Financing affordable housing: a third way for housing assistance

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1. Introduction

The quest for new ways to finance affordable housing has been a recurring theme of public policy debates and research into housing over the last decade at least.[1] The hegemony of market-based approaches to social policy from the mid 1980s put an end to 'Whitlamite' approaches that sought solutions in tax transfers and government delivery of services. As national and state economies became more integrated into international economies, and fell under the watchful eye of overseas credit raters, their governments faced more fiscal and structural constraints on what they might do – even if they were

[1] The terms affordable housing and housing affordability are often used interchangeably, but some writers distinguish a nuance between them – though both of the usages share a common basis in linking housing costs to income.
Housing affordability puts the focus on the *consumer*. Is their housing cost reasonable within their budget: are they paying less than 30% of their income on rent (or mortgage-repayments)?
Affordable housing puts the focus on the *dwelling*. Is the rent in the bottom 20% of rent levels (Cox and Miers 1998, p.7)? Or, is the rent set at a level so that a renter would be paying less than 30% of their income on rent? Yates and Wulff (1999, p.8) use a rent level of $100 a week (in $ 1996) as the indicator of this. 'It is the only stock which is remotely affordable for the 20 per cent of households in the private rental market with incomes below $300 per week.'
Affordable housing is sometimes called 'low-cost housing', where cost refers to the cost to the consumer, that is, the price they pay for the good (not to the cost of construction or to the owner's/provider's cost of supply).
Some writers use another term, 'low-income housing': this refers to housing that is affordable to *income units* with the lowest 40% of pre-tax incomes (National Housing Strategy 1991).
An important NSW report used 'lower-income' *households* to refer to households with the lowest 50% pre-tax incomes (Ministerial Task Force on Affordable Housing 1998).
The different benchmarks and measures are discussed in Wulff and Yates (2001, pp.81-86).

disposed to Keynesian or 'traditional' social-democratic approaches to macroeconomic management. Public housing estates do not capture a popular imagination as an ideal course for addressing need, and state housing authorities are reduced to being custodians of an aging and sometimes inappropriate product. The vicissitudes of the Commonwealth-State Housing Agreement since the mid 1990s reflect the lack of consensus among policy-makers about the role of government in the financing and provision of affordable housing.

Behind the insecurities of policy choice there remains a constant: a growing crisis in housing affordability for low-income Australians. This has been documented in research by the Commonwealth, such as the National Housing Strategy in the early 1990s, by state governments, such as the NSW Ministerial Taskforce on Affordable Housing in the late 1990s, and by academic researchers and nongovernment organizations. Governments have not been inactive in the face of this growing crisis: they have directed resources to addressing it. We have the Commonwealth's rent assistance program and the states and territories' social housing programs, as well as more ad-hoc, home purchase assistance schemes. Moreover, there are now also innovative tools like use of development levies by local governments. However, a skeptic might well question whether the extent of the solutions deployed matches the extent of need displayed. This is part of the reason there has been so much research and policy interest in new approaches to financing affordable housing, in recent years.

This paper focuses on the work of the Affordable Housing National Research Consortium, which commissioned research over 2000-2001, and released a series of research reports and its own conclusions in September 2001. The reasons for focusing on the work of the Consortium are four. The Consortium engaged *experts* to scope the issues and systematically work through potential solutions. The Consortium brought together *key players* from the housing industry. The Consortium focused in *practicalities* not ideologies. Its work therefore provides some *hope* for a breakthrough in the policy impasse that has bogged down supply-side versus demand-side debates in the 1980s and 1990s.

2. The housing movement's interest

Nonprofit government advocates for and providers of affordable housing have a history of research and advocacy about financing affordable housing.

At the national level, the National Community Housing Forum, which includes the Community Housing Federation of Australia, commissioned a series of reports on financing community housing (George Porter 1998; Larkin and Lawson 1998; Porter 2000).

In Victoria, Ecumenical Housing has been developing models for financing community housing, and presented a report at the 2001 national housing conference in Brisbane (McNelis, Hayward and Bisset 2001).[2] Their focus is on attracting small-scale retail investors, not institutional investors. They modeled 3 mechanisms:

- a headleasing arrangement (with market rents charged): they estimated that a headleasor (such as a retail investor) would get a net income return of 3.38% before finance costs and taxation: they thought this might be insufficient to attract private investors if capital growth is low, but possibly adequate if capital growth is high;
- debt-financing: they found that a community housing organization charging market-derived rents could borrow up to 40% of funds and remain financially viable;
- purchase of a house and renting out to tenants whose only source of income is a social security payment, and where the tenant's rent covers all operating costs and depreciation: they established house prices for a range of bedroom sized dwellings, and found that few, if any, appropriate dwellings could be purchased within those prices in Melbourne.

They concluded that a sufficiently attractive financial vehicle to attract retail investors would need significant subsidies in the form of tax breaks to investors, capital gains to community housing organizations, new forms of ongoing subsidies, or a commitment by government to underwriter a community housing program such that risks to private investors are reduced to zero (p.8).

In New South Wales, Shelter's research and advocacy has focused on town planning controls to mandate private sector financing and/or provision of affordable housing.

Cox and Miers (1998) focused on 2 types of planning mechanisms relevant for supply of low cost housing:

- those that were about retention of affordable housing, for example, State Environmental Planning Policy 10, and developer contributions under section 94 of the Environmental Planning and Assessment Act;[3] and

[2] The 1st and 3rd of this paper's authors are with Ecumenical Housing in Victoria.
[3] A state environmental planning policy is a planning tool of the state government that provides policies and processes for regulating developments affecting all or part of the state (rather than to one local government area or locality); SEPP10 deals with local government processes for dealing with development applications
This footnote continues on the next page.

- those that were about promotion of affordable housing, for example, linkage programs, inclusionary zoning, and development agreements.[4] They noted that linkage programs had had limited application in Australia and had a doubtful status in NSW law at the time: 'The complexity of the planning arguments for linkage makes Section 94, as it currently stands, a doubtful mechanism through which to apply linkage fees.' (p.23) In the case of inclusionary zoning, there was a NSW model in the City West Affordable Housing Program in Sydney.

That report noted a number of tax expenditure and outlays programs by state and local governments in New South Wales to help retain and promote low cost housing.[5] The state government has tax expenditure (revenue foregone) programs in land taxation: Owners of non-owner occupied properties providing low cost accommodation are exempt from land tax, in 2 situations: (1) where the property is a boarding house that meet certain conditions; and (ii) where the property provides low-rent accommodation in inner Sydney (5 km radius of Sydney GPO). The state government also has an outlays program, the boarding house financial assistance program: this gives funds to owners and operators of boarding houses to undertake essential fire-upgrading work (pp.32-33). Some local governments have tax expenditure programs; for example, Waverley council gives property rate rebates for boarding houses (p.33).

Shelter New South Wales also ran a seminar with the NSW Council of Social Service, on 1 September 2000, that focused on private sector financing of affordable housing through the planning system (Roden and Kirkland 2000). The center of this discussion was the *Environmental Planning and Assessment Amendment Act 2000* (NSW), which validated inclusionary zoning instruments in City West and Green Square and linkage programs in St Leonards, North Sydney, Randwick and Waverley (though the Act put a 2-year sunset clause on those validations). The NSW government was preparing a State Environmental Planning Policy that would provide the basis for linkage programs by local government councils: it would enable mandatory contributions from developers where there was a reduction in or new demand for affordable housing.

The Association to Resource Cooperative Housing (ARCH) has commissioned the Australian Centre for Cooperative Research and Development to suggest, among other matters, means by which the cooperative housing sector could be sustained, including financing (Fowkes 2001).

affecting the supply of 'low cost rental housing' in Sydney, Newcastle and Wollongong.
The Environmental Planning and Assessment Act allows local government councils to impose conditions on land/property developers when those developers apply to the council for permission to undertake new development ('development consent'). Section 94 of the Act establishes processes by which councils can require monetary contributions from developers to enable the council to undertake activity that is consequential to the new development, such as provide more community services.

[4] A linkage program is one that establishes a cause-effect relationship between a development and a need for goods and services, such as greater demand for housing. Inclusionary zoning is where a state or local government planning tool enables a council to provide incentives to developers or to impose conditions on developers to provide a desired use in a new development (such as affordable housing). A development agreement is where the local government and developer negotiate a package of proposals around a new development (such as inclusion of affordable housing units).

[5] A tax expenditure is where a government foregoes collecting revenue through taxation, for example, by allowing 'negative gearing' of rental housing properties; it is a 'virtual expenditure' not an actual expenditure. An outlay is where there is 'real' amount of money allocated to a particular program, for example, grant funding to tenancy advocacy services.

Individual community sector agencies have been developing their own financing models, too. For example, Berry and Hall (2001, p.107) cite an initiative of Centrecare in 1999. Centrecare approached NSW Landcom with a proposed model for affordable housing. The model was based on a joint venture between private investors and income tax-exempt public benevolent institutions. Landcom commissioned a feasibility analysis of this approach. From the data available to them, Berry and Hall summarized the model as one depending on a private investor contributing part of the initial investment in the form of a 'donation' that is immediately deductible against other taxable income, with the remainder committed to generate an investment income flow over an agreed period. The dividend or interest returns are, in turn, donated back to the public benevolent institutions and are tax-deductible in the year of receipt.

3. Affordable Housing National Research Consortium

The major research and policy development initiative on financing affordable housing over 2000-2001 was that undertaken by the Affordable Housing National Research Consortium.

The Affordable Housing National Research Consortium was an ad hoc group comprising the Housing Industry Association, Australian Council of Social Service, Real Estate Institute of Australia, Australian Council of Trade Unions, National Community Housing Forum, Urban Development Institute of Australia, Property Council of Australia, Royal Australian Institute of Architects, Master Builders Australia, and Royal Australian Planning Institute.

The principal consultants were the Australian Housing and Urban Research Institute and Allen Consulting.

This section summarizes the research reports commissioned by the Consortium. The reports are downloadable from the Consortium's website, <www.consortium.asn.au>.

3.1 First report

Berry and Hall (2001) scoped the extent of housing stress in Australia. Their focus was on private tenants, because research by the National Housing Strategy (early 1990s) and others had found very low proportions of outright homeowners and public tenants to be paying more than 30% of their incomes on housing. They cite ABS data from 1999 that indicated the relative proportions of people in different tenures paying more than 30% of their incomes on housing costs as 4.9% for outright home owners, 27.9% for purchasing owners, 9.9% for public tenants and 54.7% for private renters (p.51).

They found that, in June 2000, no private tenants in the bottom 40% of incomes could affordably buy any dwelling in any metropolitan locations in Sydney. They concluded (p.53):

> … low income private renter households have very, very limited affordable housing choices; both by location and dwelling type. Moreover, where a small degree of choice appears to exist – viz. renting a one bedroom unit on the fringe – this ignores the question of *appropriateness*. Clearly this only represents a choice for small households.

They predicted that, if the rate of growth in stressed households continues, the number of households in that situation would double in the next 15 years (p.13).

Some 227,480 low-income private-tenant households in metropolitan cities were experiencing housing stress in 1996. The estimated total cost of constructing new dwellings to meet their needs would be around $27 billion (p.55). Berry and Hall suggest there is a need for extra government funding to improve affordability (p.73; their emphasis).

> However, in order to stretch available housing subsidy funds further, it would be wise for government to consider ways of leveraging some of these public funds with private funds, *as well as expanding rent assistance through the income support system and capital provision through the CSHA*. In the light of the various financial and operating risks facing housing authorities, a mixed strategy of delivering the necessary expanding pool of housing assistance through these three main channels – RA, CSHA and leveraged private investment – is most likely to maximize the overall effectiveness of policy on housing affordability and minimise the long term subsidy costs per household assisted.

They suggested that the private rental market would have increasing demands placed on it because of increasing affordability problems for aspiring low-moderate income homeowners, and because of social housing agencies being unable to significantly expand their stock (p.80). The question of financing social housing is not a new one. Berry and Hall summarize the findings of 9 reports on financing social housing in Australia that were undertaken over 1991-2000. See
Box 1.[6]

Box 1: Recent literature on financing social housing

Brian Elton and Associates, *The supply-side of the private rental market*, National Housing Strategy, Background Paper 2, Canberra, 1991; Caversham Partners Limited, Malleson Stephen Jaques, TPFandC, Alternative ways of raising finance for social rented housing, Report to the Commonwealth Department of Health, Housing and Family Services, Canberra, 1991; J.R. Hall and Associates, G. Glazebrook and Associates and Residex Pty Limited, National Youth Housing Strategy: Financing youth housing, Draft Discussion Report, 2 vols., report to National Youth Housing Strategy, Canberra, 1995; East Perth Redevelopment Authority, Affordable housing proposal, EPRA, Perth, 1995; George Porter, *Financing community housing: options for private sector involvement – a review of existing research*, Brian Elton and Associates, National Community Housing Forum, Sydney, 1998; Ecumenical Housing Inc., Private funding models for church community housing, National Churches Community Housing Network, Melbourne, 1999; M. Berry, J. Flood, J. Fisher and M. Lindfield, Development of investment models aimed at encouraging institutional investment in rental housing, report to the Department of Family and Community Services, Australian Housing and Urban Research Institute, Melbourne, 1999; George Porter, Private financing and community housing: recent initiatives, Brian Elton and Associates, Sydney, 2000; Landcom, Report on Centrecare public benevolent institution (PBI) model for affordable Housing, Sydney, 2000.

Source: Berry and Hall (2001, pp.99-107).

Australia has had little investment in affordable housing by institutional investors, compared with some other Western societies. The ownership of most private rental housing is held by small 'retail investors'. There are barriers to private sector and nongovernment finance for affordable housing. Those are (pp.109-110):

- low returns. Gross rental yields currently average between 5-7% and a high proportion of individual investors reap negative or zero returns. Investment in the

[6] This list does not include a report prepared for the Victorian Department of Human Services on a number of matters for renewal of social housing programs, including their financing, which was prepared by Hal Bisset in November 2000 (Bisset 2000).

current market environment will not return the after-tax return on equity (in particular) that institutional investors require for this class of investment.

- high risks. These include the revenue risks associated with uncertain vacancy rates and maintenance costs; uncertainty over future capital gains; a perceived prevalence of poor property and tenancy management practices; and possible impacts of future changes in government policy (such as taxation treatment of depreciation, capital gains and property values).

- high management costs. There are limited opportunities or economies of scope and scale in the private rental housing industry because of the small-scale nature of the industry.

- illiquidity of property investments.

- poor market information. The secondary market for dwellings is highly segmented and unevenly monitored: this makes it harder for investors to accurately price risk.

- no track record. There are not many examples of successful models. One of these models is the Public Equity Partnership joint ventures between the NSW Department of Housing and the AMP Society, in which the Society bought public housing dwellings from the Department and then leased them back. However, the costs and complexity of the venture means it is *unlikely* to be followed elsewhere (p.87).

Berry and Hall conclude that these factors, taken together, ensure that the rental stream required to meet the risk-adjusted rate of return required by institutional investors is significantly higher than ruling market rents at the moment. This means that the primary aim of any policy designed to encourage institutional involvement should be to close the *rent yield gap* (p.110).

They identify a number of strategies that could be used to close the rent yield gap – strategies that could be used in combinations. Those strategies are (pp.111-114):

- government subsidies: cash to tenants, tax subsidies to investors, mandates on developers (inclusionary zoning, linkage fees), provision of government-owned land;

- efficiencies in housing management systems and land development and construction regulatory systems, and innovative financial products;

- risk reduction through government guarantees, insurance, and/or improved market data on performance;

- enhancement of the residual value of the asset (capital gain), by diversifying investment across dwelling types and locations and over 2 or more property cycles;

- government prescription (such as a prescribed assets ratio on superannuation funds [or threat to introduce such prescriptions], tax surcharge).

In short, the first report set the scene, by describing the extent of housing stress in Australia; it pointed to the lack of institutional financial investment in private rental housing as a key deficiency in the national response to the problem; and it laid out some broad strategies to address that deficiency.

3.2 Second report

The 2nd in a series of 4 reports commissioned by the Affordable Housing National Research Consortium (Hall, Berry and Carter 2001) opened with a pessimistic assessment of the capacity or willingness of Commonwealth and state governments to contribute sufficient taxation revenues to meet the need for housing assistance identified in the 1st report. Those two spheres of government contribute to addressing the need through outlays programs, the rent assistance program delivered by the Commonwealth's Centrelink, and capital construction and maintenance programs delivered by state housing authorities, underpinned by the Commonwealth-State Housing Agreement (CSHA).

They argued that there is no optimal cost-effective delivery mechanism for housing assistance. Each of the 4 major delivery mechanisms or models has risks. Those models are capital provision of dwellings, subsidized home loan schemes, subsidized share equity schemes, and rent assistance. Each of those models is 'the most effective option depending on the state of the economy and, especially, of housing and finance markets.' (p.37)

Putting this assessment together with the lack of institutional investment in rental housing identified in the 1st report, they proposed: 'The only practicable way in which the required expansion of affordable housing might be achieved is by some form of (gearing) Commonwealth and State housing assistance funds to private sector finance.' (p.4)

They presented this course as complementary with, not an alternative to, capital provision of dwellings and rent assistance. Indeed, they argued that government subsidies needed to be increased across all three approaches. However, this increased subsidy would minimize long-term subsidy costs overall, because mixing subsidy delivery would enable efficient management of various systematic risks associated with each approach (p.4).

They describe the most common approach to a gearing option as one where the housing options are sold at the end of, say, a 25 year period, with part of the proceeds used to repatriate any principal owed on the debt, or to provide equity to a private owner. The report established a short-list of policy options that would achieve the gearing option in the most effective way.

They identified 7 main private sector financing options. Those were (p.41):

- 3 debt options –
  at a floating rate of interest,
  at a fixed rate of interest,
  at a real rate of interest;

- 3 equity options –
  a stock exchange listed company (attracting wholesale and retail funds),
  a retail property trust,
  a direct equity investment;

- 1 that was a mixture of both debt and equity financing, namely a stock exchange listed company supplemented by substantial debt-financing (at either a floating, fixed or real rate of interest).

On balance there will be very few circumstances where private sector financing will be cheaper than issuing government debt (p.43).

Based on interviews with a number of investment managers, they reported that Australian institutions were particularly keen to develop new investment opportunities at the low-risk/low-return end of the spectrum. They concluded that the institutions might be responsive to housing-related semi-debt investment instruments and vehicles that provide steady, secure returns delivered through income and/or capital guarantees by government (p.49).

They identified 121 policy packages or options and narrowed these down to a short-list of 11 preferred policy options. Those options were (pp.51-53):

- *capital provision* of dwellings, that would be government-managed, with the Commonwealth subsidizing the cost of finance by allowing investors an interest income tax exemption (a ‘tax expenditure’);

- *capital provision* by private firms through a new Commonwealth outlays program only available for privately-owned dwellings, with the Commonwealth assisting in the form of cash outlays, rather than revenue foregone;

- *capital provision* of dwellings, that would be government-managed, financed by a stock exchange listed company to which the Commonwealth would subscribe 20%;

- *capital provision* of dwelling, that would be government-managed, financed by the Commonwealth prescribing designated financial institutions (such as superannuation funds) to hold assets in ownership of rental dwellings managed by social housing providers;

- *home loans*, through a new outlays-based subsidy program directed at subsidizing mortgage repayments and supporting credit and other risks on state-developed and –managed, but privately-funded, home loan programs, which would be financed by a floating rate debt instrument or a fixed rate debt instrument (2 options);

- *home loans*, through provision of income-tax concessions by the Commonwealth on interest received for loan funds raised to support a program directed at subsidizing repayments and supporting credit and other risks on state-developed and –managed, but privately-funded, home loan programs; this would allow house purchasers to pay less than market interest rates for their home loans, since the interest would be tax-exempt to the private lenders (2 options);

- *shared equity*, with a state housing authority funding its share of the dwelling by selling real rate debt, incorporating a Commonwealth tax concession to the private lender; the low-income purchaser would take out a fixed-rate mortgage loan to finance the remaining equity share;

- *direct assistance*, through the Commonwealth providing a tax exemption on net rents received by private suppliers of low-priced housing to households in housing related stress;

- *direct assistance*, through a new rent assistance program targeted to non-pensioner and –beneficiary households experiencing housing stress, using a prescribed assets ratio approach.

3.3 Third report

The Affordable Housing National Research Consortium considered the 2nd report it commissioned (Hall, Berry and Carter 2001) and chose 4 ‘broadly feasible policy approaches’. These were considered in a 3rd commissioned report (Allen Consulting Group 2001).

This report affirmed some of the somber assessments made in the 1st and 2nd reports. Specifically, that – either individually or together – rent assistance and public housing are not providing an effective response to Australia’s affordability problem.

In relation to rent assistance, the report noted that, even after the receipt of rent assistance, 40% of recipients (some 385,000 households) still suffer housing stress (on a 30% affordability benchmark). This does not include households in need who are not eligible for rent assistance. Assuming there are another 115,000 households facing housing stress but ineligible for rent assistance, there would be some 500,000 households in housing stress. If it is assumed that each of these households need an average of $25 a week in additional support, addressing this need through rent assistance would cost the Commonwealth government an additional $910 million a year (p.34).

In relation to public housing, there is an estimated shortfall of 150,000 affordable rental dwellings in Australia. To meet this shortfall with public housing would cost $15 billion, based on a construction cost of $100,000 a dwelling (p.33).

Thus, the effectiveness of both the rent assistance and public housing programs to deal with housing stress will not be improved without a significant injection of funds into both of them. However, such a significant injection of funds into both or either of those programs was ‘… unlikely in the current fiscal climate nor any time in the near future.’ (p.32) Moreover, neither of those two programs addresses the lack of institutional investment in residential rental housing.

The report did not argue that governments should not be asked to *not* spend on housing assistance. On the contrary, they argued that governments will need to spend more. Doing nothing would not save money because governments will have (non-housing) costs in dealing with the negative spillover effects of poor housing such as poor health, lower educational attainment, and higher levels of crime.

Rather, it proposed consideration of alternative means of financing, involving a new public/private partnership. The key policy proposal underpinning the options considered … is that the government can use a relatively small amount of money to leverage a potentially large volume of institutional funds into investment in affordable housing. The result is that governments could achieve a significant reduction in housing stress at a fraction of the cost of addressing the issue through the existing housing support measures of public housing and rent assistance. (p.18)

They proposed 6 criteria for assessing alternative means of financing: efficiency, equity and fairness, incidence and size of risk, overall effectiveness, budgetary implications, and political feasibility (p.21; detail on pp.21-38).

And they proposed 3 key objectives that any policy option needed to achieve (p.30):

- an increase in the supply of affordable housing, to address the significant shortage of low-cost rental housing and improve the efficiency of the rental market;

- a reduction in housing stress, through improved housing affordability, leading to more equitable assistance arrangements; and

- a reduction in the barriers (in particular, risk barriers) to institutional investment in residential rental housing.

The report evaluated 3 supply-side responses and 1 demand-side option. Those options were (pp.46-62):

- 1st possible supply-side response: a Commonwealth subsidy program to encourage private investment in affordable housing. This approach involved the Commonwealth or state governments raising finance for affordable housing through the issue of a bond with a 'guaranteed minimum' after-tax return. The funds would then be distributed to social housing providers for the construction of affordable rental dwellings. A Commonwealth subsidy would be provided to close the gap between the guaranteed minimum return and the expected net rental yields, taking into account the proceeds from the sale of the dwellings at the end of the transaction. The subsidy can be provided either through a tax concession or through an expenditure program. See Box 2 on page 12 for a fuller description of this option.

- 2nd possible supply-side response: establishment of a stock exchange-listed company as a vehicle for private sector investment in affordable housing. The company would invest in affordable housing with funds drawn from 3 sources: 20% Commonwealth government equity, 30% private shareholder equity, and 50% borrowed funds. The Commonwealth equity in the company would be in the form of 'subordinated' facility that could be drawn on to meet investors' returns up to a predetermined level necessary to encourage private investment.

- 3rd possible supply-side response: a prescribed ratio for affordable investment assets. The Commonwealth would mandate that a minimum proportion of the assets of designated financial institution (notably superannuation funds) be held in ownership of rental dwellings managed by social housing authorities.

- a demand-side response: assisted home loans. State and territory governments would issue bonds in which institutions and others could invest, and they would use the funds to provide subsidized home loans to low-income earners at market rates. There would also be a new Commonwealth outlays program to further subsidize repayments, if necessary, to remove households from housing stress.

Box 2: Option 1 evaluated in the 3rd report

The Commonwealth would provide a subsidy to the states and territories on the condition that it is used to leverage private sector investment into affordable housing …
One approach would be for the Commonwealth or state governments to raise funds for investment in affordable housing through the issue of a bond with a ‘guaranteed minimum’ after tax return. The Commonwealth subsidy would be used to make up the difference between the guaranteed minimum return and the net rental yield from the properties over the life of the bonds, say, 25 years. The funds raised would be distributed to state housing authorities or other eligible housing providers (e.g. community or other private housing providers) on the condition that they are used for the construction of affordable rental dwellings ... The dwellings would be managed by state housing authorities or other eligible providers. The target households would be those in the lowest 40 percent of incomes.
The sale of the dwellings at the end of the period would provide the funds for the repayment of the bond principle or equity owned by private investors. If they wished, state housing authorities could retain the assets, for example, to make additions to their public housing stock, by repaying the bond issuer an amount equivalent to the estimated sale value of the dwellings. The Commonwealth could issue bonds for about 0.5 percent less than the states, which would lower the cost of the scheme. If the Commonwealth issued the bonds, the states would be required to repay the principal and interest, less the subsidy amount.
Another approach would be for states to use the Commonwealth subsidy to directly leverage the construction of affordable dwellings by private sector developers. For example, property developers could be subsidised to include affordable dwellings in proposed residential housing developments. With this variant, government and/or community agencies could be given responsibility for identifying eligible clients to ensure that the dwellings were targeted to those in need.
A key issue is how the Commonwealth subsidy is provided. Under the bond issue approach the Commonwealth could use a tax concession or an outlays program. For example, the Commonwealth could provide an income/company tax concession on the annual return on the bond. The bonds could then be issued at a below-market rate of return reflecting the tax-exempt nature of the income earned from them. The objective would be to bring the after-tax return on the bonds into closer alignment with the expected rental return generated from the dwellings while still giving investors an after-tax return comparable with similar debt instruments.
The other option would be for the Commonwealth to fund the return gap out of consolidated revenue. In other words, the bonds would be issued at market rates of return with normal taxes applying. A new outlays program would be established to subsidise the gap between the bond yield and the net rental returns from the dwellings, and after taking into account the proceeds from the sale of the dwellings at the end of the transaction.
The level of support and, hence, ability to leverage more private sector investment, could be increased if support was provided by both levels of government. The Commonwealth could provide assistance on the condition it was matched in whole or in part by state governments. This would allow greater flexibility in methods of support if the Commonwealth was to choose to use a tax concession approach. The reason is that the tax concession method is restricted to the bond approach and does not lend itself to the approach of directly subsidising affordable housing in private sector residential developments.

Source: Allen Consulting Group (2001, pp.46-47).

The report’s authors applied a ‘balanced scoreboard approach’ to assess the options. This involved using quantitative and qualitative factors to assess each option. The authors rated each option against 6 criteria and gave it a score of 0-6 on each criterion. The criteria were: efficiency, equity, risk, effectiveness, budgetary impact, and political feasibility. Thus, the highest score that any option could get was 36, and the lowest was 0.

This is how each option scored.

- The 1st possible supply-side response involved a direct government subsidy to institutional investors. Governments would issue a bond with a 'guaranteed minimum' after-tax return, using a Commonwealth subsidy to make up the difference between the guaranteed minimum return and the net rental yield from the properties over the life of the bonds (say 25 years); the Commonwealth could issue bonds for about 0.5% less than the states could. A variant on the model involved the states using a Commonwealth subsidy to get private developers to include affordable dwellings in housing developments. The option scored well against the key criteria of efficiency, equity and effectiveness; it did not score badly in relation to risk and political feasibility; it was not as bad as some options in terms of the level of expenditure and budgetary risk involved. Its overall score was 26-27/36[7].

- The 2nd possible supply-side response involved establishment of a stock exchange-listed company that invests in affordable housing, with its funds drawn from Commonwealth government equity, private shareholder equity and borrowed funds. The option scored well on efficiency and equity grounds, but poorly on risk, resulting in a moderately good outcome on overall effectiveness; it fell short on budgetary implications and political feasibility. Its overall score was 19/36.

- The 3rd possible supply-side response was a prescribed assets ratio for assets of designated financial institutions to be held in social housing. This option performed well on efficiency and equity and overall effectiveness and budgetary impact, but scored poorly on risk and political feasibility. Its overall score was 21/36.

- The demand-side response was a home loan assistance schemes managed by the states and territories. This option performed poorly on efficiency and equity grounds, had a neutral score on risk, and scored poorly on overall effectiveness. It had a marginally 'negative' score on budget impacts, and performed poorly on political feasibility. Its overall score was 7/36.

The supply-side options were preferred to the one demand-side response because they directly addressed the shortage in affordable housing (p.65), which was one of the 3 policy objectives (see page 11 of this report, above). Of the 3 supply-side options, option 1 – a *housing bond* – scored the highest.

Schemes similar to option 1 have been suggested before, but the authors proposed it be implemented in a flexible way, for example (pp.66-67):

- the bonds could be issued by either the Commonwealth or state/territory governments;

- the subsidy could be provided by either the Commonwealth or state governments or both;

[7] The two possible scores depend on whether the subsidy takes the form of a tax concession (which scores 26) or an outlay (which scores 27).

- the funds could be provided to state housing authorities as well as other approved government, community or private sectors, or provided directly to residential property developers;
- the bond could have various characteristics in relation to duration, price basis, etc.;
- the subsidy could be delivered through a tax concession or an outlays program.

The report's authors suggested that interested parties (that is, implicitly, the Commonwealth and state/territory governments) consider precise specification of the scheme depending on their willingness and ability to bear the risks and costs and to manage it (p.67).

3.4 Fourth report

The 4th report (Hall 2001) commissioned by the Affordable Housing National Research Consortium provided cost estimates for the preferred option for an affordable housing bond that was identified in the Consortium's 3rd report (Allen Consulting Group 2001).

The report focuses on the subsidy costs that would be needed from Commonwealth and state governments. It provides a simulation model to calculate the commencing amount of funds (subsidy support) that should be put on deposit to pay a required rental subsidy for low- to moderate-income tenants and for capital shortfalls on debt repayments, (if any), for the term of the transaction. The modeling assumes dwellings required to house low- to moderate-income tenants are initially purchased from the proceeds of a bond issuance, and that as time goes on the proceeds of sales of the dwellings are used to repatriate the principal owed on the bonds and to provide for any operational shortfalls. (p.10)

It found that, under a 'Base Case', a national program of $100 million would produce a gross cost to the Commonwealth of $22 million and net cost after direct tax receipts of $8.9 million for the total term of all State transactions. A program of $2 billion capital would have a gross cost of $440 million (once off), and a net cost of $180 million. This would provide accommodation for 14,900 assisted tenant households (p.24).

3.5 Final report

The Consortium's final report (Affordable Housing National Research Consortium 2001) brings together the findings from the 4 reports commissioned by the Consortium (Berry and Hall 2001; Hall, Berry and Carter 2001; Allen Consulting Group 2001; Hall 2001) and also presents the Consortium's own views.

The report summarizes the research findings and analysis from the earlier reports, and also has an advocacy flavor.

The Consortium took as its starting the point the existing suite of Commonwealth housing assistance policies, 'which play an indispensable role in helping to address the problem'. However it declares them to be insufficient to overcome housing stress and argues that a *new strand* is needed: one which targets the supply side of the housing market, and which emphasizes a finding solution to close the investment gap in low-cost housing (p.3).

The Consortium repeated its support for the preferred option that emerged from the 3rd report (Allen Consulting Group 2001). (See Box 2 on page 12 of this report.) This is a supply-side response: it is about funds for construction of new affordable dwellings. Every $1 billion dollars raised by such a scheme would have a gross cost to the Commonwealth of $220 million (the net cost is $90 million, after taking into account tax receipts), and would assist 7,450 tenant households. For every 1 dollar of government subsidy provided in this way, 3 or 4 private sector dollars would flow into expanding the stock of affordable housing (p.32).

The Consortium argued that this leverage enabled a ‘convincing attack’ on the looming crisis in (lack of) affordable housing.

4. The 'politics' of financing affordable housing

The fiscal challenges for housing assistance programs in face of housing need are not new. State housing authorities have had a declining capacity to meet the demands on their waiting lists over the last decade, at the same time as public housing has become more and more stigmatized. Cashed-out forms of assistance became popular in the late 1980s and early 1990s during the heyday of 'neo-liberal' dominance of social policy in late capitalist societies (Winnick 1995, Orlebeke 2000). But they did not displace provision of in-kind support, in Australia (Yates 1997). While the rent assistance program is growing, it is nevertheless rationed, through eligibility conditions and a low monetary subsidy.

Nongovernment advocates of housing affordability have been aware of the limitations of the two major modes of housing assistance and have looked for other, supplementary, solutions. In 1998, the Australian Council of Social Service (ACOSS) called for the Commonwealth government to develop financial instruments to facilitate private institutional investment in social housing (Nicolades, Webb and Hounslow 1998, p.17).

ACOSS participated in the Affordable Housing National Research Consortium, as did the National Community Housing Forum. Following the release of the Consortium's reports in October 2001, 4 national nongovernment peak bodies – the Community Housing Federation of Australia, National Churches Community Housing Network, National Shelter and ACOSS – joined with the Housing Industry Association in releasing a 6-point National Housing Plan (Housing Industry Association 2001).

The Plan urged consideration of options identified by the Affordable Housing National Research Consortium and other stakeholders to increase private sector investment in low-cost housing. It proposed the provision of additional budgetary support to test and facilitate some innovative approaches to housing provision through a Commonwealth Housing Innovation Fund. It suggested examples of projects that could be supported by such a Fund included attracting private sector capital into low-cost housing, community housing partnerships, and alternative financing instruments, particularly for low-income tenants aspiring to owner-occupancy.

There was support for these directions by at least two of the major political parties during the federal election campaign of October-November 2001. The Labor party said that it would 'explore and test innovative strategies to encourage private investment in affordable housing and home ownership' and 'encourage institutional investment in the private rental market' (Albanese 2001b). The Democrats supported 'a wholesale financing solution designed to close the "investment gap" in low cost housing' and specifically endorsed the 6-point national housing plan (Democrats 2001).

However, there was no express or implied support for the policy direction, the 6-point national housing plan, or the Consortium's preferred option, by the Liberal and National parties, who won the 2001 election. Clearly, the Consortium's proposal will not go ahead without the support of the (new) Commonwealth government.
4

5. Questions

In a way, the Consortium's work represents a strategic challenge or shift for the nonprofit nongovernment organizations that comprise the 'housing advocacy lobby'. This is not only because of the process of its work, during which key, peak nonprofit nongovernment organizations were involved with the major housing industry players. And it is not only because peak nonprofit nongovernment organizations participated a tactical political alliance with the Housing Industry Association, in proposing the '6-point national housing plan' following the Consortium's research.

It is because the reports have re-written the basic elements of an affordable housing campaign agenda. The implications of the Consortium's work are that either/or approaches and binary models are failing and will not work. The arguments of supply-side versus demand-side, about public (or social) housing versus private rental housing, about public sector versus private sector, these are not helpful. The looming crisis calls for a breakthrough of these ideologically-based deadlocks, and a search for creative solutions.

Yet the approach that follows from the Consortium's work does not reject components of the agenda proposed by the nonprofit 'housing advocacy lobby' over the 1980s and 1990s. Its major recommendation (the 'housing bond') is a supply-side response. The rationale for the bond is to finance social housing. The scheme will rely on governments to initiate it and manage it. Above all, the approach does not shy from calling for a greater fiscal input by government into housing assistance programs.

What is new is the sober reflection that the ability of the two major modes of housing assistance, taxpayer-funded public housing construction and taxpayer-funded rent assistance, to meet the looming crisis is limited. Bleak. And what is new is an elevation of suggestions for tapping private sector financing of affordable housing – that have been around in various forms for some times – to a 3rd prong. So instead of debating public housing *versus* rent assistance, the strategic alternative is public housing *and* rent assistance *and* private institutional financing of social housing.

This 3-pronged approach might not be comfortable for activists in nonprofit nongovernment organizations who eschew partnerships with capitalists *per se*. But the participants in the Consortium process have a compelling case based on achieving outcomes for low-income Australians in housing stress.

Mike Berry argued (2001, p.19):

> *Finally and critically*, this approach is not presented as a substitute for the two established housing assistance programs in Australia, rent assistance to social security beneficiaries in the private rental sector and capital grants provision through the CSHA for public housing. Rather, this approach is offered as a 'third way', a supplement to the established programs that has the capacity to increase the stock of affordable housing in a targeted and very significant way in the short to medium term. This latter point is crucial. The current affordability crisis and its 'business as usual' trajectory require urgent action by government. Capital constraints on public investment and recurrent expenditure are likely to limit the volume of resources available to achieve an immediate increase in the affordable stock.

The approach does not present a magic solution. The Consortium's preferred model will allow 7,450 households in housing stress to be housed (at a gross cost to the Commonwealth of $220 million). On the other hand, it would cost some $27 billion of taxpayers' money to construct new dwellings to meet the needs of the 227,500 low-income private-tenant households in *metropolitan* cities experiencing housing stress (1996 numbers). Also on the other hand, it would cost the taxpayers an additional $910 million a year to meet the needs of the some 500,000 private tenant households in housing stress through rent assistance (assumed that each of these households need an average of $25 a week in additional support).

The model does not have to be accepted as is. (See Box 2.) It allows for choices. So, for example, even though the Consortium's 4th report (Hall 2001) modelled costs on the assumption of sale of the stock after 25 years, the option anticipates that state housing authorities could retain the assets if they wished, by repaying the bond issuer an amount equivalent to the estimated sale value of the dwellings.

If the approach and model are supported by the nonprofit nongovernment organizations that comprise the 'housing advocacy lobby' in New South Wales, this will not be the end of the housing crisis. There would be significant lead times between the NSW 'housing advocacy lobby' deciding to campaign for political acceptance of such a proposal, and then: the acceptance and negotiation of a scheme by the Commonwealth and state/territory governments, establishment of public sector management arrangements for the scheme, operationalizing the scheme, attraction of investors, generation of revenue streams, deployment of monies, actual construction of dwellings, and allocation of tenancies.

It is unlikely that the numbers of Australians in housing stress will decrease in the next 5 years. What the model offers is some hope that there will be new leverage to enable a 'convincing attack' on the looming crisis.

National Shelter has already endorsed the broad suggestion of new financing initiatives (National Shelter 2001). The Consortium's model does not have bipartisan support – critically, it does not yet have the support of the new Commonwealth government.

Here are some questions for the constituents of Shelter New South Wales to think about:

- Do you support the thrust of the Consortium's analysis, findings and policy approach?
- If not, how can the existing 2-prong approach, which is failing, be realistically made to work better?
- If so, do you support the particular model proposed by the Consortium, in whole or with some qualification?
- If not, what other model would be better?
- If so, how might the Commonwealth and state/territory governments be persuaded to adopt and implement a model as proposed by the Consortium?

These questions will be used by Shelter New South Wales to consult with its constituency on the matters in this summary paper, in early 2002.

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