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Social housing rental policy in Australia and overseas

INTERNATIONAL COMPARISONS REVEAL THAT AUSTRALIA'S PUBLIC HOUSING SYSTEM RECEIVES RELATIVELY LOW SUBSIDIES, UNDERMINING ITS FINANCIAL VIABILITY.

KEY POINTS

- Social housing organisations (SHOs) in Australia, like similar organisations in Canada, New Zealand and the United States, typically operate a dual rental system: a property rental system which determines the rent for each dwelling, and a household rental system which determines the rent for each household based predominantly upon household income. Household rent is the main mechanism through which affordability can be achieved in these countries because of the absence of any income subsidy to public housing tenants. In Australia, 88 per cent of all tenants are charged income-related or rebated rents.
- By contrast, most European SHOs operate a single property rental system. Some form of housing subsidy from central government directly to tenants is the mechanism through which affordability can be achieved in these countries.
- Australia does not compensate SHOs for housing low-income tenants, undermining their financial viability. In overseas finance systems, financial viability is ensured because SHOs charge:
  - a property rent based upon the ongoing costs of providing social housing (European countries such as the Netherlands, Sweden and the United Kingdom), or
  - a household rent and are paid a subsidy which meets the difference between the household rent and the property rent (Canada and New Zealand), or
  - a household rent and are paid a subsidy which meets the difference between household rent and cost benchmarks (United States).
- Achieving housing affordability for tenants and financial viability for SHOs requires increased subsidies per household ranging from $2 per week for a pensioner couple with a child to $129 per week for an unemployed couple with four children.

*This study, by **Sean McNelis** and **Professor Terry Burke** of the AHURI Swinburne-Monash Research Centre, presents the first comprehensive review of social housing rental systems in Australia and overseas. It describes and analyses rental systems in the social housing sector in Australia (public housing, community housing, affordable housing, Indigenous housing and aged persons' housing) and in seven overseas countries (New Zealand, the United States, Canada, the United Kingdom, Germany, Sweden and the Netherlands).*

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BACKGROUND

A key objective of social housing organisations has been to secure appropriate housing that is affordable for eligible tenants. However other considerations also come into play: should a rental policy ensure equitable treatment of social housing tenants? Are work incentives blunted by the way rents are set?

At the same time policy dictates that rents must be sufficient to sustain ongoing financial viability of social housing (Hall and Berry 2004).

METHODOLOGY

The methodology for this study involved a number of research methods, both qualitative and quantitative. These included:

- Reviewing Australian and overseas literature on rent setting policies and practices;
- Reviewing the history of rental policies and practices in Australian public housing;
- Undertaking a series of interviews with housing providers, a series of forums with housing practitioners and a small survey of public housing tenant organisations in Queensland. These sought to identify the strengths and weaknesses of current Australian rental policies and practices;
- Financial modelling of two rental policy options.

FINDINGS

What sorts of rental policies exist in Australia?

Rental policies in the social housing sector can be divided into two types: property rents and household rents. A Social Housing Organisation (SHO) can adopt one or both of these. Since the commencement of public housing in the early 1940s, tenants in public housing in Australia have paid either a property rent (determined on the basis of the quality and type of dwelling) or an income-related or rebated rent (based on the circumstances of the household).

Property rental policies determine a rent for each dwelling. There are four types:

- A historic cost-rent system where rents are determined according to three principles. First, aggregate rents meet the ongoing costs of providing social housing. Second, these ongoing costs are determined by reference to the historic costs of the existing dwellings, particularly the cost of capital for these dwellings (repayment of loans). Third, the burden of overall costs is distributed equitably among all dwellings;
- A current cost-rent system where rents are determined according to three principles. First, aggregate rents meet the ongoing costs of providing social housing. Second, these ongoing costs are determined by reference to the dwellings that will replace the existing ones and the capital required to do this (thus the current value of existing dwellings). Third, the burden of overall costs is distributed equitably among all dwellings;
- A market rent system where the rent is negotiated and agreed between a landlord and a tenant;
- A market-derived rent system where the rent is determined administratively as a proportion of what is happening in either the local private rental market or the housing market generally.

Household rental policies determine a rent according to the household occupying the dwelling. Three types of household rental policies can be distinguished:

- An income-related rental policy where rent is determined according to the income of the household, usually through some rent-to-income ratio such as 20, 25 or 30 per cent;
- A subsidy-related rental policy where a subsidy is provided to a household, and the household rent paid by the tenant is the difference between the property rent and the subsidy;
- A flat rental policy where a common rent is determined across a group of households or group of dwellings. It is based on particular characteristics of households (such as household type) or dwellings (such as size and/or type) and ignores any diversity of characteristics.

At 30 June 2004, 88 per cent of public housing tenants in Australia paid an income-related or rebated rent. Community housing organisations charge property and household rents – some with a mix of both, others just household rents. A key distinguishing feature of community housing (compared to public housing) is that tenants in this sector are eligible for Commonwealth Rent Assistance, which affects the rents they are able to charge.

Perceived strengths and weaknesses of Australian rental systems

Both social housing practitioners and tenants surveyed as part of this project saw the affordability tenants derive from income-related rents as a key strength of the Australian system. The equity between tenants, and the degree of certainty about housing costs were also considered positive features.

Amongst practitioners, the main weakness was seen to be the ongoing tension between affordability and financial viability, and the pressure on SHOs to trade off affordability for financial viability. There were concerns – especially amongst tenants – that any effort to increase rents or remove income-based rents might have adverse impacts on affordability. Practitioners argued that income based rents did not reflect location quality or amenity of dwellings and so there was potential for inequity between tenants.

Both tenants and practitioners also agreed that income-related rents were complex to administer and intrusive (involving income reviews and extensive documentation of a tenant's circumstances). The multiple objectives which SHOs seek to achieve through rental policies – including affordability, financial viability, equity, workplace disincentives administrative efficiency etc – make for an overly complicated system whereby uneven outcomes were more likely.

How does the Australian system of financing social housing compare internationally?

A rental policy not only determines a rent for an individual household, but also helps to finance the broader social housing system. A common framework for analysing, comparing and contrasting social housing finance systems both in Australia and overseas incorporates four core elements: rent, subsidies, ongoing costs and capital arrangements. Subsidies might be applied to meet ongoing or capital costs of SHOs, or they might be used to subsidise rents or incomes of tenants more directly.

In overseas finance systems, the financial viability of social housing organisations is ensured because:

- Tenants are charged a property rent based upon the ongoing costs of providing social housing, but tenants gain access to subsidies which compensate for the higher rents (eg European countries such as the Netherlands, Sweden and the United Kingdom), or
- SHOs are paid a subsidy that meets the difference between the household rent and the property rent (Canada and New Zealand), or
- SHOs are paid a subsidy that meets the difference between the household rent and cost benchmarks (United States).

A unique aspect of Australia's social housing finance system is that household rents have to serve two functions: providing housing at an affordable price, and ensuring the ongoing financial viability of social housing. In other countries, these two aspects of rental policy are dealt with in separate decisions (though they may be linked): the first through a housing subsidy from central government so that the tenant can pay the property rent, the second through the setting of property rents based upon the ongoing costs of providing social housing.

The Australian social housing finance system is unviable because, unlike others studied in this project, it relies predominantly upon household rents. The level of household rents (an income-related or rebated rent) depends upon the tenant's income. Because most public tenants are now income support recipients, this income is now largely determined by the level of these payments. As a result, many tenants are paying a rent that is below the ongoing costs of providing social housing.

Modelling improved financial viability and reducing complexity

Options for achieving financial viability and maintaining affordability

Key to reforming Australia's social housing finance system is to ensure it has a stable revenue base while ensuring low income households have access to affordable housing. Options to increase rental revenue might include increasing income support, directing subsidies to tenants or SHOs, increasing household or property rents, or changing allocations policy to favour tenants with higher incomes. It should be noted, however, that financial viability might also be improved through measures not involving rental policy – such as improving efficiencies in tenancy, property and asset management and housing acquisition.

Financial modelling undertaken as part of the project looked at the first of the options mentioned above – increasing income support. It indicated that Centrelink payments for most types of households must rise if tenants are to have sufficient income to achieve housing affordability and pay a rent that enables the lowest cost public housing provider (Victoria) to meet its basic operating costs. At December 2004, the required rise in Centrelink incomes ranged from $2 per week for a pensioner couple with a child to $129 per week for an unemployed couple with four children. These rises are based on conservative financial assumptions, and would yield the required subsidies to meet the total $341.6 million per year in operating and asset depreciation costs experienced by the Victorian public housing system and preserve affordability. Similar estimates were prepared for Community Housing

Organisations – the gaps involved here tend to be more modest due to present access to Commonwealth Rent Assistance.

Options for reducing administrative complexity and reducing workforce disincentives.

One of the options for reducing administrative complexity is to introduce a flat rental system – this rent is determined on the basis of the type of household or dwelling occupied rather than income, and so is less burdensome to administer (it does not need to be updated every 6 months) and has the potential also to improve work incentives since rent charged will not change when a tenant commences work.

Under a move to a 'midpoint household rent', some tenants would pay considerably more for their rent (for example a sole parent and three children could pay up to 20 per cent more or 14 per cent less depending on how much they are presently spending). This option would result in only marginally less rental revenue ($1.4 million or 1% less revenue) for the housing authority for this option (moving to other models such as a midpoint dwelling rent would improve revenue).

POLICY IMPLICATIONS

Of the multiple objectives of Australian social housing rental systems, affordability remains of prime importance to housing practitioners and tenants, but financial viability, administrative complexity and workforce disincentives are also concerns.

All international case studies provided evidence that improving financial viability of social housing need not come at the expense of housing affordability for tenants. The financing arrangements in place overseas had built affordability into their social housing system, by complementing their chosen system of rent with subsidies – either to renters or the social housing organisation – to ensure social housing was sustainable. The modelling in this project showed that providing greater income (such as through Centrelink payments) to public tenants would enable SHOs to increase rents and improve their financial viability, though the amount necessary would vary by household type. Other alternatives that could be modelled include direct subsidisation of SHOs.

Changes to improve the simplicity of the rental system – either by imposing flat rents on classes of persons or dwelling types, could reduce administrative complexity surrounding income based rents and confusion of tenants about what rent they pay. It could also potentially reduce workforce disincentives by removing rent increases consequent on earning more income. The modelling in the project showed this could be introduced with no adverse impact on rental revenue, though some tenants would be materially disadvantaged in the short term.

FURTHER INFORMATION

This bulletin is based on AHURI Project 50226, *Rental Systems in Australia.*

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

The following documents are available:

- Positioning Paper
- Final Report

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

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