwelling; and
- a halving of any debt servicing burden, which remains at very substantial levels of 26% of Net Income and is to be further addressed via asset sales.

Currently, 85% of tenants are rebated with the 15% unrebated tenants mitigating further Net Rent decline.

However, with 100% of new allocations being Priority, it can be expected that rebated tenants and smaller households will continue to increase as a proportion of total tenancies until such time as the proportion of rebated tenants reach saturation and the trend to smaller households is completed. Under these circumstances Real Net Rents per dwelling can be expected to decline in the near future.

However, whilst maintenance savings accruing from asset reconstruction may be small, elimination of the debt servicing would halve the existing deficit (before Depreciation) but it would still remain comparatively high. Whilst Overhead costs have grown strongly they are still around the average for the nine Housing Authorities.

Similar to most of the other State Housing Authorities, with the likely future trends in Net Income, and the current trends in overhead costs, it is probable that without any change to the distribution of tenant incomes, funding parameters, and cost structures the Deficit may continue to deteriorate.

Either additional funding will need to be provided or Housing Tasmania will have find other solutions.

It is also clear, however, that if the full cost of Housing Tasmania's community service obligation was fully recognised (i.e. if the difference between market rents and income related rents was fully funded), Housing Tasmania's Operating Deficit would become a very small surplus. Combined with some reduction in debt servicing and if funding was maintained on that basis, Housing Tasmania would likely operate at a profit for the foreseeable future."

Since 2000/01 there has been a dramatic deterioration in the operating deficit both before and after net interest and depreciation. This is primarily due to stagnating real incomes and rapidly increasing real expenditures. While there is some capacity to adjust net rents through changes to charging policies, it is no coincidence that the two states whose position has deteriorated the most are those who have made minimal changes to their rent-charging policies in the six years.

Moreover, there has been significant change in maintenance expenditures, so asset quality and asset backlogs are still a major concern. Also, 805 dwellings have been lost in the period 2000/01 to 2005/06 – this is some 6 per cent of the total stock. Therefore, without a substantial and recurring increase in revenues it is difficult to see how the deficit and asset position will not deteriorate further.

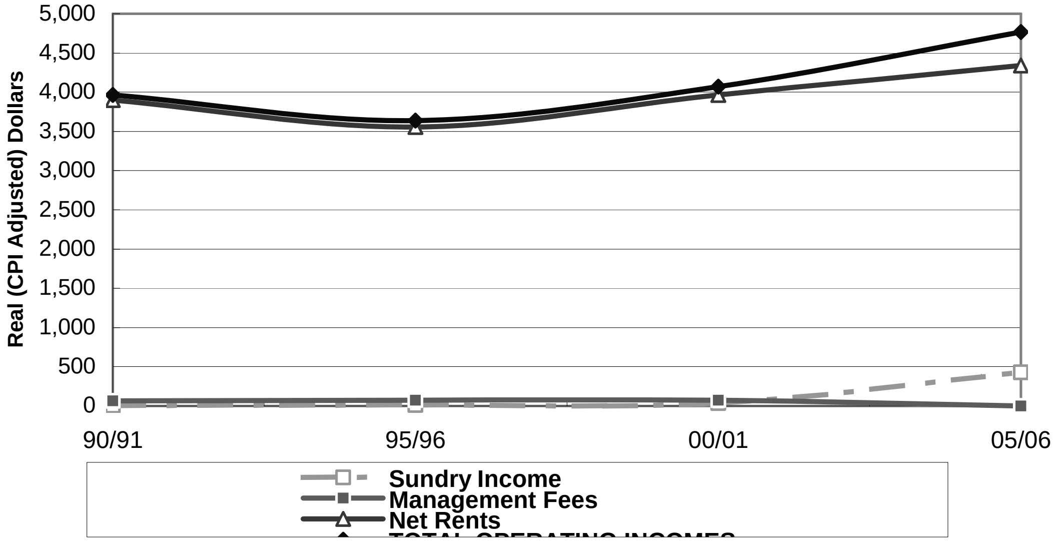
3.7 Victoria

3.7.1 Quantitative

Changes in net incomes

Graph 3.59 traces real net income per dwelling unit over the period 1990/91 to 2005/06[3] in Victoria (Vic).

Graph 3.59: Real incomes per dwelling per unit ($), Vic, 1990/91 to 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Office of Housing, Victoria to 2005/06 Operating Deficits Project

Note: Leased units have been subtracted from the total stock and net rents reduced by the average rent times the number of leased units. On the expenditure side, leasing expenses have been deleted.

Over the period 1990/91 to 2000/01, operating incomes per dwelling only increased in real terms from $3,965 to $4,072 or by about $105. Net real rents per dwelling rose by 1.6 per cent. Real rents constituted 97 per cent or more of annual operating incomes throughout the decade. Since 2000/01 net real rents have increased by nearly 10 per cent while real operating incomes have grown by 17.1 per cent. However, almost half of the growth is due to an abnormal once-off sundry income increase in 2005/06.

Quantitative factors affecting operating incomes

Over the period 1990/91 to 2000/01, rebated tenants increased from 85.5 per cent to 89.1 per cent and, more importantly, priority crisis and emergency allocations increased from 11.8 per cent of all new allocations to 67 per cent, the third-highest of all Australian states. Since 2000/01 rebated tenants as a proportion of the total have actually fallen slightly, to 86.3 per cent, but priority, emergency and crisis allocations

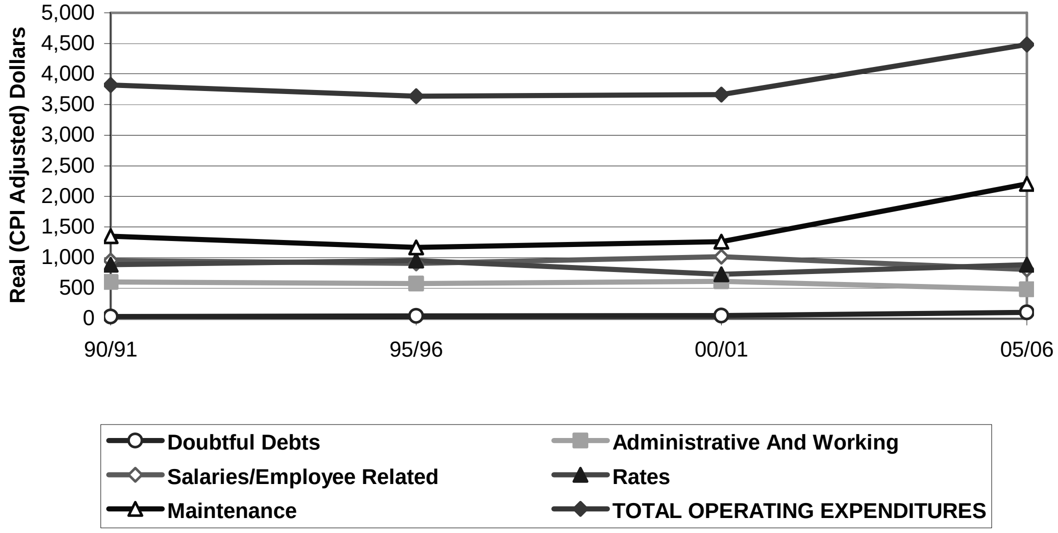
[3] Includes public, community and Aboriginal housing owned and operated by the Office of Housing but excludes any dwellings head-leased or leased from third parties.

as a proportion of total new allocations have increased slightly to 70.1 per cent. Victoria had several rent-charging policy changes throughout the full period.

Expenditures and expenditure priorities

Graph 3.60 sets out real net expenditure per dwelling unit over the period 1990/91 to 2005/06.

Graph 3.60: Real expenditures per dwelling unit ($), Vic, 1990/91 to 2005/06



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Office of Housing, Victoria to 2005/06 Operating Deficits Project

Note: Leasing expenses are excluded from the analysis to enable the 2005/06 comparisons across states and territories, and comparison with the 2000/01 analysis. In Victoria this excludes $12.9 million of leasing expenses from the total annual operating surplus/deficit. For the same reason of enabling comparisons, provisioning for bad debts has been excluded, though bad debts actually incurred have been included.

For the period 1990/91 to 2000/01, Victoria was the only state where real operating expenditures per dwelling fell – from $3,818 in 1990/91 to $3,665 in 2000/01. By far the most important factor is that real rate payments per dwelling fell by –18 per cent as a result of local government reform and amalgamations of Victorian local governments in the middle of the decade. Real maintenance expenditure also fell slightly, from $1,347 to $1,258 or by $89 per dwelling.

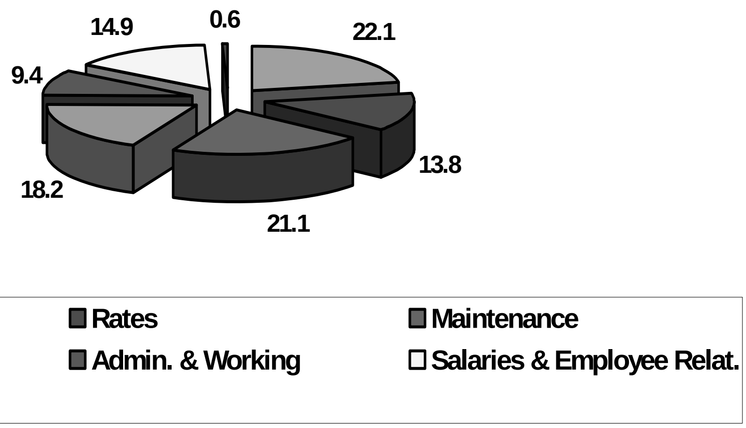
Even where real increases in expenditure occurred, with the exception of bad debts (which is a very small absolute amount), increases did not exceed 10 per cent real for any item.

Administration and working expenses only increased from $601 to $613 or by $12 (about 0.5 per cent per annum) and salaries etc from $951 to $1,014 or by $65 (about 7 per cent per annum).

Since 2000/01, however, operating expenditures have grown by 23.1 per cent due to substantial real increases in rates, up to $886, and maintenance, up to $2,206; increases of 22 per cent and 75.4 per cent respectively. By contrast, real overhead fell by nearly 21 per cent.

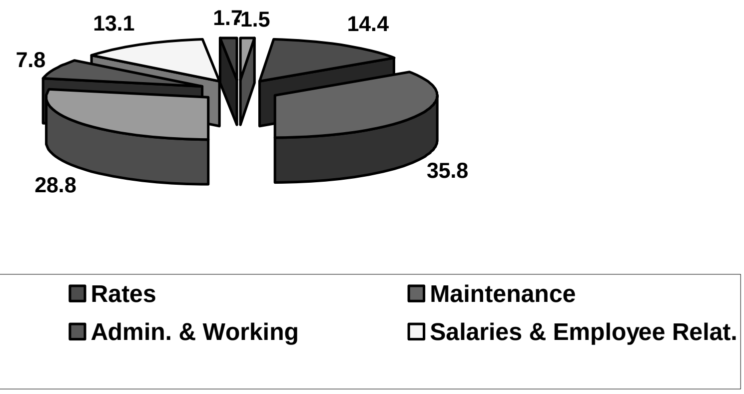
Reflecting these real changes in expenditure items, graphs 3.61 and 3.62 set out the proportion of total operating expenditure occupied by each of the core expenditure items for the years 1990/91 and 2005/06.

Graph 3.61: Line items: percentage of real total public housing operating expenditure per dwelling (excluding rebates), Vic, 1990/91 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Office of Housing, Victoria to 2005/06 Operating Deficits Project

Graph 3.62: Line items: percentage of real total public housing operating expenditure per dwelling (excluding rebates), Vic, 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Office of Housing, Victoria to 2005/06 Operating Deficits Project

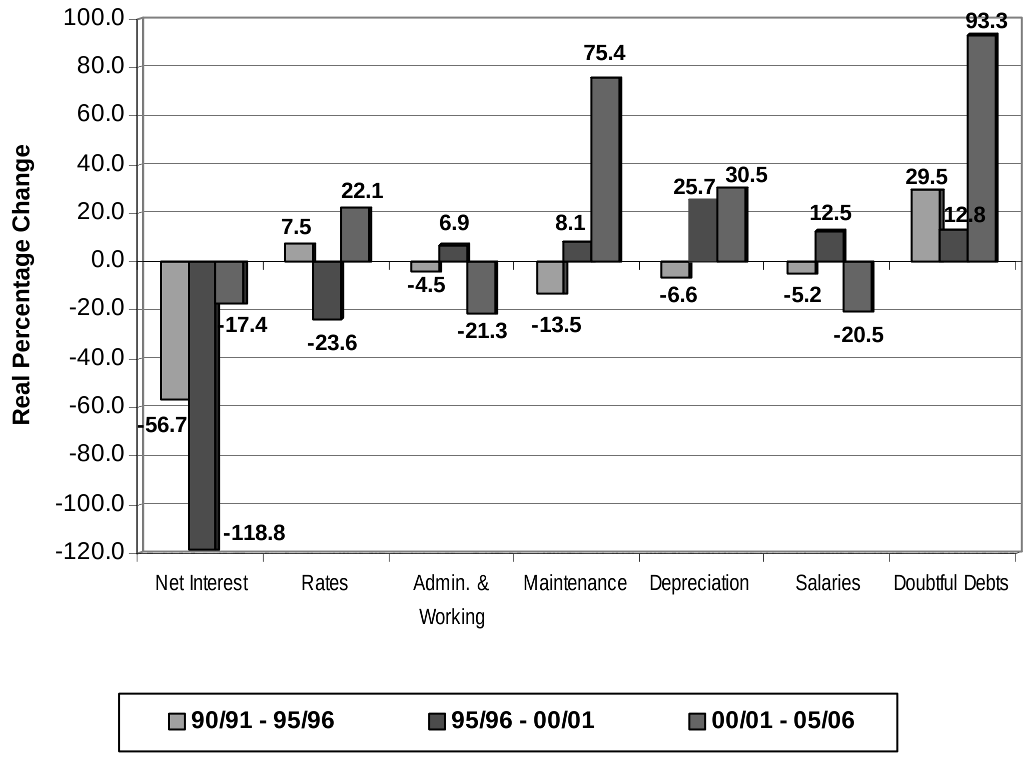
As a result of the Victorian Treasury absorbing the Office of Housing's debt in 1996/97, net interest has moved from absorbing 22.1 per cent of total operating expenditure to being positive by 1.5 per cent, i.e. earning monies on funds invested. However, it should be noted that the Office Of Housing must still make regular capital payments to Treasury.

Furthermore, administration and working, and salaries and employee-related expenditures both fell as a proportion of the total, with the total overhead expenditure dropping from 24.1 per cent to 20.9 per cent of total operating expenditure.

While rates increased slightly (from 13.8 per cent to 14.3 per cent), by far the largest proportionate increases were for maintenance and depreciation. The former increased from 21.1 per cent to 35.6 per cent of the total or more than one-third, while the latter increased from 18.2 per cent to 28.7 per cent. Asset-related expenditures now absorb more than 50 per cent of Victoria's total operating expenditures.

Graph 3.63 sets out the real percentage change in the costs of key line items.

Graph 3.63: Real percentage change in key line items, Vic, 1990/91 to 2005/06



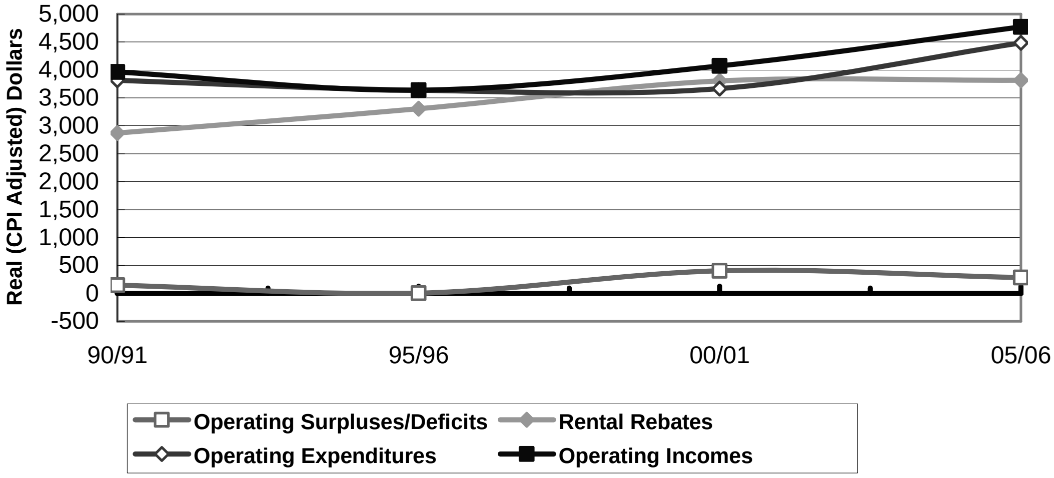
Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Office of Housing, Victoria to 2005/06 Operating Deficits Project

The graph reflects the findings outlined earlier – very significant real declines in the cost per dwelling for net interest, moderate declines in overhead and substantial increases in maintenance and depreciation.

Operating income, expenditure and surplus/deficits

Graph 3.64 sets out the trends in operating surpluses/deficits excluding net interest and depreciation.

Graph 3.64: Real operating surpluses/deficits per dwelling ($), Vic, 1990/91 to 2005/06



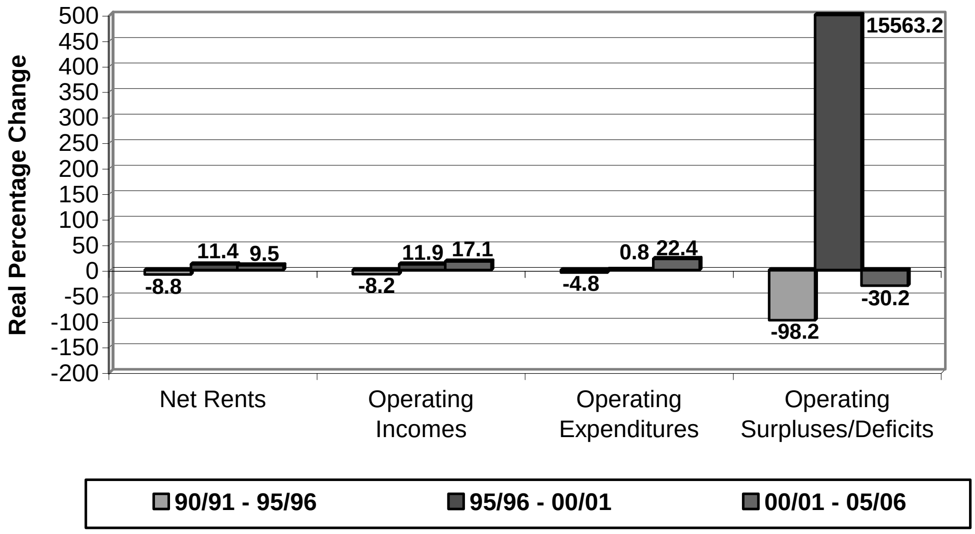
Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Office of Housing, Victoria to 2005/06 Operating Deficits Project

In 1990/91 Victoria produced a real surplus per dwelling (excluding net interest and depreciation) of $147, which increased to $407 in 2000/01.

By 2005/06, however, the trend had reversed, with operating surpluses halved to $284 per dwelling.

This reversal in trends is primarily a function of the different rate of real growth of operating expenditures and incomes over the period 2000/01 to 2005/06. During this period the former grew by 23.1 per cent while the latter grew by a robust but lesser 17.1 per cent and, when the once-off sundry income item is excluded, the more likely income growth rate was around 9 per cent. Almost all the expenditure increase can, however, be attributed to increasing maintenance expenditure. Graph 3.65 sets out the real percentage change in net rents, operating incomes, expenditures and surpluses/deficits.

Graph 3.65: Real percentage change in net rents, incomes, expenditures and surpluses/deficits, Vic, 1990/91 to 2005/06



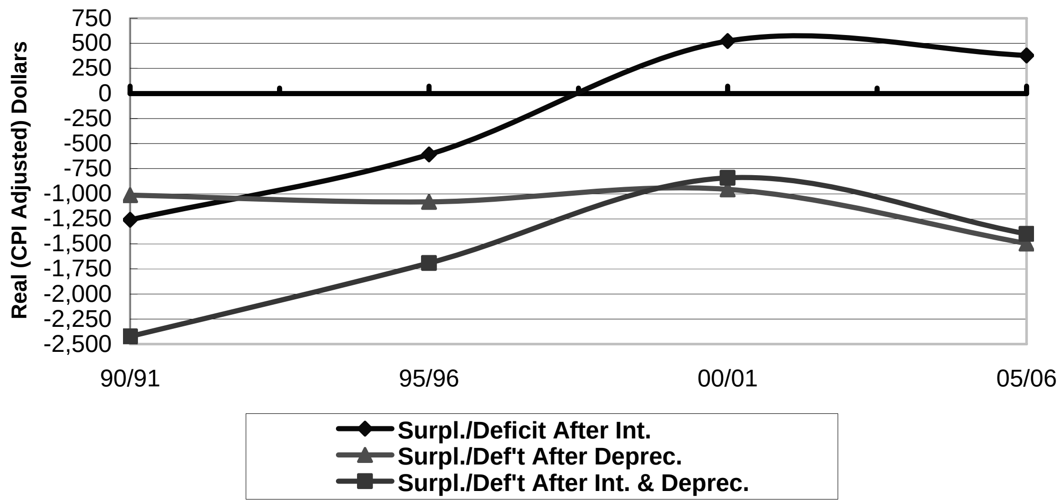
Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Office of Housing, Victoria to 2005/06 Operating Deficits Project

To summarise, over the whole period real operating incomes (excluding net interest and depreciation) increased by 20.3 per cent, with real operating expenditures growing by 18.2 per cent, resulting in a surplus growth of 93 per cent.

Impact of net interest and depreciation

Graph 3.66 sets out the impact of net interest and depreciation on the operating surplus/deficit.

Graph 3.66: Real surplus/deficit per dwelling after 'add backs' ($), Vic, 1990/91 to 2005/06



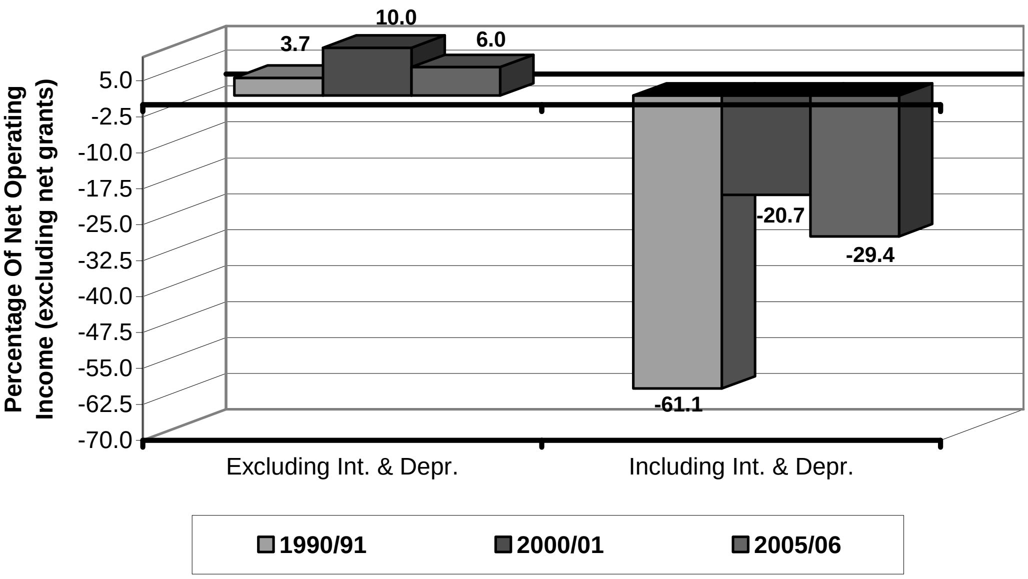
Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Office of Housing, Victoria to 2005/06 Operating Deficits Project

Over the period 1990/91 to 2000/01, the impact of net interest costs and depreciation declined substantially and then increased again to 2005/06. In 1990/91 net interest moved the real operating result from surplus to deficit by approximately –$1,409 per dwelling. Depreciation added a further –$1,162 to the deficit, increasing it after interest from –$1,262 to –$2,423 per dwelling.

In 2000/01, however, net interest added nothing to the expenditure line, and depreciation some $1,363, turning the operating surplus from $522 after interest to a deficit of –$841, or by less than half the shift that occurred a decade earlier.

Since 2000/01, while net interest has continued to add to the before-depreciation surplus, depreciation has grown substantially, turning the operating surplus from $379 after interest to a deficit of –$1,400 or nearly double that of 2000/01. Graph 3.67 sets out the operating deficits as proportion of net income before and after net interest and depreciation.

Graph 3.67: Real public housing operating surpluses/deficits as percentage of net income before grants, Vic, 1990/91, 2000/01 and 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Office of Housing, Victoria to 2005/06 Operating Deficits Project

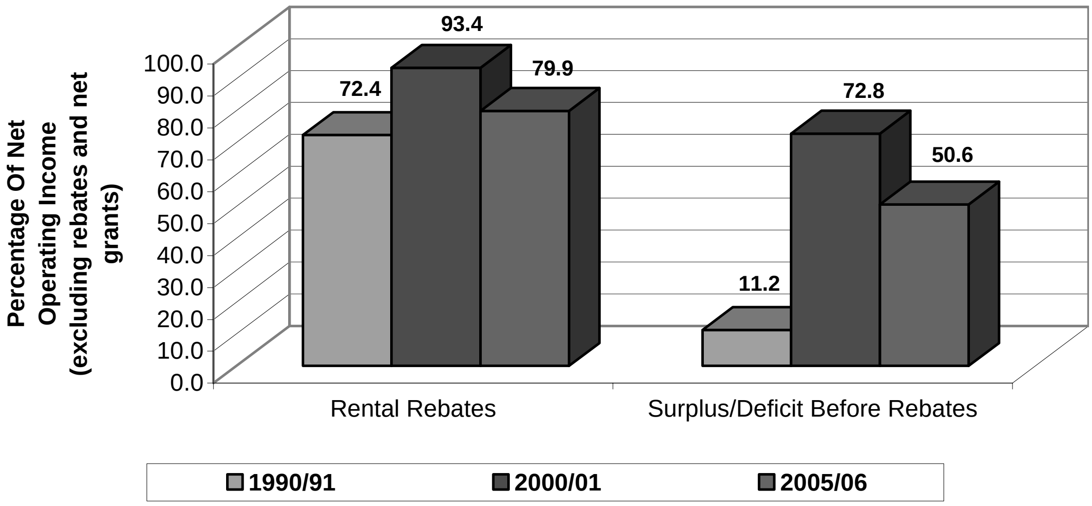
These results reinforce the earlier comments on the impact of net interest and depreciation. These expenditure components added 60 per cent to the operating deficit as a percentage of net income in 1990/91, while in 2005/06 they merely added about 30 per cent to the deficit. Consequently, the impact on the operating deficit of these items has reduced by 50 per cent in real terms over the period.

The importance of rebates

Real average rental rebates per dwelling have actually increased significantly from $2,434 in 1990/91 to $3,320 in 2000/01. Conversely, net grants applied to public housing have decreased rapidly, from just over $1000 to negative –$47 per annum (Victoria paid more grants than it applied to the operations).

Graph 3.68 sets out rental rebates as a proportion of net Income before grants.

Graph 3.68: Real public housing rental rebates as percentage of net income before rebates and grants, Vic, 1990/91, 2000/01 and 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Office of Housing, Victoria to 2005/06 Operating Deficits Project

Whilst the extent to which rental rebates reduce net income has declined, they still remain very significant.

Of most importance is that if Victoria received a commercial return based on market rents it would be very viable financially and would provide double digit returns.

3.7.2 Qualitative

Key responses to the operational deficits questionnaire, 1990/91 to 2000/01: 2004 study

"The Victorian respondent indicated that tighter targeting would be exerting some downward pressure on average rents received, but that the trend to smaller households has probably had a greater affect on Net Rents. There have been a number of unrepeatable rent charging policy changes over the decade:

- in October 1995, rents for existing residents were increased from 10% to 15% of assessable income and from 15% to 20% in October 1996;
- in November 1997, rebated rents for new tenants were increased from 20% to 25% of gross household income; and
- in April 1998, the rent paid by rebated tenants was increased from 20% to 23% of gross household income.

A large amount of Victoria's stock is in large estates, and about 60% of stock is over twenty years old and is maintenance intensive. Victoria has increased its capital improvement expenditure from $43million in 1992/93 to $170million in 2002/03, whilst maintenance expenditure has increased significantly in recent years. Accrued maintenance reached $140million in 1998/99 but had declined to under $130million by June 2002. The respondent stated that according to a Commonwealth Scientific and Industrial Research Organisation (CSIRO) model prepared for the Office of Housing, about $180–$190million is required to bring all stock to appropriate standards.

Victoria applies a business attitude to managing the operation and has successfully engaged Victorian Treasury on both debt and recovering GST costs. Victoria's housing debt was taken over by the Victorian Treasury in 1996/97 and since then the amount paid to the Victorian Treasury each year has been by negotiation and relative to the State's Budget position and Housing program needs. However, the Office of Housing still makes regular capital payments to the Victorian Treasury. Victoria attempts to breakeven on a cash basis with its Operating Income and Expenditure, but some grants are required to support Operations. Operating Deficits are simply one of a number of reasons preventing substantive additions to supply."

Key responses to the operational deficits questionnaire: 2005/06

"During 2003, rents for existing tenants increased from 23 per cent of income to 25 per cent of income.

The Office of Housing's asset management strategies over the past 10 years have focused on, [first], disposing of the 'worst' (i.e. maintenance-intensive) stock, and secondly, on improving asset condition. A key element of the increased physical improvements funding has been to address the lifecycle needs of the asset, as a significant proportion of stock (over 60 per cent as at 30 June 2006) is over 20 years old. Expenditure on property maintenance and upgrade has increased over the past 10 years from approximately $90 million to $250 million per annum.

However, despite increased expenditure on physical improvements, property condition costs have increased, due to:

1. more accurate property condition inspections providing more up-to-date costings
2. a significant proportion of physical improvement works [being] directed to high-rise units
3. reductions in stock disposals to limit stock losses [resulting] in the retention of stock with high property condition costs.

Public housing rates and charges payments (excluding community housing) have increased by 33.4 per cent over the last five years, from $42.9 million in 2000/01 to $57.4 million in 2005/06, and now represent 13.8 per cent of total public housing operating expenses. Rates and charges (a key component of operating expenses) have increased at a much greater rate than CPI (14.7 per cent over the period).

It is estimated that tighter targeting has contributed approximately 10 per cent to the increase in current tenant rental arrears. The Office of Housing has recognised the potential impact of tighter targeting on tenancies and revenue. A number of changes have been implemented to provide tenants with additional support in establishing and maintaining their tenancies. These changes range from increased local office contact with those most at risk of tenancy failure, through to the introduction of the Social Housing Advocacy and Support Program, which funds community-based providers to assist new tenants in establishing successful tenancies and is able to intervene when tenancies are breaking down. The funding allocated to this program for the six months to June 2006 was $2.95 million. ([Note] that SHASP commenced mid-2005/06. Full year funding for 2006/07 is $6.1 million.)

Untied grants and state matching grants are required to cover the Office of Housing's operating deficit before being applied to capital purposes.

Victoria's existing operating deficit is effectively preventing the Office of Housing from making substantial additions to the supply of new social housing. The operating deficit, a function both of declining revenue and rising costs, is currently funded largely by cross-subsidy from asset investment funds. This has reduced the capacity of the Office of Housing to invest in new stock or undertake necessary physical improvements, with the former inhibiting growth in new social housing, and the latter risking a deterioration of the built asset."

Victorian Office of Housing: conclusions

The 2004 study stated:

"There are a number of particular circumstances which make Victoria unique. The Office of Housing's performance in the last decade is not likely to be replicated in future years.

Firstly, Victoria was first authority in beginning to change its rent charging policies and very quickly completed the movement from charging proportions lower than 25% of household income in rent to 25%. This had the effect of allowing the Net Rents received to grow slightly even when the trends to smaller households and lower income households were moving the Income trend in the opposite direction. These gains will not be able to be repeated in future years and it is more likely that as the tenant composition moves more completely to rebated tenancies, and allocations become almost exclusively priority, some decline will occur in the Net Rent received per dwelling.

Secondly, Victoria engaged in serious reform and amalgamation of Local Authorities in the mid 1990's which, in many locations, saw the rate in the dollar fall. This reform is primarily responsible for the 15% fall in rates per dwelling, although some shift to smaller (and lower value) dwellings may also have contributed. This Rate result will not be able to be repeated in the next decade.

Thirdly the assumption by the Victorian Treasury of all of the public housing debt eliminated a significant interest burden and these cost savings are now fully booked.

Fourthly, the structure of the portfolio and its concentration in major estates and high density housing will no doubt have provided some maintenance efficiencies not available to other Housing Authorities.

There is no doubt, however, that Victoria has exercised rigid discipline over its expenditures, as reflected in both its Salaries costs rising the second slowest of all Authorities and its Operating Expenditures actually falling in real terms (before Depreciation and Net Interest). It's aim to break-even on a cash basis has probably contributed to these outcomes.

In the interests of sound financial management Victoria has taken a careful approach to the provision of its client services, one necessitated by the adherence to a cash neutral outcome.

This of course raises the question as to whether Housing Authorities can expect to substantially improve the quality of their services to tenants without equivalent increases in costs. With flat or falling Incomes what quality of services can Housing Authorities afford? If rising service standards are a high priority, where are the additional funds necessary to support them to come from? These are important policy questions for Australia's housing authorities, in the light of the analysis in this report."

Since 200/01 Victoria has continued to improve the efficiency of its management and to allocate substantial resources to the improvement of its stock. In addition, changes to rent-charging policies have generated considerable revenue growth and, if not for a major expansion in maintenance outgoings, operating surpluses before interest and depreciation would have increased.

Furthermore, the focus on asset management has led to the maintenance of a portfolio in relatively good condition, with only 25 per cent of the stock in a fair condition. As a result, the future costs associated with asset improvement are likely to be manageable.

Notwithstanding the above, rent-charging policy is now bumping up against affordability barriers, and maintaining the current healthy operating position will require continued vigilance on overhead and tenancy management costs.

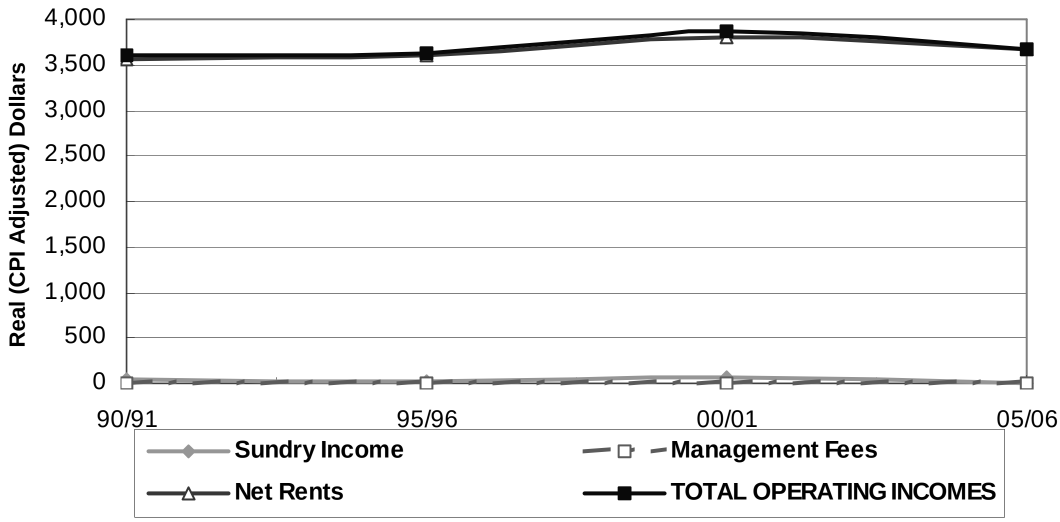
3.8 Western Australia: 'Homeswest'

3.8.1 Quantitative

Changes in net incomes

Graph 3.69 sets out real net Income per dwelling unit over the period 1990/91 to 2005/06, in Western Australia (WA).

Graph 3.69: Real incomes per dwelling unit ($), WA, 1990/91 to 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Homeswest to 2005/06 Operating Deficits Project

Note: Includes public, community and Aboriginal housing owned and operated by Homeswest but excludes any dwellings head-leased or leased from third parties.

Over the period 1990/91 to 2000/01, operating incomes per dwelling increased in real terms from $3,601 to $3,862 or by about $260 per dwelling. Net rents per dwelling rose by 6.7 per cent. Real rents constituted more than 98 per cent of annual operating incomes throughout the decade.

Since 2000/01 real net rents per dwelling have fallen by $121 to $3,676 and operating incomes have also fallen by $182 to $3,680.

Quantitative factors affecting operating incomes

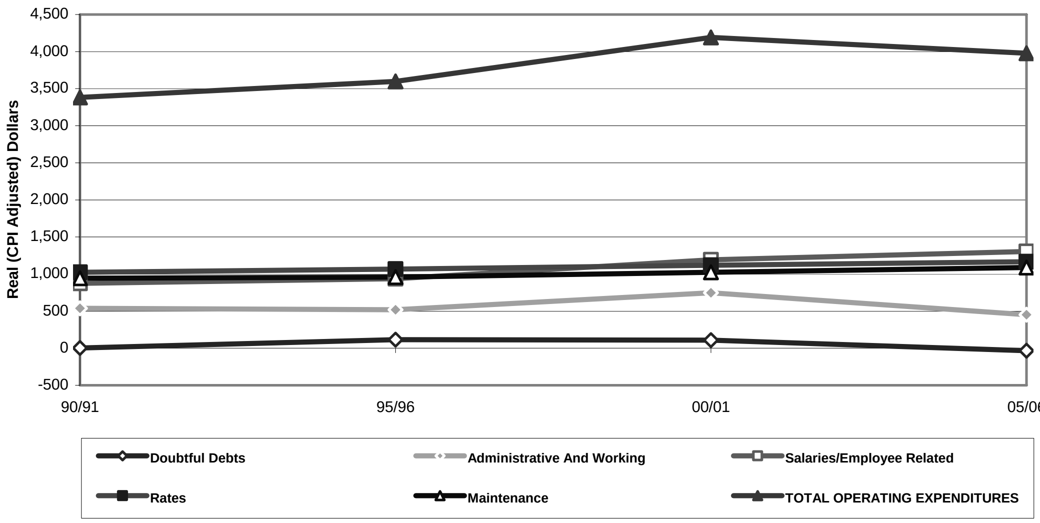
Over the period 1990/91 to 2000/01, rebated tenants as a proportion of the total increased only slightly, from 78 per cent to 83.7 per cent, and priority, crisis and emergency allocations only increased from 10 per cent of all new allocations to 19 per cent, the lowest of all Australian states.

Since 2000/01 rebated tenancies have fallen slightly to 81.9 per cent, while the proportion of new allocations going to priority crisis and emergency categories has increased to 25.7 per cent.

Expenditures and expenditure priorities

Graph 3.70 sets out real net expenditure per dwelling unit over the period 1990/91 to 2005/06.

Graph 3.70: Real expenditures per dwelling unit ($), WA, 1990/91 to 2005/06



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Homeswest to 2005/06 Operating Deficits Project

Over the period 1990/91 to 2000/01, real operating expenditures per dwelling increased from $3,383 to $4,192.

Real increases in maintenance and rates outgoings was moderate during this period, with maintenance expenditure per dwelling increasing from $944 to $1,024, (8 per cent) and rates from $1,023 to $1,119 (9 per cent).

Significant real increases in expenditure occurred in the administrative and working and salaries and employee-related items, with the former increasing from $539 per dwelling to $748 (or by 39 per cent) and the latter from $875 to $1,192, (or by 36 per cent). Total overhead increased in real terms from $1,414 to $1,940 or by approximately 37 per cent.

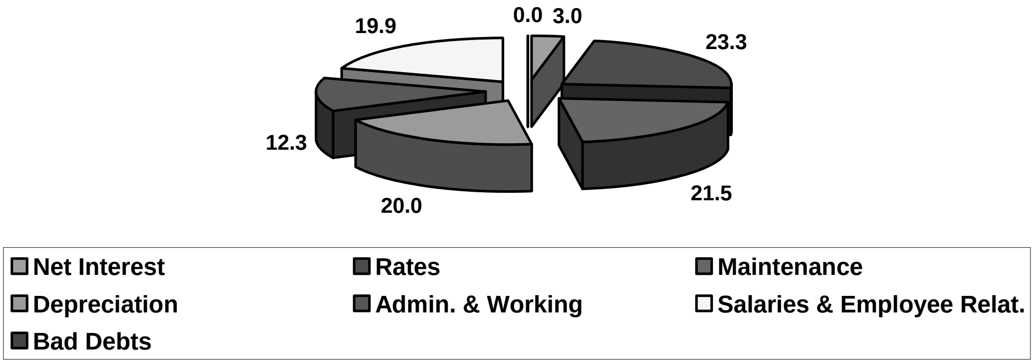
By far the greatest real increase in expenditure occurred in net interest payments, increasing from $131 to $655 or by 398 per cent.

Since 2000/01 real operating expenditures (before net interest and depreciation) have fallen by $214 per dwelling (5.1 per cent), to $3,978. This reduction has largely been achieved because of a major cut in administration and working expenditures, which have fallen by $295 per dwelling (39 per cent) to $453, and very moderate real growth in salaries and employee-related (9.4 per cent), maintenance (6.2 per cent) and rates (4.3 per cent).

Reflecting these real changes in expenditure items, graphs 3.8.3 and 3.8.4 set out the proportion of total operating expenditure occupied by each of the core expenditure items for the years 1990/91 and 2005/06.

The graphs show how the proportion of Homeswest's total expenditure per dwelling for each item (including depreciation and net interest) has changed over the decade.

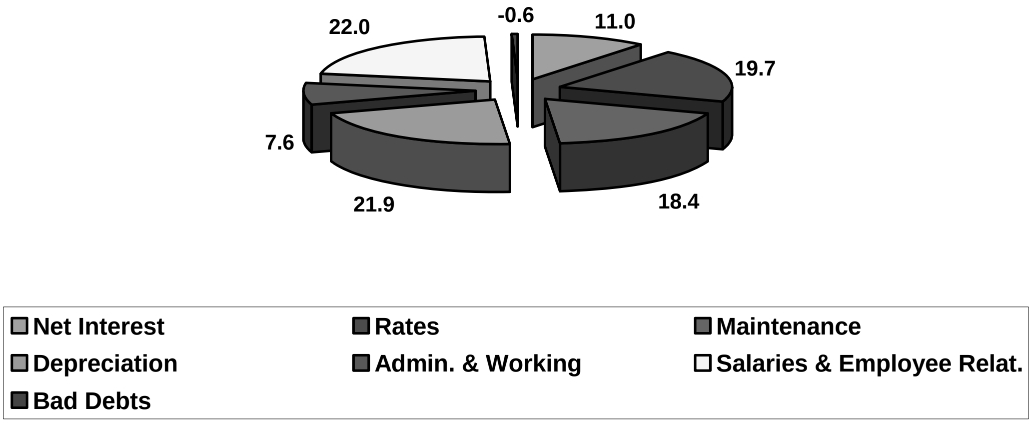
Graph 3.71: Line items: percentage of real total public housing operating expenditure per dwelling (excluding rebates), WA, 1990/91 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Homeswest to 2005/06 Operating Deficits Project

Note: Bad and Doubtful Debts Figure for 1991/92 has been used because of an anomaly with the 1990/91 figure.

Graph 3.72: Line items: percentage of real total public housing operating expenditure per dwelling (excluding rebates), WA, 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Homeswest to 2005/06 Operating Deficits Project

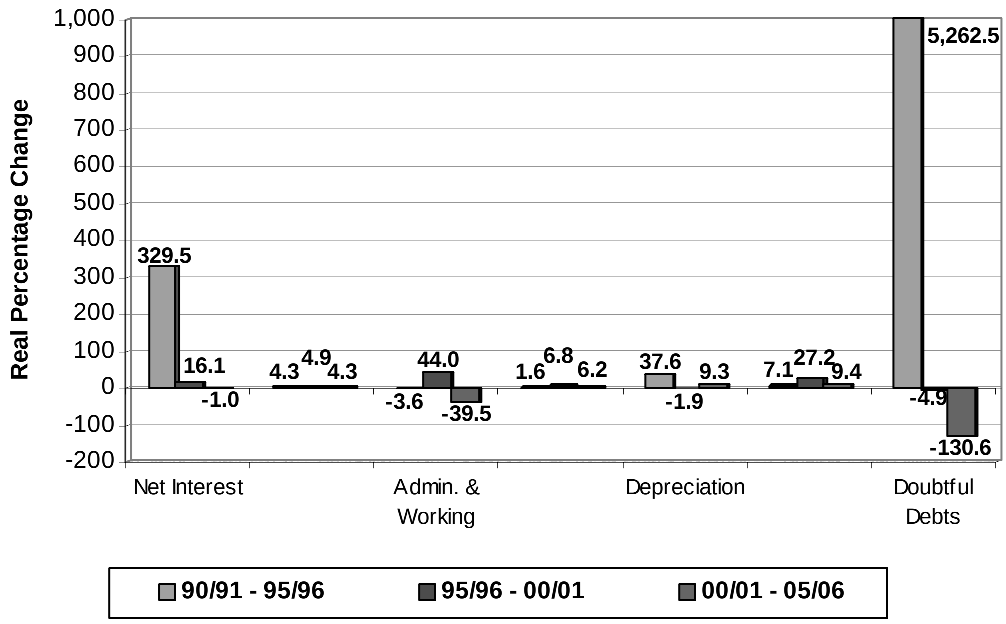
The proportions of total expenditure absorbed by both rates (down from 23.3 per cent to 19.7 per cent) and maintenance (down from 21.5 per cent to 18.4 per cent) have declined substantially. So too has administrative and working (down from 12.3 per cent to 7.6 per cent).

Depreciation has risen slightly as a proportion of total expenditures per dwelling, from 20.0 per cent to 21.9 per cent, while salaries and employee-related has risen moderately, from 19.9 per cent to 22 per cent.

As outlined in the analysis of expenditure growth, by far the greatest change in proportions has occurred in net interest, increasing from 3.0 per cent to 11 per cent.

Graph 3.73 sets out the real percentage change in the costs of key line items.

Graph 3.73: Real percentage change in key line items, WA, 1990/91 to 2005/06



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Homeswest to 2005/06 Operating Deficits Project

Note: Base year for bad and doubtful debts is 1991/92 because of an anomaly with the 1990/91 figure.

Over the whole period there were moderate falls in administration and working (16 per cent), moderate increases in maintenance (15 per cent) and rates (14 per cent), and significant real percentage increases in salaries etc (46 per cent), and a major increase in net interest.

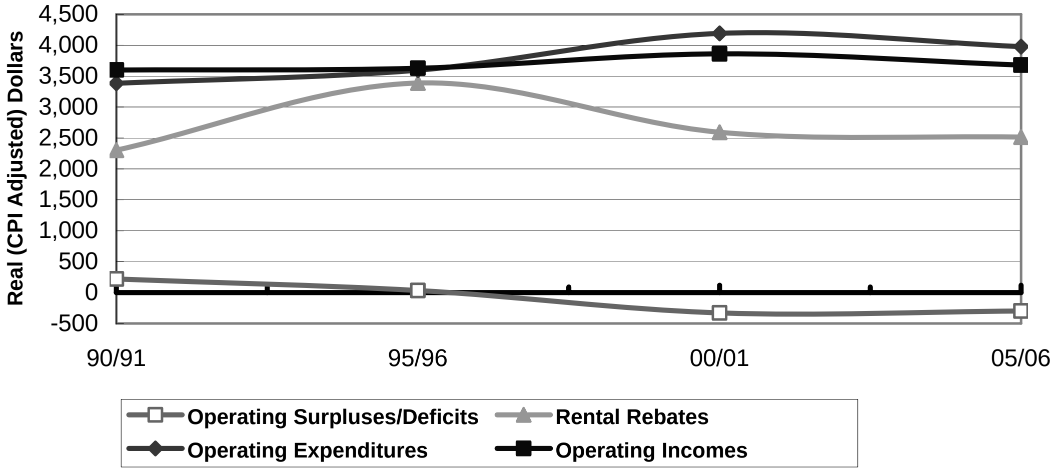
Operating income, expenditure and surplus/deficits

Graph 3.74 sets out the trends in operating surpluses/deficits, excluding net interest and depreciation.

In 1990/91 Homeswest produced a real surplus per dwelling (excluding net interest and depreciation) of $219, which fell to a deficit of –$330 per dwelling in 2000/01. As can be seen from the graph, expenditures increased steadily in this period, from $3,383 to $4,192 or by $809, while net incomes increased much more moderately from $3,601 to $3,862, an increase of $263 per dwelling.

Since 2000/01 real operating deficits per dwelling (excluding net interest and depreciation) have fallen by $32 to –$298, primarily due to a fall in real operating expenditures to $3,978 (–5.1 per cent) and a smaller fall in operating incomes to $3,680 (–4.7 per cent).

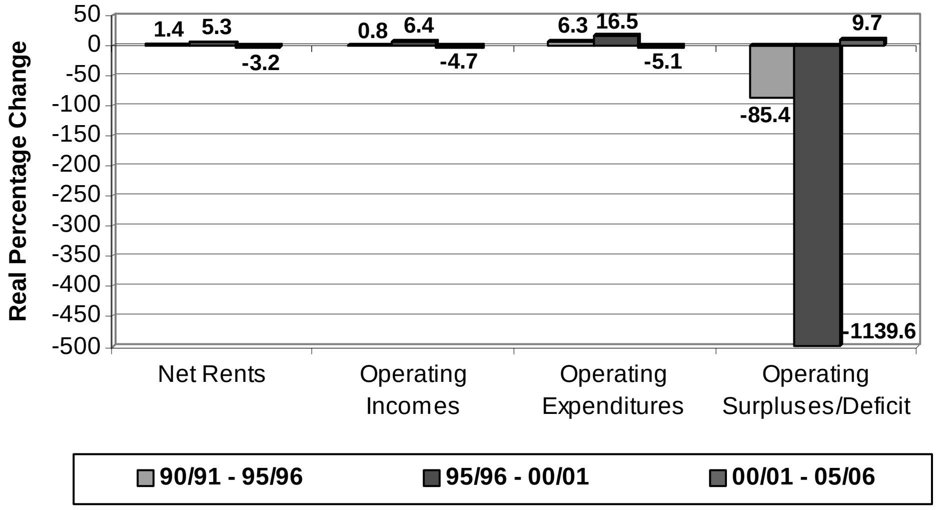
Graph 3.74: Real operating surpluses/deficits per dwelling ($), WA, 1990/91 to 2005/06



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Homeswest to 2005/06 Operating Deficits Project

Graph 3.75 sets out the real percentage change in net rents, operating incomes, expenditures and surpluses/deficits.

Graph 3.75: Real percentage change in net rents, incomes, expenditures and surpluses/deficits, WA, 1990/91 to 2005/06



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Homeswest to 2005/06 Operating Deficits Project

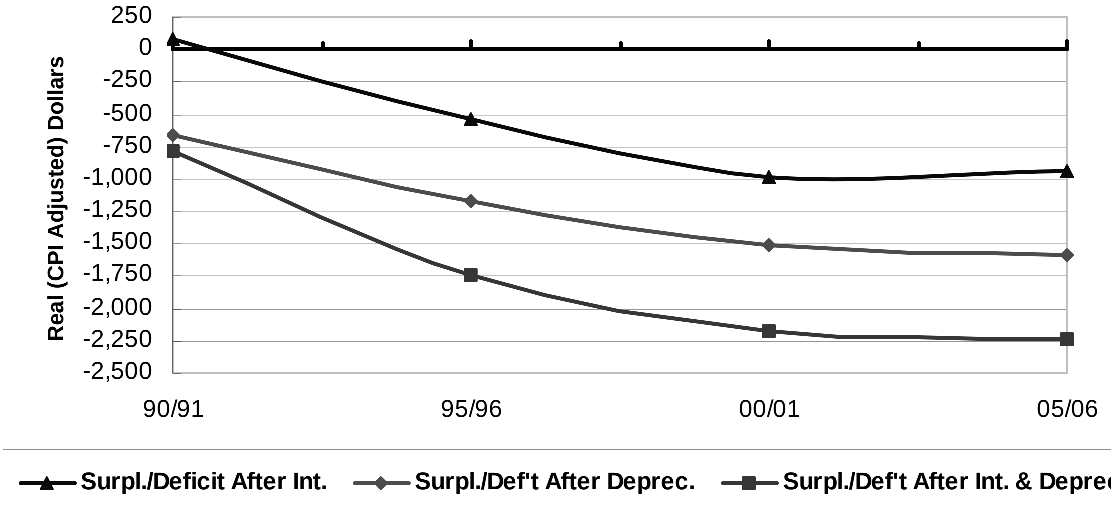
To summarise, real operating incomes (net of grants and interest earned) increased by about 0.13 per cent per annum, while real operating expenditures grew by about 1.1 per cent per annum (or 18 per cent), resulting in deficit growth of 237 per cent.

Impact of net interest and depreciation

Graph 3.76 sets out the impact of net interest and depreciation on the operating surplus/deficit. The impact of both net interest and depreciation has increased substantially over the decade. In 1990/91 net interest reduced the operating surplus by approximately –$131 per dwelling.

Depreciation added a further –$877, moving the surplus to a deficit of –$790 per dwelling. In 2005/06, however, net interest added $649 to the expenditure line, and depreciation some $1,294, increasing the operating deficit from –$298 to –$2,241 or by about twice that which occurred in 1990/91.

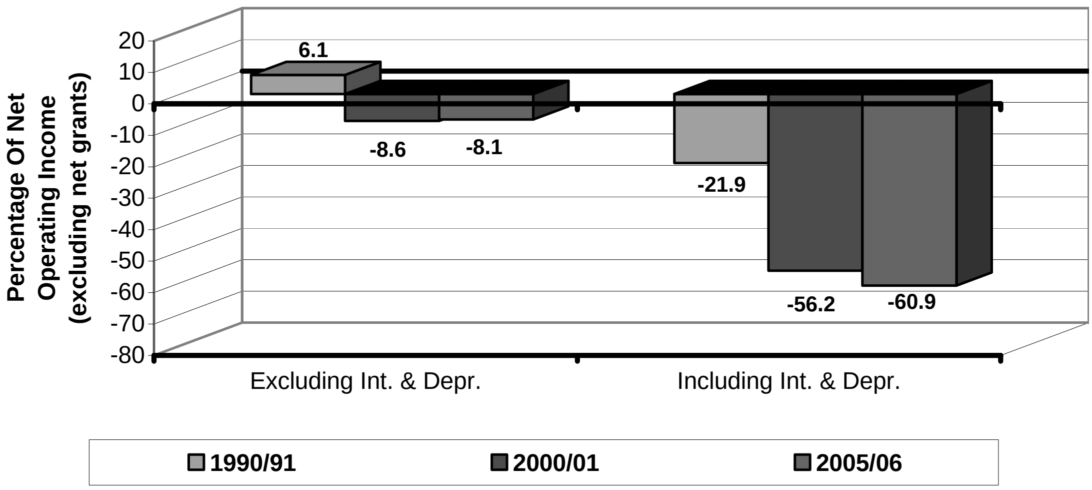
Graph 3.76: Real surplus/deficit per dwelling after 'add backs' ($), WA, 1990/91 to 2005/06



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Homeswest to 2005/06 Operating Deficits Project

Graph 3.77 sets out the operating deficits as a proportion of net operating income before and after net interest and depreciation.

Graph 3.77: Real public housing operating surpluses/deficits as percentage of net income before grants, WA, 1990/91, 2000/01 and 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Homeswest to 2005/06 Operating Deficits Project

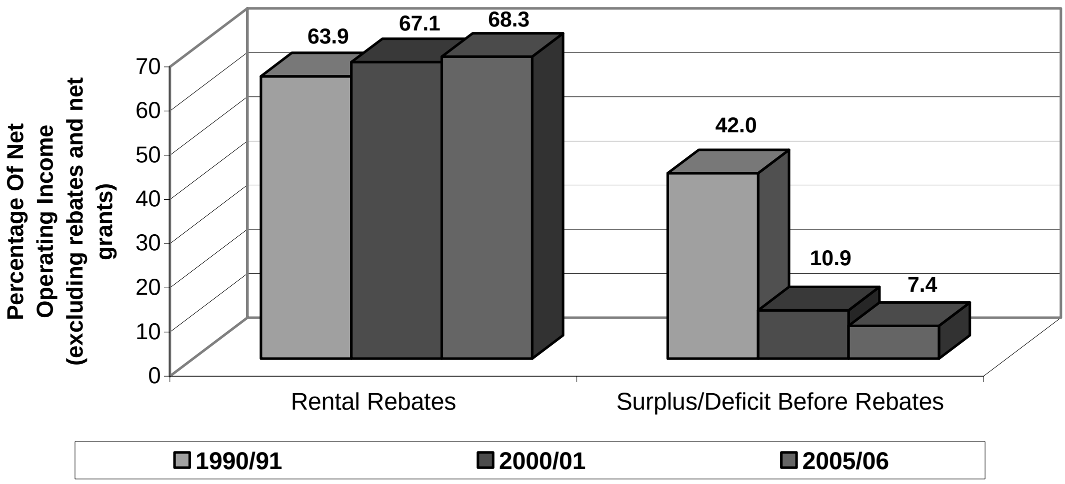
These results reinforce the earlier comments on the impact of net interest and depreciation. The importance of these expenditure components are increasing rapidly;

to the extent that 2005/06 interest in depreciation was six times larger than operating deficits before interest and depreciation.

The importance of rebates

Graph 3.78 sets out rental rebates and grants as a proportion of net income before grants.

Graph 3.78: Real public housing rental rebates as percentage of net income before rebates and grants, WA, 1990/91, 2000/01 and 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; and return from Homeswest to 2005/06 Operating Deficits Project

Real average rental rebates per dwelling increased moderately from $2,302 in 1990/91 to $2,514 in 2005/06.

The graph clearly shows that the impact of rental rebates relative to net incomes before rebates increased slightly and still remains very significant. If Homeswest received a commercial return based on market rents it would be financially robust and provide an appropriate operating rental return. Combined with the capital gain, this would provide a respectable double digit annual rate of return.

In the case of Homeswest, recognising the real cost of the CSO and providing a cash payment for rebates would ensure the continued viability of the sector.

3.8.2 Qualitative

Key responses to the operational deficits questionnaire, 1990/91 to 2000/01: 2004 study

"The Homeswest respondent indicated that whilst tighter targeting had occurred over the decade the effect on Homeswest had been muted and it was difficult to assess the impact on Net Rents. Similar views were expressed about changes to the household composition of the tenant portfolio.

During the second half of the decade Homeswest had moved from cost based rents to a mixed regional and market based rent to a full market based model. Rents are being progressively moved from 22.5% to 25% of assessable income.

Homeswest has managed to control maintenance expenditures which have remained relatively consistent over the period. A major urban renewal program has been undertaken and high density stock numbers have been reduced. This program will continue for the next five years.

The component of existing Administration costs allocated to non housing support services is minimal, however there is expenditure of this nature charged to rental expenses.

Some restructuring of high cost State debt has been undertaken. Low cost debt has not been targeted for restructure or early pay out. Interest payments are a significant burden.

The respondent indicated the operating position was deteriorating and grants were being increasingly applied.

Homeswest had a number of unique problems: i.e. the;

- geographical distance/isolation affecting the service provision and cost;
- boom bust townships;
- high level of indigenous population in public housing (18%).

The impact of growth in operating expenses, which are not covered by increased net rent revenue, is impacting on the deficit. With a fixed or reducing funding base and a large percentage of clients on rebated rents this situation will continue. Conversion of the Commonwealth debt to a grant would provide ongoing relief. Also important would be an increase in base funding to recognise the movement in the cost burden carried by the SHA's (including GST)."

Key responses to the operational deficits questionnaire: 2005/06

"Tighter targeting has resulted in smaller household sizes and, therefore, lower average rent. [While] the impact on costs is minimal, there is operational expenditure relating to tenant support programs which is being charged to rental expense.

Rent rebate calculations have progressively moved from 22.5 per cent to 25 per cent of assessable income over the last decade but tenants [who] occupied their rental home prior to July 1997 still have their rents assessed on 23 per cent of base income.

State debt is actively managed, with some parts of the portfolio using terms as little as three months. [Homeswest's] liabilities have grown to help meet construction costs.

A major urban renewal program, which substantially improves the quality of the rental stock, has been undertaken. The program has also included the reduction in high-density accommodation to address social issues on public housing estates. The condition of the stock is now excellent

Geographical distance/isolation affecting service provision and cost, construction and maintenance costs are much higher in remote areas of the state.

The state's economic boom has [affected] the median price of property and rents in [most] regional areas. Significant pressure is being placed on remote communities due to the cost of service provision and new construction, being a direct result of focus on local services providers to the mining industry. This has resulted in increases in costs and significant increases in time for completion of contracts for new construction.

Shortages in land and rental housing in the metropolitan area has resulted in increased pressure on the Department in terms of an increasing [waiting] list, increased demand for priority housing, reduced turnover of public housing stock and reduction in take up of bond assistance loans because of an inability of low-income households to access affordable private rental stock.

Shortages in land supply and continued demand for construction of new homes and apartments is expected to continue [in] 2008.

The ability to cover operational costs from recurrent rent revenue is being reduced and [is therefore] restricting the ability to substantially increase the supply of new social housing."

Homeswest: conclusions

The 2004 study stated:

"In the last decade Homeswest has embraced tighter targeting, introduced income improvements through changes to its rent charging policy, substantially completed a major asset and urban renewal program, and a reduction of high density stock, and restructured some component of its debt, controlled and contained its maintenance expenditure, and improved its services to its clients.

Whilst targeting had increased the proportion of tenants who are rebated and the proportion of new allocations allocated to priority recipients, Homeswest, has the third lowest proportion of rebated tenants and the lowest proportion of priority allocations.

These priorities and characteristics have been reflected in the following outcomes:

- Given the slow accretion in rebated tenants, the focus on moving public tenants into homeownership and the slow rate of growth of priority allocations it is likely that real Net Rent growth may persist for some time in the future;
- a significant increase in the burden imposed by Net Interest, probably as a result of the new debt absorbed in the redevelopment process;
- significant improvements in tenants' ranking of both their satisfaction with the service provided and the quality of their dwelling.

It would appear that Western Australia has the potential for some Net Income growth and also some additional cost savings from debt reduction. For example, if Net Interest per dwelling was reduced to the average for the group and Net Rents continue to grow at 1% real per annum it is possible that Western Australia could turn the current 'core' (before Net Interest and Depreciation) Deficit into a small surplus.

It is also clear that if the full cost of Homeswest's community service obligation was correctly recognised (i.e. if the difference between market rents and income related rents was fully paid for), Homeswest would generate small operating surpluses after both Net Interest and Depreciation, and with Income and capital growth would remain viable for the foreseeable future."

2005/06 update

Since 2000/01 Homeswest has reduced its overhead cost by about 10 per cent and has contained the rate of expenditure growth on other items. With real operating deficits before interest and depreciation having fallen to below $300, with some room to move on net incomes through changes to rent-charging policy, and with an excellent overall asset condition, it appears that Homeswest may be well placed to achieve some further improvements in its operating position.

4 CONCLUSIONS

4.1 Client targeting

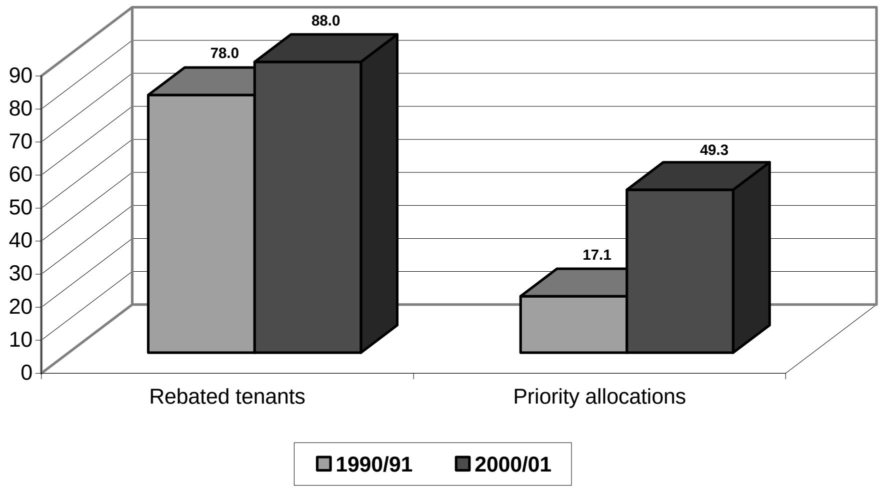
4.1.1 2004 report

The 2004 report stated:

"With the introduction of the 1995/96 CSHA the Commonwealth Government placed considerably greater priority on ensuring that new public and community housing allocations were targeted to those most in need, i.e. experiencing the lowest incomes or in dire or emergency situations and/or both. Many State Housing Authorities responded by introducing segmented waiting lists whereby 'priority applicants' received first call on available allocations.

These priority applicants are normally households with dire financial and housing needs, i.e. for example with no money, and/or living on the street and/or in some kind of emergency or transient housing situation. [Graph 4.1] sets out the proportion of tenancies which were rebated in 1990/91 compared to 2000/01 and the proportion of total allocations provided to 'priority allocations' for the same two years. In regard to the latter, it should be noted that the Northern Territory and Queensland were unable to provide information on priority applicants for 1990/91 and so have been excluded from the analysis, whilst the figure for NSW for 1990/91 had to based on a later years figure so is probably slightly overstated for that year.

[Graph 4.1]: Rebated tenants and priority allocations as proportion of all public and community housing tenancies and allocations 1990/91 – 2000/01



Source: Hall J and Berry M, 2004, Operating Deficits and Public Housing, Policy Options For Reversing The Trend, AHURI

Note: Priority Allocations analysis excludes the Northern Territory and Queensland (unable to supply), which have been left out of the weighted average derived.

The increasing focus on targeting to those in greatest need is clearly reflected in the increasing proportion of tenants who are in receipt of some kind of rebate and the rapid escalation of the allocations to emergency, crisis and dire situation households. There are three key consequences of the targeting outcomes:

→ because of the acceleration of the targeting of allocations to those on the very lowest incomes (almost all of these households depend almost entirely on pension and benefit payments) and even with changes in rent charging policies, it is likely that the medium term real rent received per tenancy will fall or at the very best remain flat;

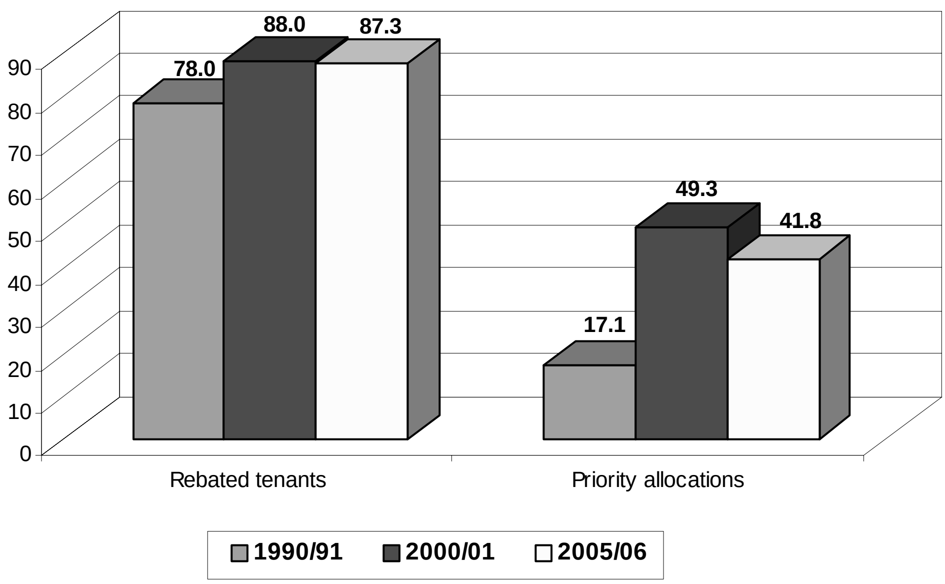
→ whilst the trend to priority allocations has been rapid there is still considerable room for a substantial increase in the proportion of total new allocations provided to these classes of tenants. Therefore it is possible that the average real rent received per tenant could decline in the immediate future.

→ Increasingly, households receiving priority allocations have non-housing related problems which require service support, adding to the average real costs per household of providing the relevant services to these clients. This trend is likely to continue in the foreseeable future."

4.1.2 2005/06 update

In this update study we asked STHAs to again provide us with information on both rebated tenancies and priority allocations. Graph 4.2 sets out a comparison with the earlier analysis.

Graph 4.2: Rebated tenants and priority allocations as proportion of all public and community housing tenancies and allocations, 1990/91, 2000/01 and 2005/06



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; returned spreadsheets of STHAs to the 2005/06 Operating Deficits Project

Note: 2000/01 Priority allocations analysis excludes the Northern Territory and Queensland (unable to supply), which have been left out of the weighted average derived.

As a proportion of total tenancies, rebated tenants declined in three states, remained static in three states and increased only marginally in two states. For priority allocations as a proportion of total new allocations, in three states these also declined and in three states they increased marginally. Changes in Queensland and the Northern Territory could not be ascertained because of the absence of a 2000/01 return.

The evidence suggests that the impact on revenues of changing client profiles may now have plateaued. The majority of public housing authorities may be developing 'mature' portfolios where the loss of income associated with the replacement of a non-rebated tenant with a rebated tenant may be matched by income growth in existing longstanding tenancies.

If this is the case then it can be expected that, in a stable stock situation, real rent revenues will stop declining and at least stabilise for the foreseeable future. Where rents account for more than 97 per cent of all operating revenues, a similar prognosis should apply to operating incomes.

4.2 The implications of targeting in the Australian context

4.2.1 2004 report

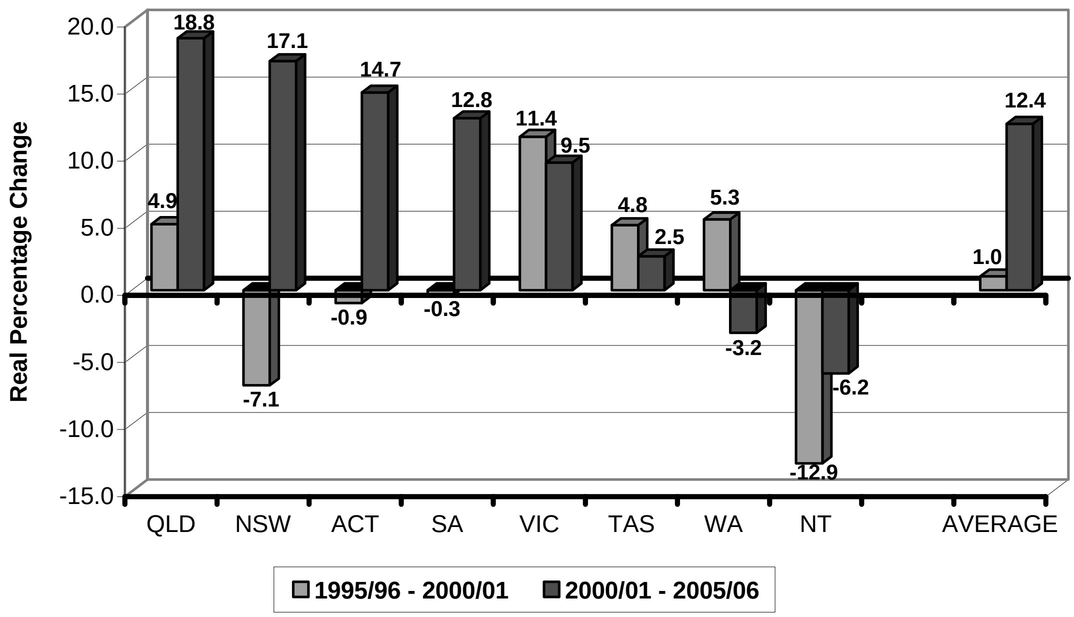
The 2004 study stated:

> "The analysis demonstrates the very low level of Net Income growth being experienced by Australian public housing authorities. If the Northern Territory is removed from the analysis then the weighted average outcome for the remaining authorities will be less than a third of 1% per annum.
>
> There is an almost perfect correlation between the rate of Net Income growth experienced by a Housing Authority and the rate of growth in the proportion of its tenants who are rebated and/or receiving priority allocations.
>
> For example, in 2001, the Northern Territory had the lowest proportion of rebated tenants of all Australian Housing Authorities at 80% and Homewest has the third lowest proportion of rebated tenants and the lowest proportion of priority allocations. By contrast those two Authorities who now have the highest proportions of rebated tenants i.e. New South Wales and Queensland now have the highest proportions of rebated tenants of all Australian Authorities.
>
> The potential reduction in Net Income was mitigated to some extent by the number of authorities who changed their rent charging policy and moved from less than 25% of assessable income paid in rent, to 25% of assessable income. This is particularly true of the Northern Territory, Western Australia, Victoria and New South Wales.
>
> All of the indicators on household composition indicate that a substantial movement from two to one income public tenant households is underway and will continue for some time. This will contribute to falling incomes per dwelling.
>
> Finally, as only two authorities have 90% or more rebated tenants and only three are in the situation where priority allocations make up more than 50% of new lettings the process of tighter targeting has yet to fully run its course.
>
> Based on these three factors, it is likely that the reduction in Net Income per dwelling unit will accelerate for the foreseeable future."

4.2.2 2005/06 update

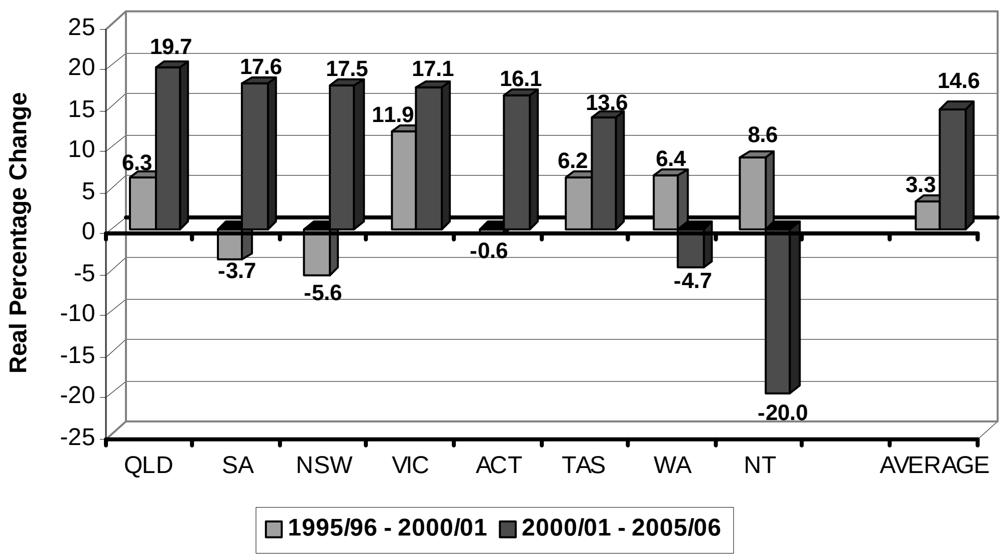
Graphs 4.3 and 4.4 set out real net rent growth and real net operating income growth over the period 1995/96 to 2005/06.

Graph 4.3: Real percentage change in net rents per dwelling, all state and territory housing authorities, 1995/96 – 2000/01 and 2000/01 – 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; returned spreadsheets of STHAs to the 2005/06 Operating Deficits Project

Graph 4.4: Real percentage change in net incomes per dwelling, all state and territory housing authorities, 1995/96 – 2000/01 and 2000/01 – 2005/2006 (June 2006 dollars



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; returned spreadsheets of STHAs to the 2005/06 Operating Deficits Project

Marked turnarounds in revenue growth have been achieved by six of the eight STHAs (although Tasmania's income growth has been achieved on the back of a very high and likely one-off sundry income increase).

This turnaround can be attributed to two main factors:

→ the stabilisation of the client profiles outlined earlier; and

→ a context in which seven of the eight STHAs introduced major rent-charging policy changes. These policy changes have resulted in a very high proportion of all rebated tenants now paying at least 25 per cent of their household incomes in rent. Only in the Northern Territory are rent requirements substantially less than 25 per cent of income.

Growth in incomes from increases in rent charged is predominately a once-off effect. Most STHAs are now bumping up against affordability barriers, which will effectively prevent real rents per dwelling from increasing.

4.3 Mismatches in incomes and expenditure growth: the genesis of deficits

4.3.1 2004 report

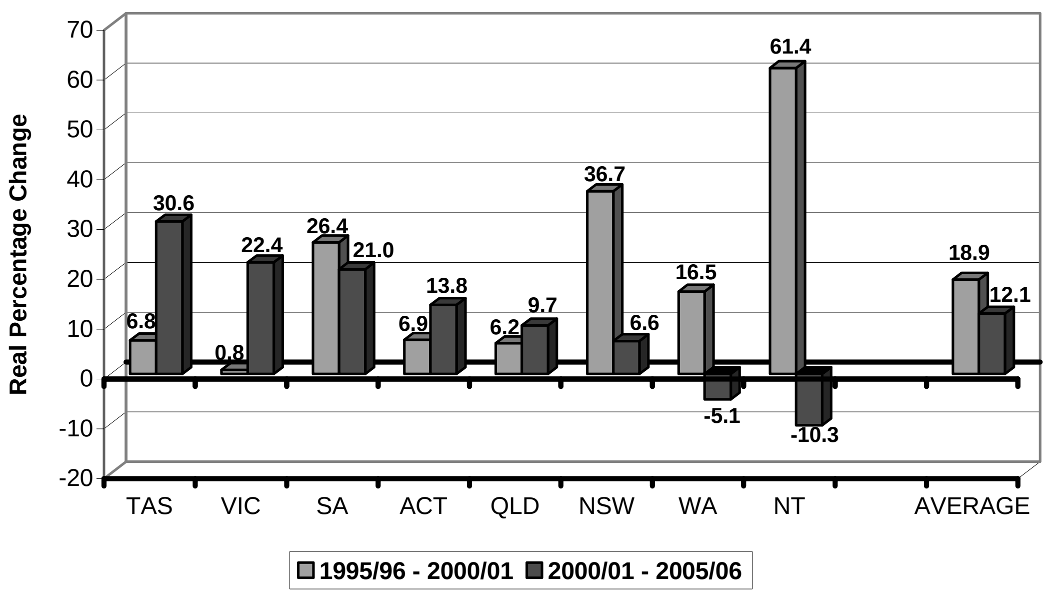
The 2004 study drew attention to the mismatch in the growth between operating incomes and expenditures. The study found that the weighted average net income per dwelling grew by 7.5 per cent and net expenditures by 38.2 per cent over the period 1990/91 to 2000/01.

In 1990/91 eight of the nine housing authorities were generating real operating surpluses. Only Tasmania was experiencing operating deficits. Of the Australian housing authorities, by 2000/01 only Victoria and South Australia were still in the black, with South Australia generating a small surplus.

4.3.2 2005/06 update

Graph 4.5 sets out the percentage change in real operating expenditures over the period 1995/96 to 2000/01 and compares this to the period 2000/01 to 2005/06. Graph 4.6 compares real Operating and Expenditure growth over the period 2000/01 to 2005/06.

Graph 4.5: Real percentage change in net expenditures per dwelling (excluding net interest and depreciation), all state and territory housing authorities, 1995/96 – 2000/01 and 2000/01 – 2005/06



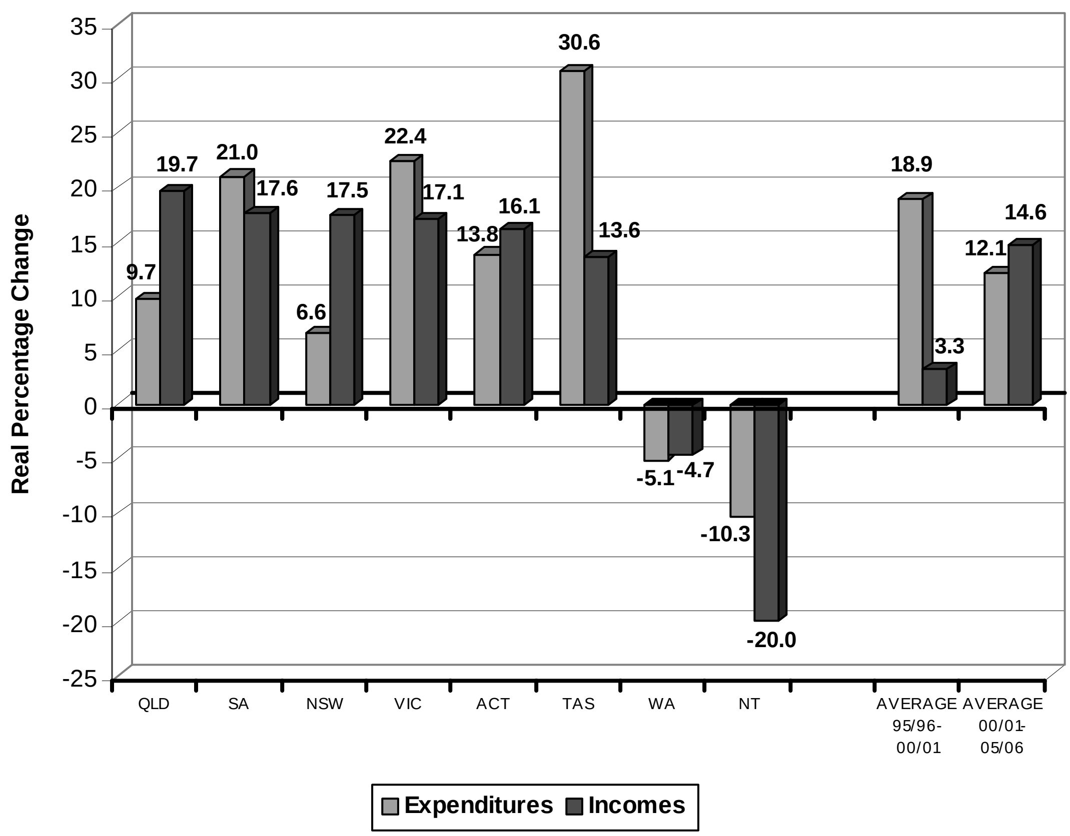
Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; returned spreadsheets of STHAs to the 2005/06 Operating Deficits Project

Graph 4.5 shows that for the period 2000/01 to 2005/06, four states (NSW, NT, SA WA) enjoyed expenditure growth at lower rates than have applied in the previous period, and in NSW the rate of expenditure growth was one-sixth that which applied in 1995/96 to 2000/01.

In four states (ACT, QLD, Tas and Vic), expenditure growth for the latest period exceeded that for 1995/96 to 2000/01, with Victoria's rate increasing to 22.4 per cent from a no growth situation and Tasmania's growth rate being just under five times that which applied in the previous period.

Graph 4.6 shows the relationship between the rate of growth in operating expenditures and operating incomes for the two periods.

Graph 4.6: Real percentage change in net incomes and expenditures per dwelling (excluding net interest and depreciation), all state and territory housing authorities, 2000/01 – 2005/06 (June 2006 dollars)



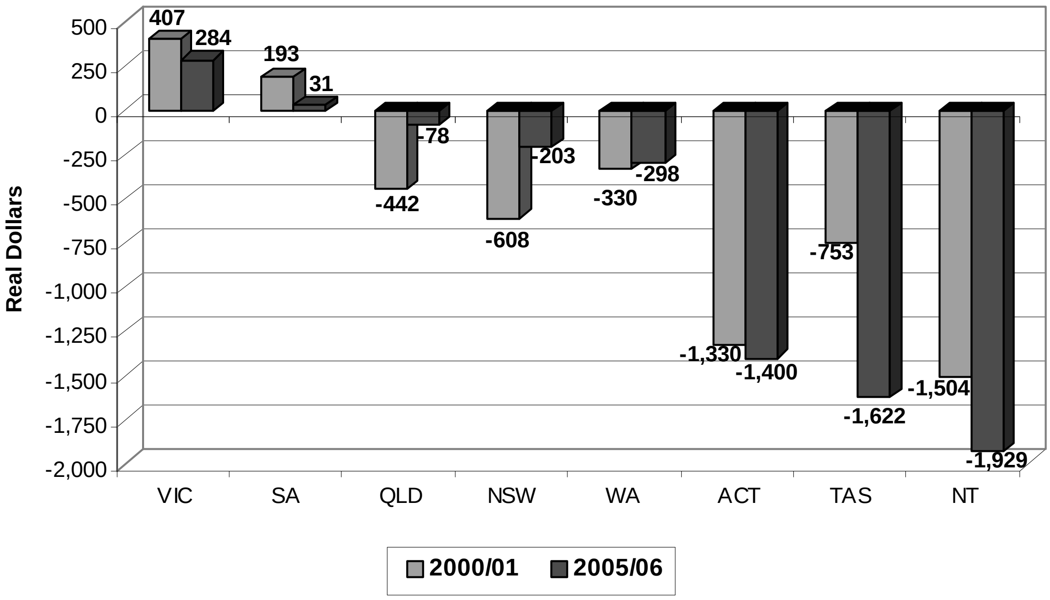
Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; returned spreadsheets of STHAs to the 2005/06 Operating Deficits Project

Notwithstanding all the initiatives to raise revenue, only in three states (ACT, Qld and NSW) did income growth rates exceed expenditure rates for the period 2000/01 to 2005/06, with operating incomes growing at almost three times the rate of operating expenditures in New South Wales.

For all of Australia, average income growth exceeded average expenditure growth by a small margin, considerably better than the five-fold difference between the averages for the period 1995/96 to 2000/01.

Graph 4.7 sets out an update of the operating deficits position (excluding net interest and depreciation), as at 30 June 2006.

Graph 4.7: Real operating surpluses/deficits per dwelling (excluding interest and depreciation), all state and territory housing authorities, 2000/01 and 2005/06 (June 2006 dollars)



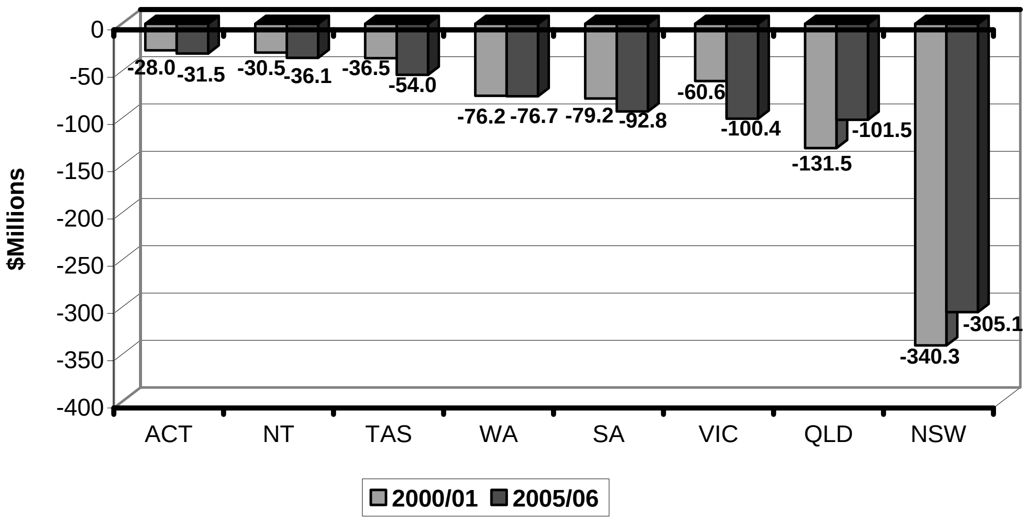
Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; returned spreadsheets of STHAs to the 2005/06 Operating Deficits Project

The graph indicates that only in three states (WA, Qld, and NSW) did the operating deficits position improve, and the improvement in Western Australia was marginal. In five states the operating positions continued to deteriorate and only one state, Victoria, has anything other than a marginal surplus. In both Tasmania and the Northern Territory the deterioration has been substantial.

All the improvement in both Queensland and New South Wales can be attributed to rent-charging policy changes that are likely to be unrepeatable.

Graph 4.8 sets out the absolute deficits by state after net interest and depreciation for the period 1995/96 and 2005/06.

Graph 4.8: Total real operating deficits including interest and depreciation ($m), all state and territory housing authorities, 2000/01 and 2005/06 (June 2006 dollars)

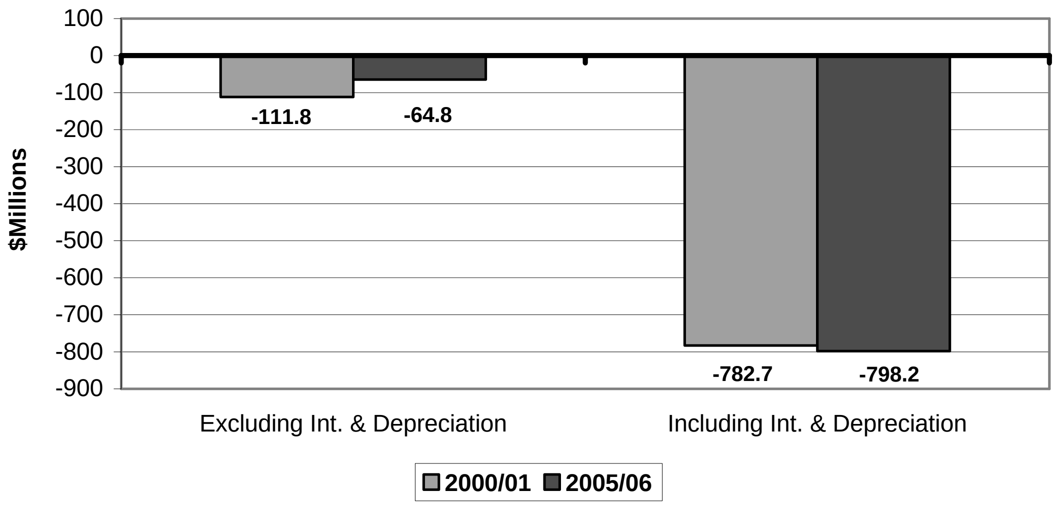


Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; returned spreadsheets of STHAs to the 2005/06 Operating Deficits Project

After adding in net interest and depreciation, the deficit position improved in only two states (Qld and NSW) for the reasons outlined earlier. The deterioration was marginal in Western Australia, moderate in both the ACT and the Northern Territory, and substantial in Tasmania, South Australia and Victoria.

Graph 4.9 sets out the total of the real operating deficits for all STHAs in Australia both before and after net interest and depreciation.

Graph 4.9: Total real operating deficits ($m), all state and territory housing authorities in Australia, 2000/01 and 2005/06 (June 2006 dollars)

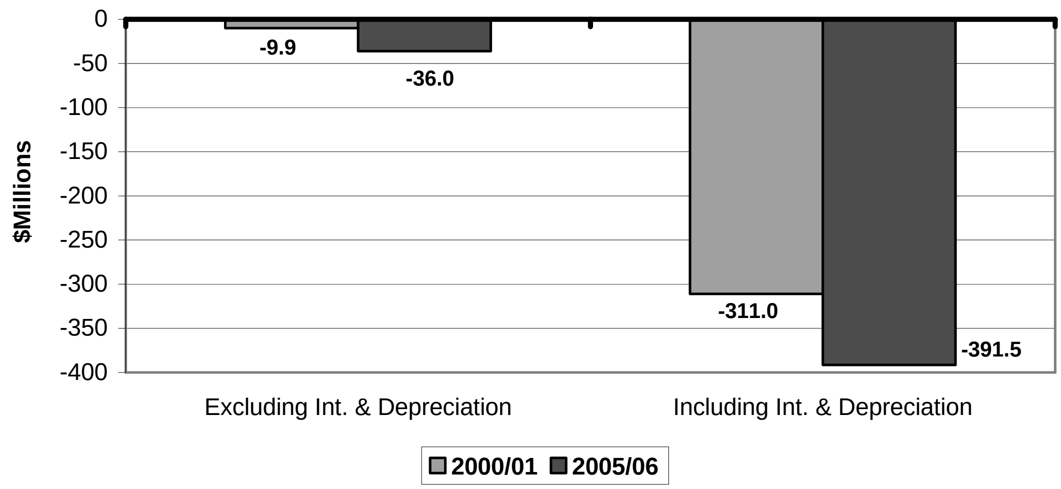


Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; returned spreadsheets of STHAs to the 2005/06 Operating Deficits Project

After net interest and depreciation, the current operating deficits substantially exceed the total of the base grant to STHAs under the current CSHA ($725.2 million) .

While the graph suggests that the overall position has not deteriorated significantly, this is entirely due to the improvements in Queensland and New South Wales. Graph 4.10 sets out the position for all states in Australia excluding Queensland and New South Wales.

Graph 4.10: Total real operating deficits ($m), all state and territory housing authorities excluding Qld and NSW, 2000/01 and 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; returned spreadsheets of STHAs to the 2005/06 Operating Deficits Project

The deterioration in the other six states has been dramatic, with deficits after net interest and depreciation growing by more than 25 per cent.

4.4 Where are the expenditure problems?

4.4.1 It isn't debt servicing

2004 report

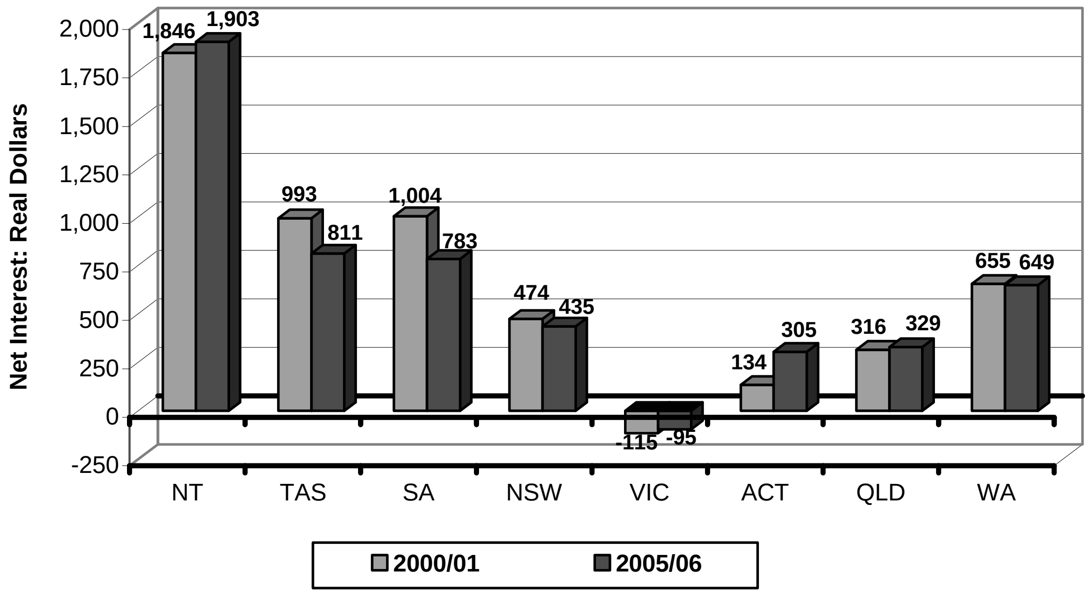
The 2004 study stated:

> "In the last decade (with the exception of Homeswest) all housing authorities have reduced their exposure to debt and substantially reduced their debt servicing payments, to the point where the weighted average is now almost half what it was a decade ago.
>
> More pointedly, if Net Income does not fall any further and all debt servicing payments were eliminated three of the nine authorities would just eliminate their deficits and three would not. Given the trends in income it is unlikely that this measure would provide longer term relief except perhaps for the Northern Territory, Tasmania and South Australia. Such relief would need to be accompanied by either consistent revenue increases or a rapid reduction in the rate of growth of other costs."

2005/06 update

Graph 4.11 sets out a comparison of real net interest payments per dwelling for 2000/01 and 2005/06.

Graph 4.11: Net interest paid per dwelling, all state and territory authorities, 2000/01 and 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; returned spreadsheets of STHAs to the 2005/06 Operating Deficits Project

For all except the ACT and Queensland, real net interest payments per dwelling have continued to decline, and in a context where there have been substantial stock reductions, indicating that such reductions have also been accompanied by further debt repatriation.

4.4.2 Maintenance is contributing

2004 report

The 2004 study stated:

> "Real Maintenance expenditure grew faster than the CPI for building materials for all Authorities other than the ACT, Tasmania and Victoria. Much of the increase in the Northern Territory can be attributed to the unique circumstances applying in that location and the difficulties of obtaining a competitive tender market for building repairs. In addition, until 2001, Maintenance expenditures were under the control of another Government organisation.
>
> However, the rapid increase in Maintenance expenditures can also be attributed to Housing Authorities assuming a more pro-active and information rich role in asset management and the development of 'stock audits' throughout Australia. These processes revealed the extent of maintenance backlogs currently existing and quantified the additional expenditures which are required to bring the portfolios up to acceptable standards. Furthermore, housing authorities concentrated on the introduction of processes designed to ensure rapid responses to responsive maintenance queries and to ensure minimal 'down' time between tenancies. All of these processes have, of course, added to costs being experienced."

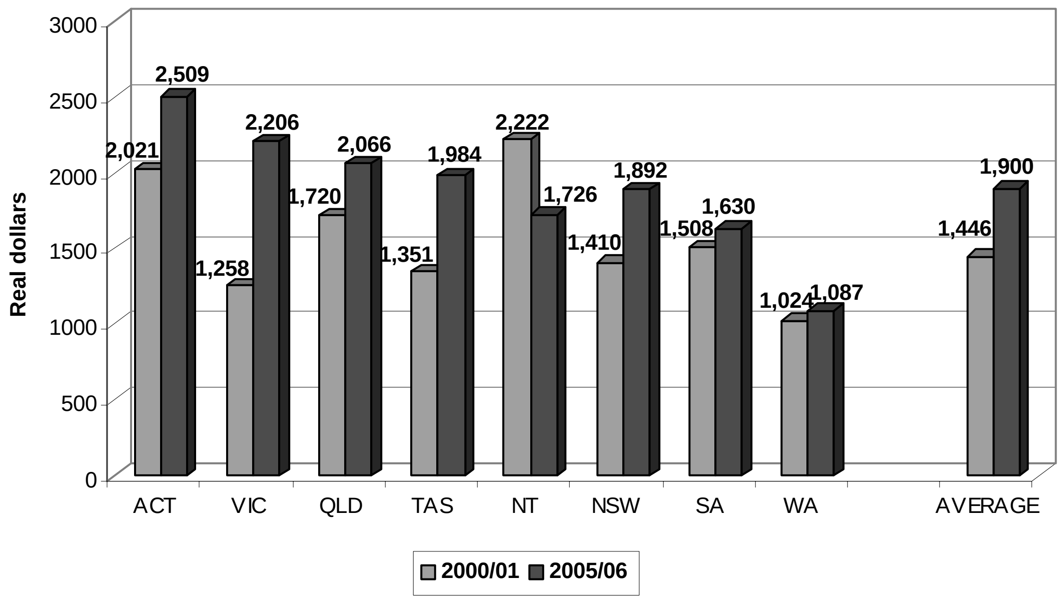
2005/06 update

Graph 4.12 sets out the real maintenance expenditure per dwelling for all states for 2000/01 and 2005/06. Five states have substantially increased their maintenance expenditure per dwelling, two states have experienced small increases and one state has declining outgoings.

Average maintenance expenditure has increased in real terms by more than 30 per cent over the period 2000/01 to 2005/06 and this is double the 15 per cent average increase that occurred in 1995/96 to 2000/01.

In Victoria, expenditure has grown by more than 75 per cent, in Tasmania it has increased by nearly 50 per cent and NSW by more than 33 per cent.

Graph 4.12: Real maintenance expenditures, all state and territory housing authorities, 2000/2001 and 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; returned spreadsheets of STHAs to the 2005/06 Operating Deficits Project

4.4.3 What are the extent and implications of maintenance backlogs?

2004 report

The 2004 study stated:

"As the majority of stock reaches acceptable standards it can be anticipated that the rate of growth in average maintenance spend per dwelling will decline. However, for four of the Housing Authorities this is not likely to be achieved in the next half a decade. [Table 4.1] sets out the Maintenance backlog estimated to exist by the four housing authorities as at March 2003.

[Table 4.1]: Housing Authorities: estimated public housing maintenance backlogs as at March 2003

State or Territory	*Backlog: $M's*
ACT	**80–120**
NSW	**600+**
Tas	**50**
Vic	**180–190**

Source: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI,

2005/06 update

Table 4.2 sets out the current table and includes 2005/06 figures provided by STHAs.

Table 4.2: Housing authorities: estimated public housing maintenance backlogs as at March 2003 and June 2006

State or territory	*Backlog: 2003 ($m)*	*Backlog: 2006 ($m)*
ACT	80–120	100
NT	–	180
NSW	600+	686
SA	–	100
VIC	180–190	180–190
TAS	50	50
Total	935	1,301

Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; returned spreadsheets of STHAs to the 2005/06 Operating Deficits Project

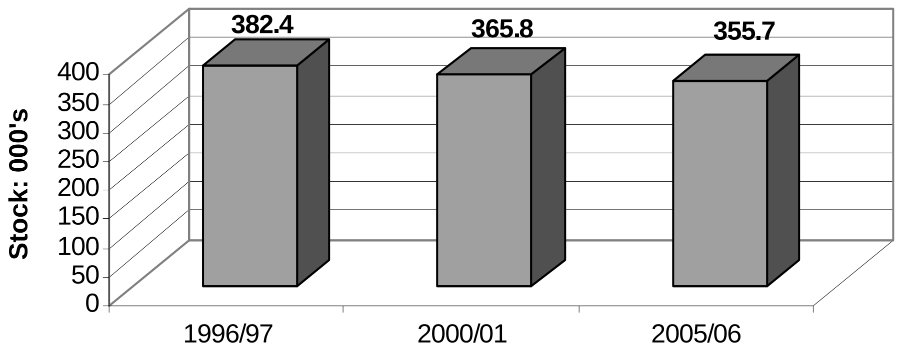
It is clear that because of substantial investments in asset assessment and management information and procedures, STHAs now have considerably more accurate and performance-related estimates of the real extent of existing maintenance backlogs.

These assessments suggest that the extent of the requirement is now 40 per cent higher than that which was reported in 2000/01 and will require continued moderate applications of capital funds for the next few years.

Assets are being liquidated improve the assets that remain

Graph 4.13 sets out the state-owned public and community housing stock net of inter-sector transfers for 1996/97 (when stock levels peaked), 2000/01 and 2005/06. Graph 4.14 documents the stock losses over the same period.

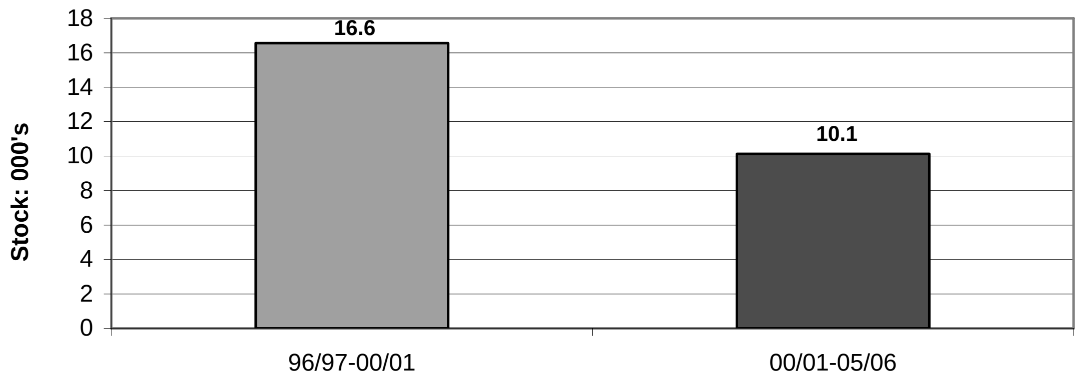
Graph 4.13: Public and community-owned housing stock, Australia, 1996/97 – 2005/06



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; returned spreadsheets of STHAs to the 2005/06 Operating Deficits Project

Note: The 2000/01 figures have been revised downwards by 6,094 owned, but community housing managed, dwellings in NSW to ensure consistency with the 2005/06 supplied figures (which do not include owned but community-managed dwellings in that state).

Graph 4.14: Public and community-owned housing stock losses net of inter-sector transfers and adjustments, Australia, 1996/97 – 2000/01 and 2000/01 – 2005/06



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; returned spreadsheets of STHAs to the 2005/06 Operating Deficits Project

The trend to stock losses that occurred over the period 1996/97 to 2000/01 has continued, albeit at a much slower rate.

In 1996/97, when stock levels peaked, there were approximately 382,000 owned dwellings. By 2000/01 this had fallen by approximately 16,600 to approximately 365,800 and by 2005/06 this had fallen by a further 10,100 dwellings to approximately 355,700.

Most STHAs have advised that because of the squeeze on operations, the strategy has been to heavily invest grants in asset and estate revitalisation; and because grants have been inadequate, proceeds from the sale of older and inappropriate stock have been applied to both debt repatriation and asset revitalisation. In the realisation that operating costs are continuing to rise and revenues have probably reached their zenith, agencies are selling assets in order to potentially reduce their future maintenance and debt service outgoings as a means of extending operational viability.

4.4.4 Will asset restructuring bring about major longer-term operating cost savings?

2004 report

The 2004 study stated:

> "The South Australian Housing Trust was one of the first Housing Authorities to commence asset restructuring and is the most advanced in this process. The Trust has virtually restructured the majority of its portfolio in the last ten years, and sold off nearly 20% of the public housing stock. Whilst this has managed to contain the growth of maintenance expenditure to the lower middle end of the range (38.1%), and has assisted South Australia to reduce its debt servicing burden, such an extensive asset restructuring has not been able to prevent the Trust recently experiencing an Operating Deficit. Unless attention is paid to the rate of growth of other Operating Expenditure items it is probable that the savings achieved from such exercises will be insufficient to prevent deficits from increasing."

2005/06 update

To date there is no evidence from maintenance expenditure data that savings are currently accruing.

4.4.5 Salaries and administration have grown rapidly

2004 report

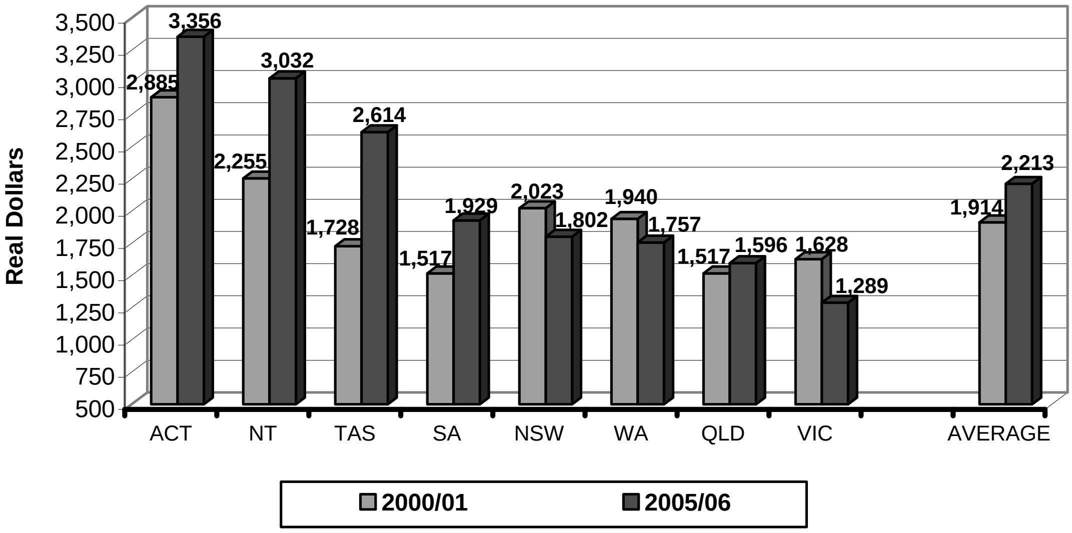
The 2004 study stated:

> "Overhead expenditure is the fastest growing and now one of the largest components of Housing Authority Total Operating Expenditure, exceeding Maintenance expenditure in five Authorities and exceeding Rates expenditure in eight out of the nine Authorities examined.
>
> Given that Wages and Salaries generally tend to grow at just below 1% real over the long term (see Australian Bureau of Statistics Average Weekly Earnings Series), a 10% increase over a decade implies no real growth, and anything less an actual real reduction.
>
> With the exception of Victoria, however, expenditure growth for these components far outstrips the 'no growth' scenario. There is no doubt that a substantial part of the cost increases is due to the drive by Housing Authorities to improve the quality and responsiveness of customer services.
>
> There is also no doubt that, whilst it has not been possible to quantify, Housing Authorities now provide considerable supporting services of a 'non housing' related nature. In addition some component of the increase can be attributed to investment in systems and processes focused on asset management and stock auditing and assessment.
>
> By limiting a large part of the application of funding to capital, earlier CSHA's imposed a discipline on the way in which Housing Authorities approached Operating Expenditures. Effectively, this discipline has now been removed.
>
> A 30% reduction in Overhead would eliminate deficits (before Net Interest and Depreciation) in all but three of the Housing Authorities. When combined with modest reductions in Debt Servicing payments all Housing Authorities, (except the ACT), would return to surplus."

2005/06 update

Graph 4.15 sets out the actual real payment per dwelling for overheads (salaries and employee-related, and administration and management combined) for both 2000/01 and 2005/06. Graph 4.16 shows the real percentage change in this outgoing.

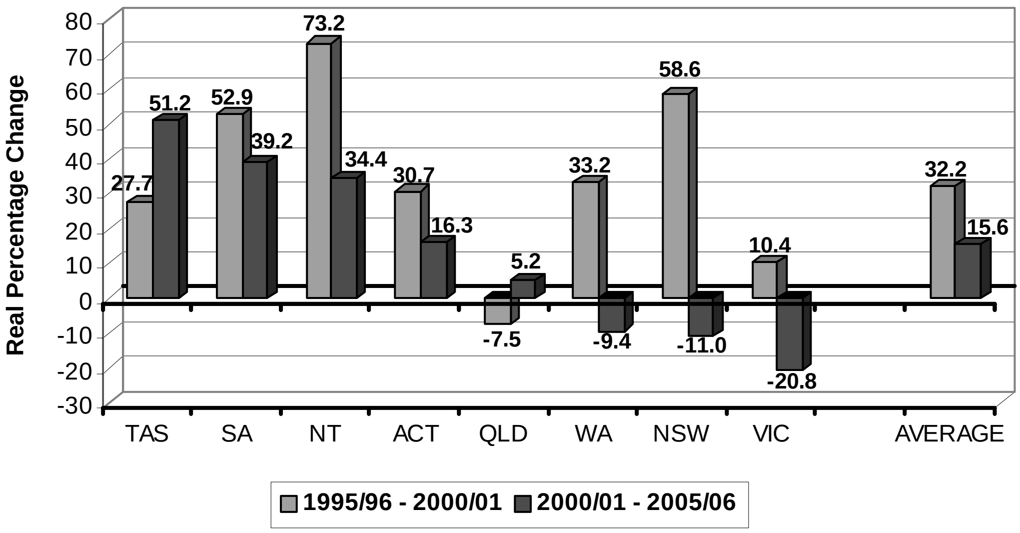
Graph 4.15: Real overhead expenditure per dwelling, all state and territory housing authorities, 2000/01 and 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; returned spreadsheets of STHAs to the 2005/06 Operating Deficits Project

For five states, overhead expenditure grew in real terms over the period 1990/91 to 2005/06 but in one state this was a marginal increase. In the other three states (comprising the two largest STHAs), real overhead expenditure per dwelling fell.

Graph 4.16: Real percentage change in total overhead per dwelling, all state and territory housing authorities, 1995/96 – 2000/01 and 2000/01 – 2005/06



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI, returned spreadsheets of STHAs to the 2005/06 Operating Deficits Project

Graph 4.16 shows the real rate of growth in overhead expenditure for the period 1995/96 to 2000/01 compared to the 2000/01 to 2005/06 outcomes. In the latter period, growth fell in six states, marginally increased in one state and increased substantially in one STHA.

Consequently the average real expenditure increased by 15.6 per cent, less than half the rate of increase of 32.2 per cent experienced in the earlier period.

STHAs have generally sought to rein in overhead expenditure in the period 2000/01 to 2005/06, and in the three largest states, maintenance has taken over as the largest single component of operating expenditures before net interest and depreciation. However, the rate of growth of overhead expenditure is still unreasonably high in three STHAs.

The impact of non-housing support services on operating expenditures has been the subject of debate among housing professionals. At least half the STHAs have now attempted to estimate the cost of these services. The consensus view is that non-housing support services adds between 5 per cent and 10 per cent to total overhead. In 2005/06, the total overhead expenditure averaged 43 per cent of operational expenditure for all STHAs, so a conservative estimate suggests that non-housing support services costs about 4.3 per cent of total operational expenditure before interest and depreciation. If this is a representative outcome then these costs are significant. Put another way, 10 per cent of overhead costs equates to 4.9 per cent of rents after rebates across Australia. This is more than two-thirds of the 6 per cent of the gross rents amount that private sector residential managers commonly receive for their services.

4.4.6 Depreciation has become a major issue

2004 report

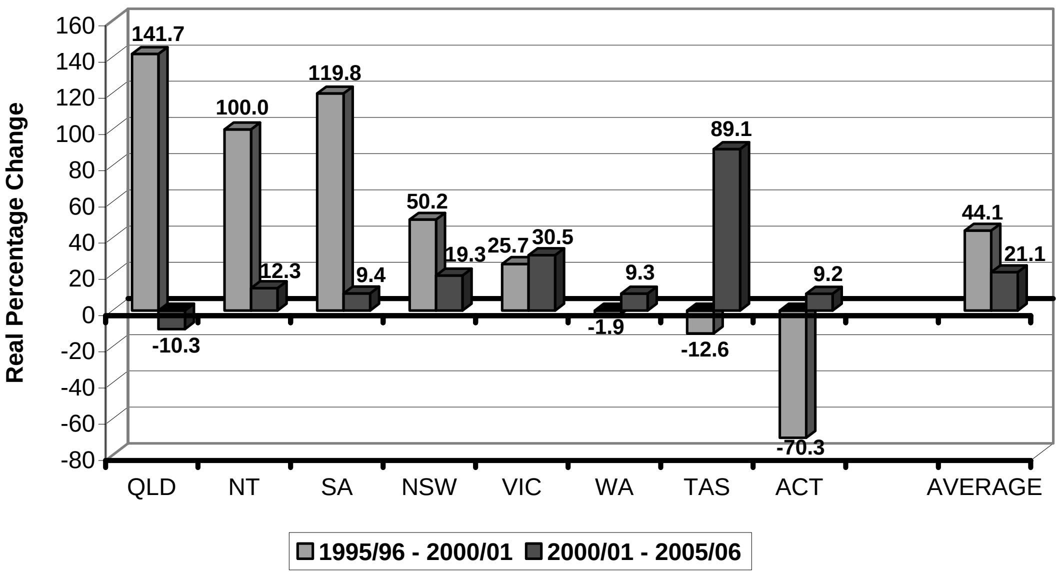
The 2004 study stated:

> "Under Commonwealth requirements Housing Authorities are required to revalue their portfolio at least every two years. Revaluations combined with asset restructuring and improvement are rapidly increasing the provision required for depreciation under the 2% 'straight line' method employed by most Housing Authorities. However, some authorities only undertake formal valuations every five years and perform interim valuations on an annual basis. Some also use a range of depreciation rates of between 2% and 4%.
>
> Revaluation achieves the same balance sheet outcome as that provided by Depreciation and the approach to this expenditure item needs to be revisited."

2005/06 update

Graph 4.17 sets out the real rate of growth of depreciation expenditure per dwelling for the period 1995/96 – 2000/01 and 2000/01 – 2005/06.

Graph 4.17: Real percentage change in depreciation per dwelling, all state and territory housing authorities, 1995/96 – 2000/01 and 2000/01 – 2005/06



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; returned spreadsheets of STHAs to the 2005/06 Operating Deficits Project

Graph 4.17 shows that in all except two STHAs, the rate of growth of depreciation has slowed substantially from the previous period. However, in most STHAs this is still the largest item of expenditure and the comments made in the 2004 study remain valid.

4.5 Valuing the community service obligation correctly: rebates and the implications for funding policy

2004 report

The 2004 study stated:

> "In all other corporatised government services the difference between the commercial price and the amount paid by the recipient of a concession is recognised as a CSO (CSO) and, is fully funded.
>
> For example, for electricity and water supply, the difference between the price per unit of consumption and the amount charged to concessional consumers is treated as a CSO and is normally provided as a Treasury payment to the authority concerned.
>
> 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 CSO per tenancy is the cost of the difference, i.e. the rebate.
>
> There is, in principle, no distinguishing or special reason why the principle applying to CSOs in other corporatised government organisations should not be applied to public housing authorities and the CSO (rebates) fully funded by government.
>
> The issue is not whether this principle should be violated, but whether or not the current concessional price is appropriate to Government housing objectives. If the answer is 'yes', then the principle applying elsewhere should be applied to public housing. Housing Authorities should not have to deal with an ad-hoc and expedient approach to funding policy. The corollary is that a dividend might be demanded, as would be appropriate under the circumstances.

Not only would funding the rebate eliminate deficits in all Authorities except the Northern Territory, it would also provide a basis for longer term financial stability for Housing Authorities.

From the advice of a number of Housing Authorities approximately 50% of all public housing expenditure is either Salaries or has a substantial component which is salary related (for example labour costs account for over 60% of maintenance expenditure in some Authorities). As outlined earlier, Average Weekly Ordinary Time Earnings (a proxy for Salaries and Wages growth) has increased over the last twenty years at slightly less than 1% real. Consequently, even if Housing Authorities were to freeze all costs at today's outlays, expenditures must grow in real terms, i.e. by a proportion greater than the Consumer Price Index. Yet for the next half a decade at least the prognosis is that Net Incomes are going to at best match Inflation and at worst fall substantially in real terms.

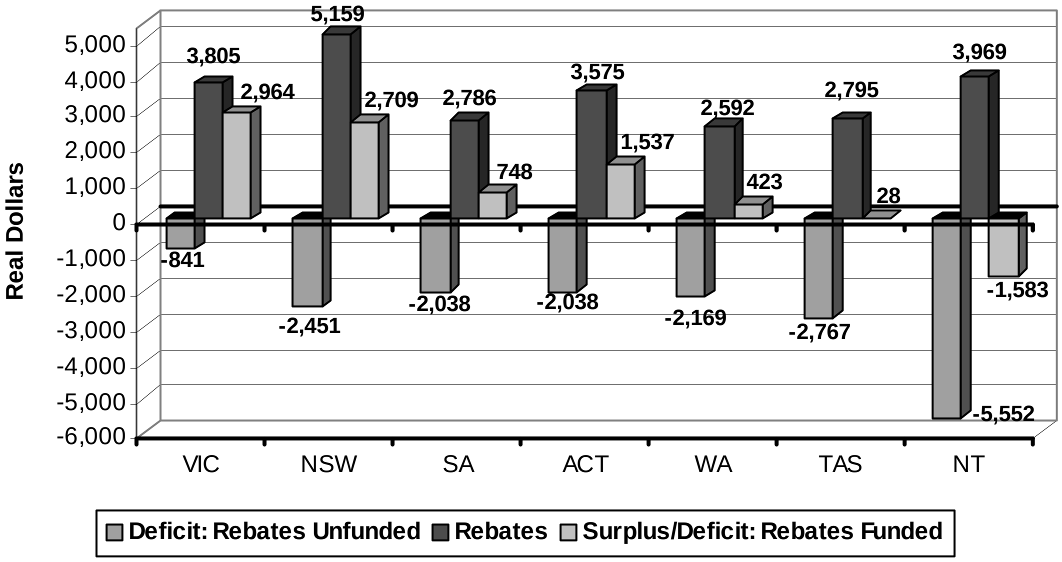
Consequently, it will not be sufficient for Housing Authorities to eliminate current Deficits. If Deficits are not to worsen Housing Authorities must also achieve some real Net Income growth.

Our analysis of rebate growth indicates that for almost all Housing Authorities market rents grow in real terms at about the same rate as AWE (i.e. at around or just less than 1% above Inflation). It can be anticipated that a financial solution based upon fully funding the rebate will enable Net Incomes to at least keep pace with efficiently managed cost structures."

2005/06 update

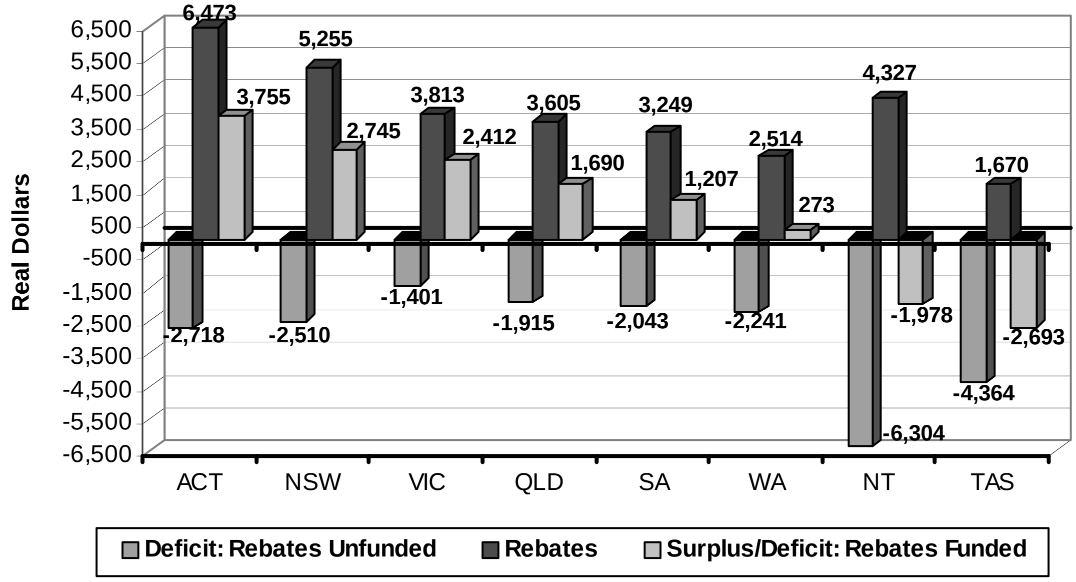
Graphs 4.18 and 4.19 set out for 2000/01 and 2005/06 the real operating surpluses/deficits per dwelling if rebates were fully funded.

Graph 4.18: Real operating surpluses/deficits per dwelling (including net interest and depreciation) if rebates fully funded, all state and territory housing authorities, 2000/01 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Tren*d, AHURI; returned spreadsheets of STHAs to the 2005/06 Operating Deficits Project

Graph 4.19: Real operating surpluses/deficits per dwelling (including net interest and depreciation if rebates fully funded, all state and territory housing authorities, 2005/06 (June 2006 dollars)



Sources: Hall J and Berry M, 2004, *Operating Deficits and Public Housing, Policy Options For Reversing The Trend*, AHURI; returned spreadsheets of STHAs to the 2005/06 Operating Deficits Project

These graphs show that for six of the eight STHAs the comments in the 2004 report are still valid. For both the Northern Territory and Tasmania, however, substantial additional assistance would be required to ensuring operational viability.

4.6 Transparency issues: housing authority financial statements and Productivity Commission performance indicators.

4.6.1 Housing authority income and expenditure statements

2004 report

The 2004 study stated:

> "The analysis on which the conclusions above were based required substantial re-working and supplementation of the relevant housing authority financial statements in their current public form.
>
> The published income and expenditure statements of most Housing Authorities do not reveal clearly how the Operating part of the business is actually functioning.
>
> Firstly, the statements include many receipts and payments which are not recurrent but more in the nature of capital. The statements also show these receipts and payments are irregular, and variable in their amounts.
>
> Such receipts and payments include:
>
> → profits or losses on the sale of dwellings;
>
> → project management fees calculated with reference to the capital value of redevelopment or asset restructuring projects; and
>
> → premiums or discounts arising from the sale of investment instruments.

Secondly, whilst some housing authorities excise ‘abnormals’ from above the line calculations of income and expenditures, many do not. Because of the magnitude of some of these ‘abnormals’ they can have a material effect on the reported operating result.

Such abnormals include:

- adjustments for over or under provision of Superannuation and other employee entitlement liabilities; and
- adjustments to income or expenditure accruing from forgiven loan liabilities or increases in loan liabilities as a result of interest rate movements.

Thirdly, most authorities include grants being applied to public housing in the income statement and grant payments to third parties in the expenditure statement. In many cases the amounts are substantially different. Grant payments to third parties may not be related to public or community housing outcomes.

Finally, the costs associated with head-leased dwellings are often treated differently to the costs associated with mainstream public housing. In the former, no income is normally bought to book, nor are the normal expenditure items of rates, maintenance etc. In some cases the subsidies payable re commercial head-leased rents may be shown as lease payments above the line, in other cases, these subsidies may be included in grants made and be outside the standard expenditure outcome.

There is therefore a need to obtain regular financial performance reporting on an appropriate per unit basis (tenantable dwellings), which can more accurately reflect the short and longer term trends affecting the financial performance of public housing.

Productivity commission performance indicators

The Productivity Commission produces a set of indicators which are used by the Commonwealth to assess the ongoing performance of public housing authorities.

These indicators have been designed to assess efficiency and effectiveness.

The Indicators which are of concern to this analysis fall into three main categories, indicators which are designed to assess:

- the efficiency of public housing authorities;
- the targeting of public housing authorities; and
- the quality and timeliness of the service of public housing authorities.

Efficiency

These indicators are set out in Table 15A17 of the Productivity Commission’s Report On Government Services and attempt to quantify per unit (tenantable dwellings) outcomes for various aspects of recurrent and capital expenditure.

The recurrent indicators are inaccurate because:

- the gross recurrent expenditure figures suffer from the definitional problems and inaccuracies outlined above.
- the divisor, i.e. tenantable dwellings, makes no distinction between head-leased or dwellings leased from a third party and owned stock. If headlease subsidies are stated as grants and subsidies paid and set below the bottom line then they could easily substantially discount the per unit cost calculated for the expenditure items. This is because head-leased dwellings would be included in the number of dwellings used to divide the expenditure item to arrive at the cost per unit, yet no expenditures may be recorded for these dwellings in the expenditure component of the statement.

Consequently components like average administration costs per dwelling etc., will be erroneous.

Targeting

There are two primary indicators relating to targeting and these are:

- proportion of households in need and who are in public housing; this measure assesses the proportion of total households both public and private in need (i.e. paying more than 25% income in average private rent payment required) who are in public housing; and
- proportion of those occupying public housing who are in need; i.e. this measures the proportion of public tenants who would be in need (i.e. experiencing housing stress) if they were having to obtain accommodation in the private rental market.

The assumption behind these indicators is that targeting to those most in need (which usually equates with the lowest household incomes) meets the vertical equity objectives of the CSHA.

However, given the clear evidence that tight targeting is instrumental in driving down the Net Incomes of public housing authorities (and probably contributes to higher per unit costs because of the additional support services that many new tenants require), it must be questioned as to whether, in conjunction with the other indicators, this is a sensible measure of public housing performance, under the current funding and regulatory settings.

Service Quality: Indicators Related to Continuous Improvement

The indicators which fit this category are:

- Overcrowding or underutilisation[3]; i.e. match of dwelling to household size;
- Average turnaround time (days)[4]
- Tenant satisfaction[5]; and
- Tenant assessments of housing stock condition[6].

With the exception of overcrowding, these indicators do not rely upon an objective standard, but as stated earlier, on the notion of continuous improvement, and on comparing the performance of one Housing Authority to another.

There is no doubt that the relationship between the Commonwealths focus on improving the condition of the housing stock, the introduction of continuous improvement indicators, and the removal of the restrictions on the application of funds to recurrent expenditure has provided a major contribution to the growth in expenditure outcomes per dwelling unit identified in this report and highlighted in earlier sections of this chapter."

[3] Productivity Commission, 2000, Report On Government Services, Table 15A.14 pg1431
[4] Ibid, Table 15A.23 pg 1436
[5] Ibid, Table 15A.12 pg1430
[6] Ibid, Table 15A.17 pg 1433

2005/06 update

The issues pertaining to transparency have not changed and the comments in the 2004 report are still valid.

4.7 The characteristics of financially successful social housing services

2004 report

The 2004 report stated:

> "Some useful general lessons can be learnt from considering the situations of financially successful social housing services in Europe.
>
> There appear to be three main characteristics that distinguish these services from Australian public housing authorities. These characteristics all relate to the Income side of operations, viz:
>
> - central governments fully recognise the CSO inherent in providing affordability outcomes, and the principal form of financial support is recurrent subsidies based on the difference between market and cost or income related rents;
> - social housing authorities are assured that their Net Rents per household will grow in real terms because the sector is not rigidly targeted to the very lowest incomes. Many portfolios include a tenant population with a range of incomes, with a substantial proportion of the tenant population in employment, whose incomes grow in real terms. This enables housing authorities to be confident that real cost increases will be able to be met through revenues, notwithstanding additions to the housing stock. Combined with central government support, it enables social housing providers to grow their portfolios and so maintain their income mix whilst attending to those in greatest need.
> - the real incomes of pension and beneficiary social housing recipients is considerably higher than in Australia because the base level of pensions and benefits is a greater proportion of average weekly earnings."

2005/06 update

The principles outlined in points 1 and 2 are even more relevant in the current context.

4.8 Some system options

2004 report

The 2004 study stated:

> "We conclude that, on the analysis in this study, if the current policy focus is maintained, Australian public housing will not remain viable.
>
> In the last decade many housing authorities have increased the proportion of income charged to tenants and all housing authorities now charge a minimum of 25% of assessable income. Consequently, the decline that might have been experienced in real net rents was mitigated by these changes to rent charging. If affordability benchmarks of 25% of assessable income in rent are maintained, changes to rent charging will not be an available tool to relieve growing deficits. Maintenance of tight targeting will ensure the decline in real Net Rents per unit experienced by some housing authorities will become more widespread and accelerate.

In addition, for many of the Operating Expenditure items, continuing to seek improvements in housing stock and continuous improvements in client services cannot be achieved without the acceleration of the trend to real cost increases. In a context where:

(d) the funding of public housing is divorced from its community service obligations;

(e) affordability benchmarks of 25% of assessable income are maintained;

(f) tight targeting continues; and

(g) the emphasis on continuous service improvement is enforced;

then incomes per unit will fall, real expenditures per unit will increase and operating deficits will continue to grow.

This suggests that the focus must be on firstly eliminating deficits and then assuring real Income growth per household."

2005/06 update

Notwithstanding the major effort at revenue raising and the consistent effort to rein in overhead expenditures, the operating position of almost all the STHAs has continued to deteriorate, in some cases alarmingly.

Moreover, in an effort to ensure asset viability and in the face of very difficult operating positions, STHAs have disposed of in excess of $2.5 billion of public housing stock to support debt repatriation and asset improvement.

While revenues did grow, this is a once-off effect and cannot be repeated. As costs rise further, assets are likely to be disposed of to shore up operational viability. It is 'death by a thousand cuts' and unless there are substantial new funds and/or completely different policy approaches it is likely that Australia's social housing system will be further eroded in the next decade.

All the comments in 2004 report are even more valid in 2007.

4.9 Future directions

2004 report

The 2004 study stated:

"On the basis of the study findings, summarised above, the following implications for policy are suggested;

A Working Party of Commonwealth and State Housing Officials be established to:

- examine ways in which the CSO experienced by Australian Housing Authorities can be fully funded (i.e. the difference between market and income related rents), including changes to current funding arrangements;
- prepare detailed forecasts of the likely Net Income of all Australian Housing Authorities given no change to targeting policy;
- examine other options by which Net Incomes for Housing Authorities can grow in real terms, including;
    - relaxation of affordability benchmarks and abolition of current Productivity Commission targeting indicators;
    - abandonment of current targeting policies;

- growing the housing stock to diversify the income base;
- other relevant options.

6. A similar mechanism could be used to examine in detail the current Productivity Commission efficiency indicators with a view to developing a financial reporting system which makes more transparent the trends in the operations of public housing authorities, building upon the method and definitions used in this study.
7. In the absence of any changes to Commonwealth policy, Australian State Housing Authorities could establish an in-depth investigation of the quality and extent of services that existing public housing authorities can afford and, if necessary, seek abolition of the Productivity Commission continuous improvement indicators and replacement by independent service standards;
8. For many expenditure items there was great variability between Housing Authorities. A more detailed analysis of the lowest cost authorities could be instituted to establish how these positive outcomes have been achieved and how the other authorities could benefit from the resulting efficiencies.
9. A working party of Commonwealth and State Chief Financial Officers and State Treasury Officials could examine and develop alternatives to the current treatment of Depreciation in Public Housing Authorities."

2005/06 update

In response to the 2005/06 questionnaire, STHAs overwhelmingly suggested:

- funding the CSO; and
- developing client profiles with a much higher proportion of households in receipt of incomes sourced from other than pension and benefits.

Other options suggested are:

- selling assets;
- funding the non-housing support services cost;
- forgiving Commonwealth debt; and
- increasing private sector involvement.

The changes to net income caused by client profile change may be close to an end, but the majority of the other policy suggestions in the 2004 report remain valid.

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ATTACHMENT 1: METHODOLOGY

Accrual or cash

As far as is possible an accrual approach be applied to the analysis but wherever possible historical actual outcomes be the primary source data (i.e. the previous years audited statements).

Analysis principles

The following principles apply to the deficit analysis

1. supplemental revenue or costs such as;
   - consolidated allocations;
   - grants or subsidies received or paid;

   should not be recognised.
2. the results should be adjusted so that the effect of an authority's debt structure does not overwhelm the result;
3. no receipts or payments in the nature of capital should be recognised in the analysis, i.e. such as;
   - gains or losses on the sale of assets;
   - expenses which extend the useful life of the assets or adds attributes which were not previously part of the asset;
   - assets demolished; and
   - assets written off.
4. one off's should be excised, these excisions to include;
   - revenue or costs recognised on transfer of loans; and
   - one off superannuation surplus or deficit adjustments.
5. both the receipts and payments and assets and liabilities associated with housing authority residential headleasing from private landlords should be excised;
6. a layering approach be used so that core results can be added to and the effect of particular marginal or potential distorting items can be assessed.

Unit revenue and cost analysis

In order to produce a comparable analysis for all housing authorities it will be necessary to reduce the outcomes for each line item to a per unit analysis (per dwelling or per person housed).

Revised core items

Items in Table A.1 below are included in the core analysis.

Table A.1: housing authorities: income and expenditure statements: revised core items

Revenues	*Expenditures*
→ Rents	→ Property and residential tenancy
→ Management fees	→ Employee related
→ Sundry income	→ Administrative and working
	→ Doubtful debts

Revised 'add backs'

Items in Table A2 should be added back 1 by 1 to provide a layering analysis.

Table A.2: housing authorities: income and expenditure statements: revised 'add back' items

Revenues	*Expenditures*
	→ Rental rebates
→ Grants and subsidies received (i.e. consolidated fund allocations etc.)	→ Grants and subsidies paid
→ Interest earned	→ Borrowing costs and interest paid
	→ Depreciation

ATTACHMENT 2: DEFICIT DEFINITIONS

Accrual or cash

Accrual basis means the accounting basis where the *assets*, *liabilities*, *equity*, *revenues* and *expenses* are *recognised* in the *financial* years to which they relate, regardless of when *cash* is received or paid (Australian Accounting Standard, (AAS) 6).

Cash means *cash on hand* and *cash equivalents*.

Cash equivalents means highly liquid *investments* with short periods to maturity which are readily convertible to *cash on hand* at the *investor's* option and are subject to an insignificant risk of changes in value, and borrowings which are integral to the cash management function and which are not subject to a term facility (AAS 28).

Unit revenue and cost analysis

The unit of measurement to be applied to the line items was to be tenantable dwellings owned by housing authorities and persons occupying tenantable dwellings, subject to the revenues and costs of any leasing arrangements being excised from the analysis. However, a number of housing authorities could not provide tenantable dwellings for early years so total owned and operated stock, including all owned and operated community and aboriginal housing stock, minus all dwellings leased or head-leased by the housing authority.

Rents

Rental income be defined as gross rents minus rental rebates but before arrears and defaults written off and/or provisioned for.

Grants and subsidies received (excluding rebates)

In Australia these grants and subsidies arise from two sources, the Commonwealth Government and State Treasuries for matching arrangements. In New Zealand grants would include any allocation from the New Zealand Treasury. The main grants and subsidies in Australia are:

- Commonwealth State Housing Agreement (CSHA) – General Assistance (Base funding)
- CSHA – Community Housing
- CSHA – Crisis Accommodation
- Aboriginal Housing Program
- Grants – Interest Assistance
- state matching
- Other state funding

Interest earned

Interest earned is simply any interest received by a housing authority for funds invested in the normal financial markets

Management fees

housing authorities often receive fees for managing dwellings on behalf of other governmental or non profit agencies.

Net gains on the sale of assets

This includes proceeds from the sale of residential and commercial properties, land, motor vehicles, office furniture and equipment, minus the cost of sales, including the cost of acquiring the asset sold.

Sundry income

Sundry income usually incorporates the following items as reflected in the 2001 Department of Housing NSW Financial Statements:

- contributions from other government agencies;
- rental bonds recovered;
- insurance recovery;
- loan transfers to NSW Treasury;
- project management fees;
- bad debts recovered;
- contributions from community groups; and
- other, (unclaimed monies).

Superannuation surplus distribution

For most housing authorities the calculation of the superannuation position at the end of each year uses actuarial assumptions. If the actuarial based analysis reports a surplus this is reported as revenue and if a deficit is reported the decrease is reported as additional employer's contribution to superannuation.

Net income 1

Net income 1 is therefore the sum of Net Rents, Management Fees and Sundry Income, but excluding rebates, grants and any net interest earned.

Net income 2

Net income 2 includes all of the items in Net income 1 any also any net interest earned (the net of interest earned and interest paid

Rental rebates

Rental rebates are the difference between the gross market residential rents and actual rent charged.

Grants and subsidies paid

Most housing authorities provide a variety of grants and subsidies to third parties. These take the form of grants for short term rental assistance in the private market such as bonds, grants to non-profit organisations for the provision of social housing support, grants to organisations providing care which maintains frail or disabled persons in the family home, and headleasing or leaseback private rental subsidy payments for public housing tenants. The types of typical payments are listed below

Grants

- rental assistance;
- housing community assistance;
- housing grants;
- neighbourhood improvement (community);
- home and community care; and
- other.

Subsidies

- assistance towards housing initiatives;
- land tax;
- rental subsidy;
- leasing; and
- other

Borrowing costs and interest paid

Borrowing costs represents any costs associated with the raising of a loan, and interest paid the sum of the interest payments made for the variety of current concessional and non-concessional loan liabilities of the housing authority.

Property and residential tenancy

Property and residential tenancy usually includes:

- council and water rates;
- repairs and maintenance;
- lease expense; and
- residential tenancy and other expenses.

but excludes expenditure which could properly be classified as an upgrading, improvement or redevelopment.

Assets demolished and assets written off

Most housing authorities have a policy that where properties meet certain criteria they may be written down or demolished in order to provide appropriate housing facilities in a cost effective manner.

Employee related

Salaries, annual leave and on-costs

Most housing authorities recognise liabilities for salaries, annual leave and annual leave loading at pay rates as at the reporting date. Amounts payable in respect of pay-roll tax, workers' compensation insurance premiums and fringe benefits tax, which are consequential to employment, are recognised as liabilities and expenses where the employee entitlements to which they relate have been recognised.

Long service leave

Similarly the approach to long service leave entitlements is to normally recognise them at nominal amounts, based on pay rates as at reporting date for all employees with at least five years service. The estimated value of long service leave entitlements expected to be paid during the next twelve months is classified a current liability.

Administrative and working

This line item is

- "rent;
- staff development;
- building maintenance and utilities;
- computer maintenance and software licences;
- printing, postage and stationery;
- motor vehicle expenses;
- auditors' remuneration;
- management and other fees;
- travel;
- telecommunication;
- consultants' fees; and
- other."

Doubtful debts

Coopers and Lybrand, (1995) recommended that a general and specific provision for bad and doubtful debts should be raised based on past experience. The recommended policy excluding specific provisions which may be required, is

1. For current tenants which are in arrears:
   - Nil –under two weeks in arrears;
   - 25 per cent - 2 to 4 weeks in arrears;
   - 50 per cent - 4 to 8 weeks in arrears; and
   - 95 per cent to 100 per cent - over 8 weeks in arrears.
2. For vacated tenants which are in arrears – 95 per cent to 100 per cent of the balance outstanding.

Depreciation

For accounting purposes depreciation is defined as follows:

- Australian Accounting Standard 4 (AAS 4) defines depreciation expense as "an expense recognised systematically for the purpose of allocating the depreciable amount of a depreciable asset over its useful life".
- Accounting Policy Statement No. 7 (APS 7) issued by the South Australian Treasury notes that depreciation is "a systematic charge which recognises the consumption of assets over their useful lives".

Depreciation accounts for the USE of an economic resource which has a limited life. It is a process of allocation not valuation.

Useful Life

AAS 4 defines useful life as:

> "the estimated period of time over which the future economic benefits embodied in a depreciable asset are expected to be consumed by the entity".

Coopers and Lybrand, (1995) suggested that

> "rental dwellings should be classified as fixed assets, not investment properties as the properties are not principally being held for the accretion of wealth. Accordingly depreciation should be calculated on a straight line basis at a rate which realistically represents the useful of the asset.
>
> Therefore depreciation should be calculated on a straight line basis at a rate which realistically represents the useful life of the asset. For consistency a useful life of 50 years be adopted."

The Productivity Commission , (2001):

> "depreciation should be calculated on a straight-line basis at a rate which realistically represents the useful life of the asset."

Net expenditures 1

Net Expenditures include the sum of the items:

- Maintenance;
- Rates;
- Salaries and Employee Related;
- Administrative and Working; and
- Bad and Doubtful Debts;
- But excluding rebates, net interest paid and Depreciation.

Net expenditures 2

Net Expenditures 2 includes all of the above plus net interest paid and depreciation.

Operating surpluses/deficits

Operating Surpluses/ Deficits is the sum of Net Incomes 1 and Net Expenditures 1.

ATTACHMENT 3: SAMPLE SPREADSHEET FOR ANALYSIS

	1990/91	1991/92	1992/93	1993/94	1994/95	1995/96	1996/97	1997/98	1998/99	1999/2000	2000/2001
INCOME											
Net Rents	41,638,000	42,530,000	42,960,000	44,665,000	44,992,000	46,896,000	47,034,000	45,839,000	44,662,000	46,944,000	49,054,000
Management Fees	0	0	0	0	0	0	0	0	0	0	0
Sundry Income	1,150,789	485,000	513,000	1,244,000	1,468,000	1,470,000	817,000	1,670,000	1,355,000	1,460,000	1,707,000
TOTAL OPERATING REVENUE	**42,788,789**	**43,015,000**	**43,473,000**	**45,909,000**	**46,460,000**	**48,366,000**	**47,851,000**	**47,509,000**	**46,017,000**	**48,404,000**	**50,761,000**
EXPENDITURES											
Property and Residential Tenancy											
Maintenance	16,477,000	20,553,000	19,470,000	18,337,000	19,291,000	15,035,000	16,071,000	22,405,000	18,878,000	20,019,000	20,673,000
Rates	9,581,000	10,641,000	11,132,000	12,572,000	12,348,000	14,396,000	12,130,000	12,348,000	12,141,000	12,078,000	13,499,000
Total Property and Resid Tenancy	**26,058,000**	**31,194,000**	**30,602,000**	**30,909,000**	**31,639,000**	**29,431,000**	**28,201,000**	**34,753,000**	**31,019,000**	**32,097,000**	**34,172,000**
Employee Related	6,552,314	7,411,847	8,616,521	8,004,291	10,771,935	13,041,000	13,861,000	13,013,000	12,275,000	10,275,000	12,837,000
Adminstrative and Working	4,254,608	4,815,816	5,358,216	6,901,772	7,485,744	8,350,000	6,362,000	10,777,000	10,760,000	13,162,000	16,683,000
Total Administrative and Working	**10,806,922**	**12,227,663**	**13,974,737**	**14,906,063**	**18,257,679**	**21,391,000**	**20,223,000**	**23,790,000**	**23,035,000**	**23,437,000**	**29,520,000**
Doubtful Debts	682,000	685,000	1,139,000	1,095,000	2,136,000	6,225,000	1,915,000	988,000	1,343,000	1,264,000	681,000
TOTAL OPERATING COSTS	**37,546,922**	**44,106,663**	**45,715,737**	**46,910,063**	**52,032,679**	**57,047,000**	**50,339,000**	**59,531,000**	**55,397,000**	**56,798,000**	**64,373,000**
OPERATING SURPLUS/DEFICIT	**5,241,867**	**-1,091,663**	**-2,242,737**	**-1,001,063**	**-5,572,679**	**-8,681,000**	**-2,488,000**	**-12,022,000**	**-9,380,000**	**-8,394,000**	**-13,612,000**
ADD BACKS											
INCOME											
Grants and Subsidies Received	7,274,813	7,471,000	7,335,000	9,996,000	11,492,000	9,615,000	9,617,000	8,636,000	19,240,000	25,581,000	34,909,000
Interest Earned	333,871	345,000	270,000	200,000	343,000	2,187,000	2,113,000	1,654,000	1,096,000	1,325,000	1,185,000
TOTAL ADDITIONAL REVENUE	**7,608,684**	**7,816,000**	**7,605,000**	**10,196,000**	**11,835,000**	**11,802,000**	**11,730,000**	**10,290,000**	**20,336,000**	**26,906,000**	**36,094,000**
EXPENDITURES							0.41				
Rental Rebates	35,719,000	40,225,000	44,425,000	47,876,000	47,295,000	46,184,000	45,282,000	44,067,000	43,134,000	39,007,000	36,575,000
Grants and Subsidies Paid	0	0	0	567,000	2,240,000	0	0	2,628,000	33,000	622,000	0
Interest Paid	7,683,148	7,803,000	7,334,000	7,597,000	7,713,000	7,998,695	7,505,396	6,567,273	2,687,686	2,623,732	2,556,112
Depreciation	20,553,000	16,605,000	16,505,000	16,949,000	24,612,000	30,226,000	26,694,000	24,331,000	20,986,000	8,212,000	9,487,000
TOTAL ADDITIONAL EXPENDITURES	**28,236,148**	**24,408,000**	**23,839,000**	**25,113,000**	**34,565,000**	**38,224,695**	**34,199,396**	**33,526,273**	**23,706,686**	**11,457,732**	**12,043,112**
SURPLUS DEFICIT AFTER INTEREST	**-2,107,410**	**-8,549,663**	**-9,306,737**	**-8,398,063**	**-12,942,679**	**-14,492,695**	**-7,880,396**	**-16,935,273**	**-10,971,686**	**-9,692,732**	**-14,983,112**
SURPLUS DEFICIT AFTER GRANTS	**12,516,680**	**6,379,337**	**5,092,263**	**8,427,937**	**3,679,321**	**934,000**	**7,129,000**	**-6,014,000**	**9,827,000**	**16,565,000**	**21,297,000**
SURPLUS DEFICIT AFTER DEPRECIATION	**-15,311,133**	**-17,696,663**	**-18,747,737**	**-17,950,063**	**-30,184,679**	**-38,907,000**	**-29,182,000**	**-36,353,000**	**-30,366,000**	**-16,606,000**	**-23,099,000**
SURPLUS/DEFICIT AFTER GRANTS AND INTEREST	**5,167,403**	**-1,078,663**	**-1,971,737**	**1,030,937**	**-3,690,679**	**-4,877,695**	**1,736,604**	**-10,927,273**	**8,235,314**	**15,266,268**	**19,925,888**
SURPLUS/DEFICIT AFTER GRANTS, INTEREST AND DEPRECIATION	**-15,385,597**	**-17,683,663**	**-18,476,737**	**-15,918,063**	**-28,302,679**	**-35,103,695**	**-24,957,396**	**-35,258,273**	**-12,750,686**	**7,054,268**	**10,438,888**
SURPLUS/DEFICIT AFTER INTEREST AND DEPRECIATION	**-22,660,410**	**-25,154,663**	**-25,811,737**	**-25,347,063**	**-37,554,679**	**-44,718,695**	**-34,574,396**	**-41,266,273**	**-31,957,686**	**-17,904,732**	**-24,470,112**

TENANTABLE STOCK	**12,361**	**12,251**	**12,357**	**12,406**	**12,491**	**12,500**	**12,289**	**12,209**	**11,987**	**11,674**	**11,724**
TOTAL STOCK	**12,361**	**12,251**	**12,357**	**12,406**	**12,491**	**12,500**	**12,289**	**12,209**	**11,987**	**11,674**	**11,724**
PER UNIT											
	1990/91	**1991/92**	**1992/93**	**1993/94**	**1994/95**	**1995/96**	**1996/97**	**1997/98**	**1998/99**	**1999/2000**	**2000/2001**
INCOME											
Net Rents	3,368	3,472	3,477	3,600	3,602	3,752	3,827	3,755	3,726	4,021	4,184
Management Fees	0	0	0	0	0	0	0	0	0	0	0
Sundry Income	93	40	42	100	118	118	66	137	113	125	146
TOTAL OPERATING REVENUE	3,462	3,511	3,518	3,701	3,719	3,869	3,894	3,891	3,839	4,146	4,330
EXPENDITURES	32%										
Property and Residential Tenancy											
Maintenance	1,333	1,678	1,576	1,478	1,544	1,203	1,308	1,835	1,575	1,715	1,763
Rates	775	869	901	1,013	989	1,152	987	1,011	1,013	1,035	1,151
Total Property and Resid Tenancy	2,108	2,546	2,476	2,491	2,533	2,354	2,295	2,847	2,588	2,749	2,915
Employee Related	530	605	697	645	862	1,043	1,128	1,066	1,024	880	1,095
Adminstrative and Working	344	393	434	556	599	668	518	883	898	1,127	1,423
Total Admin & Working	874	998	1,131	1,202	1,462	1,711	1,646	1,949	1,922	2,008	2,518
Doubtful Debts	55	56	92	88	171	498	156	81	112	108	58
TOTAL OPERATING COSTS	3,038	3,600	3,700	3,781	4,166	4,564	4,096	4,876	4,621	4,865	5,491
OPERATING SURPLUS/DEFICIT	**424**	**-89**	**-181**	**-81**	**-446**	**-694**	**-202**	**-985**	**-783**	**-719**	**-1,161**
ADD BACKS											
INCOME											
Grants and Subsidies Received	589	610	594	806	920	769	783	707	1,605	2,191	2,978
Interest Earned	27	28	22	16	27	175	172	135	91	114	101
TOTAL ADDITIONAL REVENUE	616	638	615	822	947	944	955	843	1,697	2,305	3,079
EXPENDITURES											
Rental Rebates	2,890	3,283	3,595	3,859	3,786	3,695	3,685	3,609	3,598	3,341	3,120
Grants and Subsidies Paid	0	0	0	46	179	0	0	215	3	53	0
Interest Paid	622	637	594	612	617	640	611	538	224	225	218
Depreciation	1,663	1,355	1,336	1,366	1,970	2,418	2,172	1,993	1,751	703	809
TOTAL ADDITIONAL EXPENDITURES	2,284	1,992	1,929	2,024	2,767	3,058	2,783	2,746	1,978	981	1,027
SURPLUS DEFICIT AFTER INTEREST	-170	-698	-753	-677	-1,036	-1,159	-641	-1,387	-915	-830	-1,278
SURPLUS DEFICIT AFTER GRANTS	1,013	521	412	679	295	75	580	-493	820	1,419	1,817
SURPLUS DEFICIT AFTER DEPRECIATION	-1,239	-1,445	-1,517	-1,447	-2,417	-3,113	-2,375	-2,978	-2,533	-1,422	-1,970
SURPLUS/DEFICIT AFTER GRANTS AND INTEREST	418	-88	-160	83	-295	-390	141	-895	687	1,308	1,700
SURPLUS/DEFICIT AFTER GRANTS, INTEREST AND DEPRECIATION	-1,245	-1,443	-1,495	-1,283	-2,266	-2,808	-2,031	-2,888	-1,064	604	890
SURPLUS/DEFICIT AFTER INTEREST AND DEPRECIATION	-1,833	-2,053	-2,089	-2,043	-3,007	-3,577	-2,813	-3,380	-2,666	-1,534	-2,087

REAL PER UNIT											
CPI	*1.25*	*1.18*	*1.15*	*1.14*	*1.13*	*1.13*	*1.09*	*1.05*	*1.03*	*1.01*	*1.00*
	1990/91	1991/92	1992/93	1993/94	1994/95	1995/96	1996/97	1997/98	1998/99	1999/2000	2000/2001
INCOME											
Net Rents	4,195	4,108	3,997	4,096	4,070	4,227	4,188	3,937	3,841	4,071	4,184
Management Fees	0	0	0	0	0	0	0	0	0	0	0
Sundry Income	116	47	48	114	133	132	73	143	117	127	146
TOTAL OPERATING REVENUE	4,311	4,155	4,044	4,210	4,202	4,359	4,261	4,080	3,958	4,197	4,330
EXPENDITURES											
Property and Residential Tenancy											
Maintenance	1,660	1,985	1,811	1,681	1,745	1,355	1,431	1,924	1,624	1,736	1,763
Rates	965	1,028	1,036	1,153	1,117	1,297	1,080	1,061	1,044	1,047	1,151
Total Property and Resid Tenancy	2,625	3,013	2,847	2,834	2,862	2,653	2,511	2,985	2,668	2,783	2,915
Employee Related	660	716	802	734	974	1,175	1,234	1,118	1,056	891	1,095
Adminstrative and Working	429	465	498	633	677	753	567	926	925	1,141	1,423
Total Admin & Working	1,089	1,181	1,300	1,367	1,651	1,928	1,801	2,043	1,981	2,032	2,518
Doubtful Debts	69	66	106	100	193	561	171	85	116	110	58
TOTAL OPERATING COSTS	3,782	4,260	4,253	4,301	4,706	5,142	4,483	5,113	4,764	4,925	5,491
OPERATING SURPLUS/DEFICIT	**528**	**-105**	**-209**	**-92**	**-504**	**-782**	**-222**	**-1,033**	**-807**	**-728**	**-1,161**
ADD BACKS											
INCOME											
Grants and Subsidies Received	733	722	682	917	1,039	867	856	742	1,655	2,218	2,978
Interest Earned	34	33	25	18	31	197	188	142	94	115	101
TOTAL ADDITIONAL REVENUE	767	755	707	935	1,070	1,064	1,045	884	1,749	2,333	3,079
EXPENDITURES											
Rental Rebates	3,598	3,886	4,133	4,390	4,278	4,162	4,032	3,785	3,710	3,382	3,120
Grants and Subsidies Paid	0	0	0	52	203	0	0	226	3	54	0
Interest Paid	774	754	682	697	698	721	668	564	231	228	218
Depreciation	2,071	1,604	1,535	1,554	2,226	2,724	2,377	2,090	1,805	712	809
TOTAL ADDITIONAL EXPENDITURES	2,845	2,358	2,218	2,303	3,126	3,445	3,045	2,879	2,039	994	1,027
SURPLUS DEFICIT AFTER INTEREST	-212	-826	-866	-770	-1,171	-1,306	-702	-1,455	-944	-840	-1,278
SURPLUS DEFICIT AFTER GRANTS	1,261	616	474	773	333	84	635	-517	845	1,436	1,817
SURPLUS DEFICIT AFTER DEPRECIATION	-1,542	-1,709	-1,744	-1,646	-2,730	-3,507	-2,599	-3,122	-2,612	-1,440	-1,970
SURPLUS/DEFICIT AFTER GRANTS AND INTEREST	521	-104	-183	95	-334	-440	155	-939	708	1,324	1,700
SURPLUS/DEFICIT AFTER GRANTS, INTEREST AND DEPRECIATION	-1,550	-1,708	-1,719	-1,460	-2,560	-3,164	-2,222	-3,028	-1,097	612	890
SURPLUS/DEFICIT AFTER INTEREST AND DEPRECIATION	-2,283	-2,430	-2,401	-2,324	-3,397	-4,030	-3,079	-3,544	-2,749	-1,553	-2,087

ATTACHMENT 4: OPERATING DEFICITS: AGREED CEO/CFO QUESTIONNAIRE

1. Has tighter targeting reduced the average rent received per household and what is the extent of this effect?

   COMMENT

2. Have there been any significant changes in the average rate of income growth per household and hence the rate of growth or decline of net rents?

   COMMENT

3. Have changes in the mix of household types and incomes affected the ratio of persons to bedrooms, (or the number of smaller households being housed in larger dwellings), and the net rents being received?

   COMMENT

4. What proportion of your tenancies would have been unrebated around 1990/91?

   COMMENT

5. What is the proportion unrebated now?

   COMMENT

6. What proportion of your new lettings are priority and crisis allocations? What would it have been a decade ago?

   COMMENT

7. What changes have occurred in your rent setting and charging policies in the last decade?

   COMMENT

8. Have you been concentrating on restructuring and/or reducing your liabilities?

   COMMENT

9. What steps have been taken to pay down the principal owed on your existing debt?

   COMMENT

10. How have, and are you, financing your debt reduction strategy?

    COMMENT

11. To what extent are new grant funds being used to support existing operational deficits?

    COMMENT

12. What are the trends in rental delinquencies, rental arrears and evictions? To what extent has tighter targeting contributed to these outcomes over the past decade?

    COMMENT

13. Has the geographic distribution and structure of the property portfolio impacted on administration and maintenance costs?

    COMMENT

14. To what extent have maintenance backlogs and asset degradation contributed to the growth in maintenance expenditure or have you embarked on a major asset restoration program in the last ten years?

    COMMENT

15. If you have when do you think this program may be completed and how much more will cost?

    COMMENT

16. If you haven't do you believe you need to undertake a major asset restoration/restructure?

COMMENT

17. What do you think the costs of this program might be and how long do you think it might take?

COMMENT

18. What has happened to non planned maintenance expenditure and what are the causes of any significant expansion per household?

COMMENT

19. How would you rate the overall condition of your housing stock, excellent, good fair or poor?

COMMENT

20. Has your organisation transferred significant residential assets to community housing providers in the last decade?

COMMENT

21. If yes has this had any appreciable impact on maintenance and administration costs?

COMMENT

22. When compared to other cost components, are interest payments a substantial burden for STHAs?

COMMENT

23. How have rates payments to Local Authorities changed and how significant is this expenditure item?

COMMENT

24. What component of existing administration costs is being allocated to non-housing related support services for tenants and has tighter targeting contributed to this outcome?

COMMENT

25. Have there been any significant increases in salary and wage on-costs in the last decade? What are the main items contributing to these increases?

COMMENT

26. How is your problems different to other State And Territory housing authorities, (STHAs)?

COMMENT

27. Are existing operating deficits effectively preventing STHAs from making substantive additions to the supply of new social housing?

COMMENT

28. How fast are the operating deficits growing?

COMMENT

29. What policy options are available to policy makers to reverse the current real underlying trend to growing operating deficits?

COMMENT

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Western Australia Research Centre

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