POLICY EVIDENCE SUMMARY October 2020

Reforming Commonwealth Rent Assistance to better support low-income renters

Based on AHURI Final Report No. 342: Demand-side assistance in Australia's rental housing market: exploring reform options

What this research is about

This research examines possible cost-effective reforms of Commonwealth Rent Assistance (CRA) demand-side housing assistance that could improve housing outcomes for low-income renters.

The context of this research

Policy and academic studies have raised concerns regarding the efficacy of the CRA system in promoting housing affordability, effective targeting and tenure security among low-income private rental tenants.

CRA payments to low-income private renters are insufficient to achieve benchmark affordability because the real value of CRA has fallen well behind rent. There remains scope for improved targeting so that CRA entitlements more closely match the needs of different cohorts and accommodate the heterogeneity of housing markets across Australia.

Concern has also been raised that increases in a demand-side rental housing assistance like CRA would be shifted into higher rents, rather than being captured within renter households' budgets to ease their affordability pressures.

Who is entitled to CRA?

CRA is payable to households who are renting from private landlords, community housing providers or Indigenous housing organisations; paying more than a minimum rent threshold; and qualify for a social security payment such as Age Pension, Disability Support Pension, Newstart unemployment Allowance (now JobSeeker), along with families with dependent children who receive more than the base rate of Family Tax Benefit Part A.

Recipients receive CRA at the rate of 75 cents for every dollar of rent paid above certain thresholds, subject to certain maximum rates (sometimes referred to as caps), and are indexed to Consumer Price Index (CPI).

The lower thresholds and the maximum rates vary by household composition, but unlike most other countries' programs, not by location: the same thresholds and maximum rates apply Australia-wide.

CRA is paid directly to eligible private renters and is therefore classed as a demand-side subsidy.

The cost of CRA to Government

Government expenditure on CRA is substantial, amounting to $4.44 billion in 2018-19, though this has remained more or less constant in real terms in five years. The bulk of CRA expenditure is logged in New South Wales (NSW), Victoria and Queensland.

This reflects differences in states' populations, rather than housing costs. The average amount of CRA expenditure per income unit (i.e. people living in the same household who share resources) has remained roughly the same at around $3,000 to $3,500 over time and across states and territories.

The key findings

CRA effectiveness

This research shows that CRA simply does not go far enough in reducing housing stress for significant shares of low-income private renters. Before receiving CRA, low-income private renters who are eligible for CRA pay on average 36 cents per dollar of their gross income in rents. After receipt of CRA, this burden falls to 26 per cent.

However, over one-third (34%) of low-income CRA recipients still carry a net housing cost burden (i.e. a tenant's rent less CRA, expressed as a percentage of their income unit income) of more than 30 per cent after CRA is deducted from rents. Nearly one in five carry a net housing cost burden of over 40 per cent and nearly one in ten bear a severe housing cost burden of 50 per cent after deducting CRA from rents.

CRA appropriateness

Appropriateness refers to how well (or not) the current CRA structure matches the needs of the low-income clients it serves, i.e. CRA's targeting accuracy. Individuals who fall into the target-error groups are either in housing stress but not receiving CRA or receiving CRA while not in housing stress.

Around 246,000 or 18 per cent of low-income private renter income units pay rents that exceeds 30 per cent of their income but are ineligible for CRA. Another 330,000 or 23 per cent receive CRA despite paying rents below 30 per cent of their income. CRA's overall target error rate is thus quite high at 41 per cent.

Singles with no children make up 80 per cent of low-income private renter income units who are in housing stress but remain ineligible for CRA. This is a significant over-representation given singles with no children only make up 60 per cent of all low-income private renters. On the other hand, families with children are over-represented among the group who receive CRA while not in housing stress.

What are the impacts of reforming CRA for low-income private renters?

This research modelled three reforms:

1. Raising the CRA maximum rate by 30 per cent
2. Resetting the rent thresholds to address higher levels of housing stress among income units with no children
3. Changing the CRA eligibility criteria to reflect housing need, defined as low-income private renters paying rents in excess of 30 per cent of their income.

Raising the CRA maximum cap (reform 1) is the costliest reform, requiring additional annual expenditure of $1 billion, amounting to a total cost of $5.6 billion. This reform would generate the largest number of winners, amounting to 623,800 income units or 44 per cent of low-income private renters, albeit at the greatest cost. No low-income private renter would be worse off if the CRA maximum rate were raised. However, it is the costliest of the three reforms.

Reform 3 (changing CRA eligibility to reflect housing need) would achieve the greatest affordability improvements at the lowest cost; generating annual cost savings of $1.2 billion and reducing CRA expenditure to $3.4 billion. It would see a shift in the composition of people who benefit from CRA; reduce the number of income units whose rents fall below the moderate housing stress benchmark; and increase the number of income units whose rents exceed the benchmark. This would result in 246,000 beneficiaries from the reform and 330,300 who would see their position deteriorate as a result of the reform.

Reform 3 would also reduce the population of low-income private renter income units in housing stress by 371,200 or 44 per cent. This is a slightly greater reduction than the 342,200 (40%) decline achieved under reform 1 and the 303,700 (36%) decline achieved under reform 2. Such a reform would also reduce targeting error down to zero. The other two reforms have mild to no impact on target error rates.

Reforming the CRA eligibility rules to reflect housing need appears to draw beneficiaries from cities with significant housing cost pressures; low-income private renters in Melbourne and Sydney make up more than half of beneficiaries under this reform.

"This research shows that CRA simply does not go far enough in reducing housing stress for significant shares of low-income private renters."

Reforms not increasing ownership rates

Each reform would have negligible impact on the relative price of renting to owning for low-income renters. While reforms 1 and 2 will reduce the average net cost of renting, it is unlikely that they will assist in a move out of the private rental sector into home ownership. The small amount of annual savings is unlikely to generate sufficient funds for renters to bridge the deposit gap for home purchase.

What is the likely effect of changes in demand-side rental housing assistance on market rents?

This research's modelling detected that an increase in CRA is likely to be partially absorbed into higher rents in disadvantaged neighbourhoods. In moderately to severely disadvantaged areas, 6.6 per cent of any increase in CRA can be expected to be 'lost' to higher rents in this way. In severely disadvantaged areas, 32.4 per cent of CRA is absorbed by higher rents.

CRA is more likely be captured in higher rents in markets with relatively inelastic rental housing supply. This is because in the absence of an adequate supply response, rents rise. Capitalisation effects are thus more prominent in disadvantaged neighbourhoods because new housing supply is relatively inelastic in low-value housing market segments in Australia. This source of market failure contributes to the presence of capitalisation effects in disadvantaged areas.

Studies have shown that housing supply is, in fact, particularly inelastic in low-value segments of the market. Previous AHURI research (Ong, Phelps et al. 2019) found that the majority of new housing supply in Australia tends to be concentrated in mid-to-high price segments, with over 80 per cent of house approvals during the period 2005–06 to 2015–16 in the 6th to 9th house price deciles and the majority of new unit approvals being found to be in the high 8th to 10th deciles. Indeed, the bottom two unit price deciles accounted for under one per cent of new unit approvals in 2015–16.

International comparisons

In comparison with comparator countries (Germany, Ireland, the United Kingdom, the United States and New Zealand), Australia's CRA regime is distinctive in terms of being (a) restricted to certain categories of renters and generally excluding low waged employees; (b) regionally invariant; and (c) available by right, rather than cash limited.

Aspects of comparator country frameworks that could be considered in more detail include:

- extending eligibility to low waged workers
- calibrating and uprating standard payment rates or limits according to local market circumstances, such as rates tied to some percentile of the local rent distribution
- requiring recipient landlord compliance with defined minimum standards, as under the USA's Rent Choice Vouchers program
- regulating rents so that they may increase only in line with a declared rate.

What this research means for policy makers

Supply-side reforms

The modelled CRA reforms are likely to promote tenure security for the reform 'winners' to the extent that they alleviate the risk of evictions due to rent arrears. However, research findings indicate the reforms will have minimal impact on low-income private renters' ability to become home buyers.

Generally, since no conditions are imposed on landlords of recipient tenants, CRA fails to address concerns over service and property quality and tenure insecurity in Australia's lightly regulated private rental market. There remains scope for exploring reform options that target private landlords, such as the use of financial incentives to landlords to reduce rents or offer tenants greater control over the length of their leases.

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Demand-side rental housing assistance reform: impacts of three reform options

Reforming the CRA eligibility rules to reflect housing need would achieve the greatest housing affordability improvements at the lowest cost.

Constitutional barriers will need to be overcome to change the CRA eligibility rules to reflect housing need. CRA could be reformed as a Commonwealth-State and Territory program (with the Australian Government making grants to state and territory governments to pay Rent Assistance to eligible persons), or an expansion of the Australian Government's constitutional powers could be considered to make provision for housing benefits.

Policy concerns

When CRA is shifted into higher market rents, this affects not only CRA recipients but also non-CRA eligible tenants living in affected areas. For instance, some low-income workers living in disadvantaged areas might not meet CRA eligibility requirements, but will suffer a rise in the rents they face as a result of the capitalisation effects of CRA into market rents.

CRA recipients living in disadvantaged areas will also benefit less from increases in CRA entitlements than those not living in disadvantaged areas. When facing a rise in rents, tenants residing in disadvantaged areas, who tend to have lower average incomes, are less able to respond by exiting the rental sector into home ownership due to credit constraints.

Methodology

This research combined an international literature review, findings from the Household, Income and Labour Dynamics in Australia (HILDA) Survey and a workshop with key stakeholders.

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To cite the AHURI research, please refer to:

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