Submission to the Productivity Commission Draft Research Report on the Contribution of the Not-for-Profit Sector

7 December 2009

This submission to the Productivity Commission's Draft Research Report on the Contribution of the Not-for-Profit sector has been prepared by the Community Housing Federation of Australia (CHFA), the national peak body representing community housing organisations throughout Australia. It deals with Appendix H of the Commission's report, *A Case Study on Social Housing*. In doing so, it builds on previous work carried out by CHFA, including policy documents on the National Affordable Housing Agreement (2008)[1] and the policy conditions for a viable and sustainable sector (2009)[2].

CHFA strongly supports the work that the Productivity Commission has undertaken in the course of carrying out its project investigating the contribution of the not-for-profit sector, and in particular the research that has underpinned Appendix H of the draft report, which provides a case study on social housing.

This submission responds to a number of the issues raised in Appendix H of the report and draws on the experience of people in the sector to highlight the concerns and perspective of housing providers.

Broad vision for community housing

After years of neglect, social housing has been elevated to the top of the national agenda. We have seen positive reforms articulated in the National Affordable Housing Agreement and the Nation Building and Jobs Plan; the $6.4 billion injection into social housing through the stimulus package funding; and Government programs like NRAS have provided enormous opportunities for the community housing sector. The

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[1] *The National Affordable Housing Agreement: a community housing perspective,* Community Housing Federal of Australia, September 2008 http://www.chfa.com.au/Downloads/CHFA%20NAHA%20discussion%20paper%20FINAL.pdf.

[2] *Achieving a viable and sustainable community housing sector: an industry perspective,* Community Housing Federation of Australia, June 2009 http://www.chfa.com.au/Downloads/A%20Viable%20and%20Sustainable%20Community%20Housing%20Sector%20CHFA%20June2009.pdf

Commonwealth has indicated that they intend for the not-for-profit sector to play a pivotal role in the delivery of social and affordable housing. This is evidenced by:

- heavy emphasis on the sector in the National Rental Affordability Scheme (NRAS), which resulted in more than half of all successful applicants in the first two rounds of the scheme coming from community housing providers;
- COAG reforms articulated in the Nation Building and Jobs Plan include reforms that target the development of the not-for-profit sector;
- Minister Plibersek publicly noting her strong support for the community housing sector and expressing her view that a majority of the dwellings built with stimulus package funds be located in the community housing sector; and
- a newly dedicated team in FaHCSIA's housing branch, the Community Housing Industry Section, charged with fostering a rapid acceleration of capacity building activities in the sector.

Despite these commendable developments, what is lacking is a clear national vision of where community housing fits within the future landscape of social and affordable housing. Nor is there a blueprint on the role of community housing in a broader plan that encompasses urban design and infrastructure development. This lack of context makes for uncertainty in the sector as to its future direction. Without such a 'master plan', the sector is destined to progress in an ad hoc, responsive manner rather than in a strategic proactive approach.

Growth of the sector: key considerations

The Productivity Commission's report raised several issues in respect to the growth of the sector (e.g. regulation and stock transfer) and this submission provides some comments on those topics. As well, there are several other key areas that need to be considered when looking at the potential growth of the community housing sector and commentary on those issues are included below.

Regulation

In order to grow a vibrant community housing sector, we need the right regulatory settings. A regulatory system should have at its core the goal of enabling the social housing sector—and governments—to achieve their policy goals, including growth targets. We need a nationally consistent regulatory framework that is about regulating the provider and its business, not its day-to-day activities. Specific outcomes for providers that receive government funding should be dealt with, but within contractual arrangements, not through a regulatory system. When regulation morphs into process management and contracts become overly specific about the activities that are required to achieve the purpose of the contract, rather than just specifying the desired outcomes, then innovation is stifled.[3]

One of the key assumptions and proposals of the initial ARTD proposal for a national regulatory framework for affordable housing providers (2007) was for each state and territory to have their own regulatory legislation that specifies jurisdiction-specific regulatory requirements and intervention power. Where organisations work across jurisdictions, governments could adopt 'coordinated regulatory interventions' consistent with their specific legislative powers. Jurisdictions would work towards 'harmonised' legislation with common, nationally consistent regulatory intervention processes and

[3] Ibid, *Achieving a viable and sustainable community housing sector: an industry perspective*

powers. It is likely that this approach will further entrench existing systems, rather than assist a policy progression towards a fully integrated national regulatory system.

Rather than work with existing systems, CHFA believes that a true nationally consistent regulatory system is required. To achieve this CHFA supports the following conditions:

- *Nationally consistent regulation of the sector*. This means that the same rules apply in all jurisdictions, and that a regulatory framework is more than a loose collection of broad objectives whereby each State and Territory operates under separate regulations. Housing organisations shouldn't have to set up separate entities in each jurisdiction just to satisfy different sets of rules. Further, a regulatory framework should encompass all providers of social and affordable housing: public, private and not-for-profit. This is a national growth strategy and it requires a consistent national regulatory approach.

- *Tiered system* – A national regulatory system should be tiered, to allow providers of different sizes who carry out different types of business to be assessed accordingly, not on a 'one size fits all' basis. It should categorise organisations' activities in relation to a 'risk-adjusted' funding process. This is the system used in New South Wales, where providers are regulated according to their size and level of complexity and level of risk of their housing activities.

  One way of conceptualising the different types of organisations that currently exist would be to break activities into three broad categories: full development capacity; property 'commissioning' capacity; and property management capacity. Organisations could move between these categories depending on the regulatory requirements for the type of activities that they conduct. These three broad types of organisations, each with different regulatory requirements, are described below.

  - <u>Development status:</u> Organisations that have their own development capacity. This capacity includes sophisticated procurement, project management, and financial capabilities and experience. Additionally, many organisations in this category have a range of professionals, such as architects, on their staff.
  - <u>Commissioning status:</u> Organisations with the capacity to commission development processes, secure title to properties, and benefit from GST and other concessions associated with these activities;
  - <u>Property management status:</u> Organisations that wish to grow or continue operating at their present scale using their tenancy management expertise.

  Ideally, organisations could move along this three tiered continuum. Additionally, a national system of regulation could deal with the potential problem of organisations using assets funded by one jurisdiction to debt finance operations in another jurisdiction by 'ring fencing' these assets. Over time, these would form a diminishing proportion of organisations' total stock. Accordingly, state and territory governments would have to be mindful of the new regulations when funding any future activities.

Stock Transfer

The Productivity Commission report on social housing highlights several areas that impact on the community housing sector's growth capacity, including tenant profile and the ability to both leverage assets and service debt. The significance of these components on the likely success of the sector to grow is best illustrated by looking at these issues in relation to stock transfer.

The recent the AIHW report *Australia's Welfare 2009* notes that growth in the sector is likely to be the result of significant stock transfer from the public housing sector to community housing. While the transfer will increase the size of the community housing sector, it doesn't by itself increase the amount of social housing. What it does do is enable the community housing provider to leverage that asset to develop new housing that translates to a net increase of social housing.

In order for that to occur, though, the right policy settings have to be in place, particularly around what stock will be transferred, who the tenants will be and what funding arrangements will be established. For example, the stock being transferred needs to be of a suitable quality so that it's not in need of extensive repair and is leveragable. Location of stock will affect its value as an asset for leverage and must also be considered.

There are several issues surrounding tenants, including their rights and choice when a property is transferred from a public landlord to a community landlord. The composition of tenants is critical as organisations that cater for particular tenant groups will have different spending requirements, and differing capacities to service debt. Last, the type of tenant will dictate what, if any, government subsidy they attract and leads to policy considerations about whether that subsidy will also transfer to the provider along with the stock.

Subsidy is a key policy issue that must be addressed as part of this framework and the development of a growth strategy for the sector. This issue is broader than how it relates to stock transfer but it is a significant factor in ensuring that community housing providers can successfully manage and maintain transferred properties. Funding from the Commonwealth to the States and Territories through the NAHA is distributed on a per capita basis rather than a per dwelling basis, an issue that had been discussed early in the COAG negotiations. If properties are to be transferred to the community housing sector to continue to house people with high needs and very low incomes, the NAHA funding must be passed along, too. No other social housing system in the developed world operates without substantial housing subsidies for their most disadvantaged citizens. There is no 'magic pudding' in the community sector that can replace the need for some level of subsidy.

Financial viability

The case study into social housing notes that there 'has been an increasing move towards providing capital grants attached to specific development projects/goals, and less emphasis on recurrent grants to supplement the rental income of CHOs.'[4] This is an

[4] Appendix H to the Productivity Commission's report into the Contribution of the Not-for-Profit sector, p35.

important observation, and highlights why public policy development needs to be clear about the funding models that will be used by the community housing sector in carrying out their business, as well as the types of financial support that governments are able to offer to the sector. Governments need to give consideration to areas where community housing organisations are potentially financially vulnerable, such as changes in CRA, tenant eligibility criteria, and their tax treatment.

Another issue raised in the case study is that much of the new capital funding available to the sector is restricted to 'growth providers'.[5] CHFA believes that it is important that smaller organisations—many of whom provide unique services to niche tenant groups—continue to operate and flourish.

One mechanism that enables smaller organisations to continue operating in the new 'growth provider' funding landscape is the common equity approach. Under this approach a number of smaller organisations form a new company, of which they are all shareholders. This generates the economies of scale required to participate in a number of activities that would not be possible by any of the small organisations by themselves. This approach operates successfully in Victoria[6], and is currently being implemented with housing cooperatives in NSW. The Community Housing Council of South Australia is currently auspicing a common equity company that will comprise a range of small to medium sized organisations, and the Federation of Housing Collectives in WA has been exploring a common equity model.

The common equity approach has a number of key advantages:

- the assets of the smaller organisations are pooled, allowing for much better debt-financing opportunities;
- the economies of scale generated allow for an increased amount of specialist appointments within the organisation (e.g. CFOs, maintenance specialists etc);
- the common equity company can take care of a lot of 'back of house' business, such as accounting, payroll, rent collection, cyclical maintenance and so on, allowing the smaller shareholder organisations to spend more time focusing on their tenants and their needs.

Subsidies are a critical issue when other levers for raising income become constrained due to contractual or regulatory requirements imposed on the sector. If a stipulation of stock transfer or an affordable housing program requires providers to house people on income based rents, that leaves the provider with few options for raising sufficient income to cover costs, let alone servicing debt, without some form of government subsidy.

There is a need for a social and affordable housing system that operates on a mix of funding and is better matched to need than the current system. This means full or deep subsidies for those households in greatest need and shallow subsidies in instances where community housing is meeting general market failure by housing people on lower wages.

[5] Appendix H to the Productivity Commission's report into the Contribution of the Not-for-Profit sector, p36.

[6] See www.cehl.com.au

This includes both internal subsidies—generated through cross-subsidisation—and external subsidies, such as operating funding and/or rebates from government.

Funding processes need to set distinct outcomes for different parts of the housing market. This approach has been championed by the National Housing Summit Group, which has developed a tiered system that refers to 'bands' of housing. Such bands of housing are aimed at different tenant populations, and are catagorised by different expectations about government investment, rent structure, and length of tenure, amongst other things.

Rental income forms a significant component of organisations' income streams. In developing a more long term strategic approach to growing the community housing sector, consideration must be given to what types of rent-setting models are appropriate to enable growth and what policy settings are required to make that happen. Other than 'maximising' CRA, a number of different rent setting models are already being used across the community housing sector. The primary methods are income-based and discounted market rent.

Regarding rent setting, another important consideration is the reform areas attached to the NBJP, which have been agreed by the state and territory governments. Reform area (i) states that there will be 'improved efficiency of social housing including through better matching of tenants with appropriate dwelling types and the introduction of rent-setting policies that reflect the type of dwellings occupied by tenants'.[7] It is unclear how this will translate in practice, but it is possible that such a reform could have a significant impact on how rents are charged to tenants.

Allocations

Last, a reform area agreed on by COAG is the integration of public and community housing waiting lists.[8] This reform area potentially has significant ramifications for the tenant composition of community housing organisations, and, by extension, the income stream of organisations. As noted above, requirements that restrict an organisation's income stream or its tenant profile can negatively impact on its financial viability. It is necessary and important to distinguish between common *waiting lists* (such as that operating in NSW), which CHFA supports, and common *allocation systems* (such as the One Social Housing System in QLD). This also has implications on security of tenure , which has long been a hallmark of community housing.

For example, the OSHS in QLD goes further than simply allocating tenants, it also stipulates ongoing eligibility. This has the potential to significantly impact on an organisations' income stream. Traditionally many tenants enter community housing on low incomes, but as their situation improves they often begin to earn more, and their rent increases with their capacity to pay more, providing a greater income stream for the housing provider. Research by Hulse and Burke noted that targeting social housing to those on the lowest incomes has played a role in weakening the financial viability of social housing providers is quoted in Appendix H of the Productivity Commission's report.[9] This is an important observation, which is also backed up by anecdotal evidence provided by providers.

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[7] See Schedule C7 in the National Partnership Agreement for the Nation Building and Jobs Plan.

[8] Ibid.

[9] Quoted in Appendix H of the Productivity Commission's report, p38.