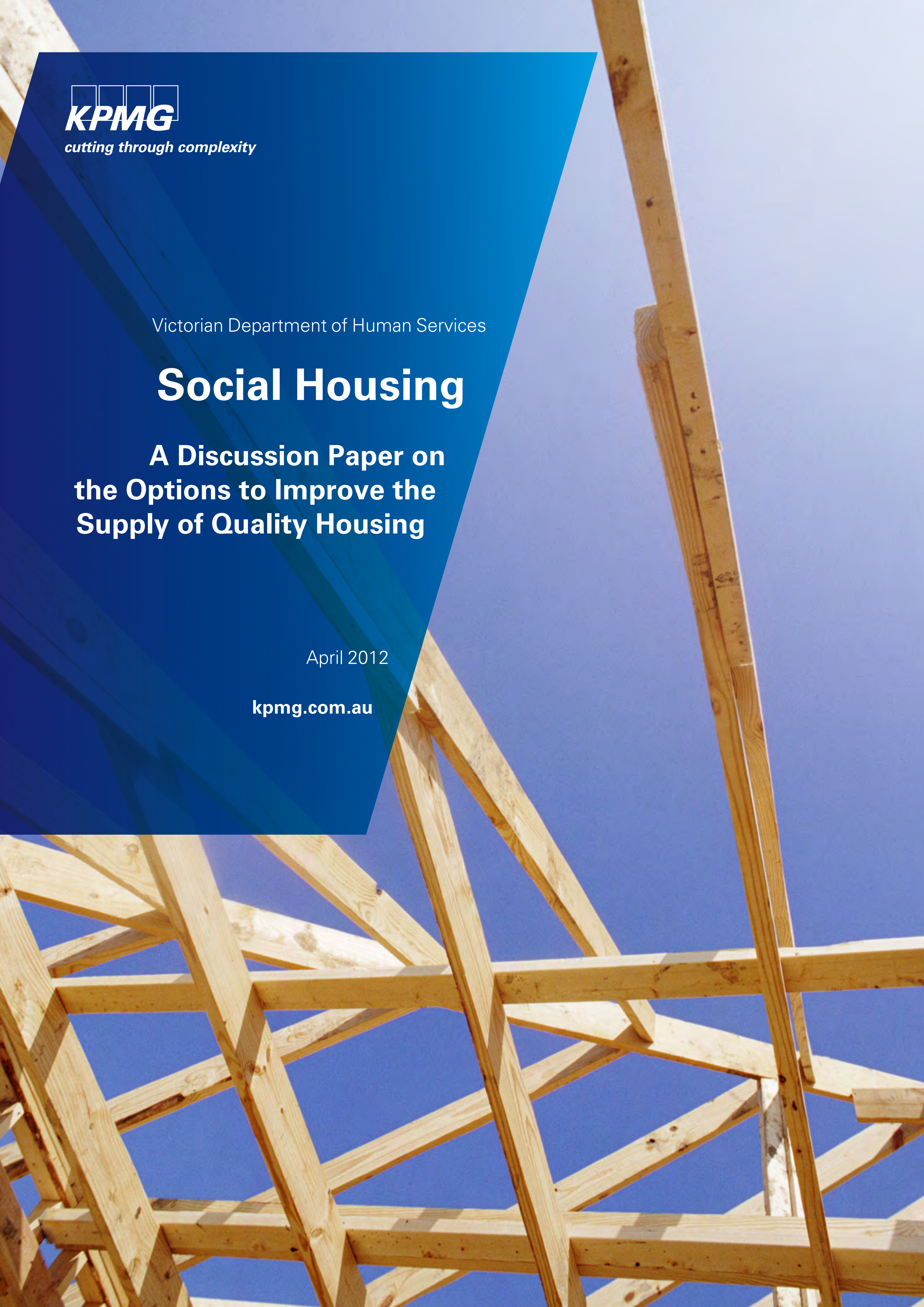

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cutting through complexity

Victorian Department of Human Services

Social Housing

A Discussion Paper on the Options to Improve the Supply of Quality Housing

April 2012

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There will usually be differences between forecast or projected and actual results, because events and circumstances frequently do not occur as expected or predicted, and those differences may be material.

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Glossary

AASB	Australian Accounting Standards Board
ACT	Australian Capital Territory
ACTU	Australian Council of Trade Unions
AHURI	Australian Housing and Urban Research Institute
AIHW	Australian Institute of Health and Welfare
ARA	Housing Fund of Finland
CHC	Community Housing Canberra
CHPs	Community Housing Providers
COAG	Council of Australian Governments
CPI	Consumer Price Index
CRA	Commonwealth Rental Assistance
DGR	Deductible Gift Recipient
DHA	Defence Housing Australia
DHCS	Disability, Housing and Community Services
DHS	The Victorian Department of Human Services
DHW	Department of Housing and Works
DIP	Designated Infrastructure Project
EURIBOR	Euro Interbank Offered Rate
FaHCSIA	Department of Families, Housing, Community Services and Indigenous Affairs
FBT	Fringe benefits tax
FHOG	First Home Owners Grants
GFC	Global Financial Crisis
GST	Goods and Services Tax
HCCBs	Housing Construction Convertible Bonds
IPSASB	International Public Sector Accounting Standards Board
IPSAS	International Public Sector Accounting Standard
NAH SPP	National Affordable Housing Specific Purpose Payment
NRAS	National Rental Affordability Scheme
NSW	New South Wales
NTER	National Tax Equivalent Regime
O&M	Operation and Maintenance
PC	Productivity Commission
PPP	Public Private Partnership
RTA	Residential Tenancies Act 1997
SPV	Special Purpose Vehicle
SUHOS	Step Up Home Ownership Scheme
VAGO	Victorian Auditor-General's Office
WA	Western Australia

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Contents

1 Executive Summary

1.1 Introduction

KPMG has been engaged by the Victorian Department of Human Services (DHS) to provide a discussion paper that explores the supply-side mechanisms available to improve the availability of quality social housing in Victoria in a financially sustainable manner. These options were examined against the key objectives of:

- Protecting and enhancing the continued use of social housing resources for those people most in need of assistance.
- Capturing the potential for growth in social housing opportunities.

The focus of this discussion paper is therefore to explore some of the options available to the Victorian Government to increase the supply of social housing in Victoria. These options are derived from three broad categories and are summarised as follows:

1.1.1 Development Models

Development Models involve participation by the non-government sector to develop new social housing stock. Options include:

1. **Development public private partnership (PPP)** – Contracting with the non-government sector for the design, construction, financing, operations and maintenance of infrastructure and involves an element of public housing stock transfer.
2. **Community housing provider (CHP) development agreement** – Community housing organisations enter into financial partnerships to undertake a socially mixed housing development project.

1.1.2 Transfer Models

Transfer Models involve the transfer to the non-government sector of responsibilities related to the ownership, management and / or operation of the public housing stock. Options include:

1. **Community housing stock transfer model** – Transferring legal title and other rights / responsibilities over the State's housing stock to the CHPs.
2. **Shared equity / ownership schemes** – Involves tenants purchasing a minimum share of the property with ownership of the remaining share of the property being retained by the State Government and / or a CHP.
3. **Outsourcing of maintenance / management** – The private sector delivers tenancy, relocation, communication, consultation, community renewal and other services to public housing tenants and other community members.

1.1.3 Financing Models

Financing Models involve mechanisms to achieve financial outcomes that do not provide a direct increase in supply but provide this indirectly via the achievement of financial benefits. Options include:

1. **Securitisation model** – A form of financing that utilises future rental cashflow streams to finance investment in the acquisition or development of new housing stock.
2. **Loan guarantees** – Reducing risks to financial institutions of commercial loans taken out by CHPs, loan guarantees can reduce the cost of private finance enabling a greater investment in housing stock.
3. **Bond issues** – The State Government acts as an intermediary to sell bonds to private investors to leverage capital for new social housing dwellings.

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4. **Sale and leaseback model** –This involves the sale of property to an investor that in turn leases the property back to the original owner pursuant to a long-term lease.

1.2 Overview of social housing provision in Victoria

Social housing encompasses both the public housing sector and the community housing sector. Public housing is owned and managed by the Victorian Government (through the Director of Housing), whereas community housing is owned and / or managed by non-government organisations (such as community or not-for-profit groups).

Social housing in Victoria is designed as a safety net through which the Government provides housing assistance to those unable to afford or access the private housing market at a particular time in their lives. It is designed to provide assistance to those most in need. The Victorian Government's objective is to ensure there that is equitable access to public housing in Victoria and that those most in need are accorded priority.

Currently around 143,000 people live in social housing in Victoria. This includes 127,000 people living in public housing dwellings.[1] As with other states in Australia, demand for public housing in Victoria far exceeds the supply of appropriate stock available.[2] To assist in managing this excess demand, the Victorian Government has created a segmented waiting list for public housing that is intended to help allocate public housing to those most in need.

1.3 Key drivers and issues for social housing

The Victorian social housing sector faces a number of key challenges to its current operations and financial sustainability. The sections below outline some of the key issues facing the social housing sector.

In March 2012, the Victorian Auditor-General's Office (VAGO) reported on *Access to Public Housing*. It highlighted that the situation for public housing was critical and the system faced significant challenges including:

- An unsustainable operating model and asset management approach, putting the long-term provision of this public service at risk.
- A lack of an overarching direction for public housing and lack of a strategic, comprehensive approach to managing its portfolio.
- An unviable operating model with costs increasingly exceeding revenues.[3]

Coupled with this, the Parliament of Victoria's Family and Community Development Committee conducted an *Inquiry into the Adequacy and Future Directions of Public Housing in Victoria*. It highlighted significant structural problems with the sector including:

- A lack of strategic direction for public and community housing in Victoria.
- Poor procedures around access to public housing and its allocation.
- Challenges in funding financial maintenance and renewal of public housing.[4]

Following the announcement of this report, the Minister for Housing announced the Victorian Government would develop a strategic framework for public and community housing. The goal of the framework would be to review policy settings with the objective of ensuring the community housing system was fair and financially sustainable.

[1] As at June 2011, source: Victorian Auditor-General (2012) Access to Public Housing, Victorian Auditor-General's Report, March 2012
[2] As indicated by the fact that there are currently more than 38,000 on the waiting list for public housing in Victoria
[3] Victorian Auditor-General's Office (2012) *Access to Public Housing*, March 2012
[4] Victorian Parliament (2010) *Inquiry into the Adequacy and Future Directions of Public Housing in Victoria*, Family and Community Development Committee

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1.3.1 A financially unsustainable sector

The cost of subsidising rents and utilities, coupled with reduced rental revenue and maintaining large and ageing stock, has resulted in a current and projected structural deficit for public housing in Victoria. Operating costs for public housing now exceed revenue collected from rent by 42 per cent.[5] The forecast structural deficit (as a result of spending being greater than revenue collected from rent) is expected to double from $56.4 million in 2011 to $115.1 million in 2015.[6] Public housing is also facing a cash crisis, with all cash reserves "expected to be exhausted during the 2012-13 financial year"[7] on current budget estimates and if policy settings remain unchanged.

1.3.2 A significant maintenance backlog

A continual operating deficit in public housing has led to a large maintenance and liability backlog[8] and a deterioration of the asset base. Forty-two per cent of Victoria's public housing stock is more than 30 years old and in need of repair or replacement.[9] In 2011, it was estimated that around $600 million would be required for portfolio maintenance over three years.[10]

1.3.3 A long waiting list

As at March 2012, there were 37,887 people on the waiting list for public housing in Victoria.[11] As the waiting list is segmented into four sections to help allocate public housing to those most in need, some people on certain segments of the list may wait many years to be allocated a public housing dwelling or may never be offered a place at all.[12]

1.3.4 A mismatch in demand and supply

The mix of housing types within the public housing stock is suboptimal and not aligned to the type of housing required by public housing tenants. As at 2011, there were 20,000 people waiting for a one-bedroom public housing dwelling and only 17,500 of this type of dwelling in the total stock.[13] In contrast, there were 25,000 three-bedroom dwellings and 6,000 people requesting this type of housing. Almost 80 per cent of demand is for a one or two-bedroom house and yet these types of houses make up just 53 per cent of the total stock.

1.4 Evaluation of options

The options examined in this discussion paper have been evaluated to show varying degrees of merit in their ability to directly or indirectly address the under supply of social housing in Victoria. Development Models offer a direct increase in supply along with significant improvements in operational efficiency, customer experience, risk transfer and ability to leverage. Transfer Models generally offer a moderate ability to increase supply with the community housing stock transfer model noted as being particularly positive in relation to risk transfer, operational efficiency, leverage and access to tax efficiencies. Financing Models offer benefits via their capacity to increase leverage and reduce the cost of finance, their flexibility to change and their lack of impact on the Government's financial statements, but are noted as an indirect method to increase supply.

A summary of the evaluation of the options is provided overleaf.

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[5] Victorian Auditor-General's Office (2012) *Access to Public Housing*, March 2012
[6] Victorian Auditor-General's Office (2012) *Access to Public Housing*, March 2012
[7] Victorian Auditor-General's Office (2012) *Access to Public Housing*, March 2012
[8] Parliament of Victoria (2010) *Inquiry into the Adequacy and Future Directions of Public Housing in Victoria*, Family and Community Development Committee, September 2010
[9] Internal Department of Human Services data and Victorian Auditor-General Office (2010) *Access to Social Housing*, June 2010
[10] As noted in a 2011 Budget submission by DHS. Source: Victorian Auditor-General (2012) *Access to Public Housing*, March 2012
[11] Internal Department of Human Services data
[12] As at March 2012 there were 27,343 people on the 'general' segment of the public housing waiting list. This segment of the waiting list is for low-income households that might benefit from assistance but who do not have an urgent need. Those on other segments of the waiting list will be allocated public housing before those on the 'general' waiting list.
[13] Internal Department of Human Services data

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Table 1-1: Summary evaluation of models

Criteria	Status Quo	Development 1: Development PPP	Development 2: CHP Development Agreement	Transfer 1: Community Housing Stock Transfer	Transfer 2: Shared Equity / Ownership	Transfer 3: Outsourcing Maintenance / Management	Financing 1: Securitisation	Financing 2: Loan Guarantees	Financing 3: Bond Issues	Financing 4: Sale and Leaseback
Increase in supply	-	✓✓✓	✓✓	✓	✓	✓	✓	✓	✓	✓
Operational efficiency	-	✓✓✓	✓✓✓	✓✓✓	×-✓✓✓	✓✓	×	×	×	×
Customer experience / quality	-	✓✓✓	✓✓✓	✓✓	✓	✓	×	×	×	×
Flexibility to change	-	✓	✓	✓	✓	✓✓	✓✓	✓✓	✓✓	✓
Risk transfer	-	✓✓✓	✓✓	✓✓✓	✓	✓	×	×	×	✓✓
Financial statement impact	-	✓	✓	×-✓	✓-✓✓	✓✓✓	✓✓-✓✓✓	✓✓	✓✓	✓- ✓✓✓
Ability to leverage	-	✓✓	✓✓	✓✓	✓	×	✓✓	✓✓	✓✓	✓✓
Tax / subsidies impact	-	✓✓	✓✓✓	✓✓✓	×	✓	✓	✓	✓	×
Contractual complexity	-	✓	✓✓	✓✓	✓	✓✓	×	✓✓	✓✓	✓✓

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1.5 Conclusion

The public housing system is facing significant challenges and in its current form is considered to be financially unsustainable. There are pressures from the growing waiting list and the ageing of the portfolio significantly compounds this problem. Furthermore, there is a mismatch between supply and demand, meaning that the mix of housing types within the public housing system is suboptimal and not aligned to the needs of tenants. There is a clear current need for significant measures in order to address the long term sustainability of this vital public service.

The incremental approach applied in recent years has been ineffective in increasing supply to match the increased level of demand and the sustainability challenges have intensified. This report provides an overview of a range of potential options that could be utilised to assist in increasing the supply of quality housing. Each of these have various advantages and disadvantages in the manner in which they may directly or indirectly increase the supply of housing. However, it is recognised that in order to materially address the challenge, the implementation of an appropriate combination of solutions will be required.

The optimal combination will be dependent on a number of factors including the inter-related benefits or challenges between sets of options and their overall ability to address the key issues facing the social housing sector in Victoria. The implementation of a combined set of solutions will also need to consider the size and scale required by each option to make them viable. For example, an incremental approach regarding the transfer of stock to the non-government sector is not expected to have a material effect on supply. It is therefore suggested that both the scale and potential combination of options be considered.

Based on the evaluation of each model outlined in this discussion paper, all options and variables warrant further investigation, but in particular it is suggested that further consideration of the following be undertaken:

- Identification of projects suitable for a development PPP.
- Stock transfers to the non-government sector.
- Implicit or explicit government guarantees.
- Further discussions with financiers in relation to the manner in which they assess lending in housing sector.

Applied with significant size and scale and as part of a long-term portfolio realignment strategy, an optimal combination of options should not only increase the supply of quality social housing and help support a financially sustainable asset base, but it should also assist in rebalancing the supply and demand of social housing to better meet the needs of the community.

The optimal solution to drive an increase in the supply of quality social housing in Victoria must also be considered in the context of Victorian Government policies in the social housing sector. For example, if policy settings remain unchanged, a number of the options considered in this discussion paper will be unviable. A holistic approach is therefore required that considers the supply-side mechanisms in conjunction with their enabling policies.

In order to help shape the future of a sustainable social housing sector, the Victorian Government is currently undertaking a market consultation process to seek views on the issues and options outlined in this document.

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2 Introduction and Context

2.1 Background and scope

KPMG was engaged by DHS to provide a discussion paper that explores the supply-side mechanisms available to improve the availability of quality social housing in Victoria in a financially sustainable manner. These options have been examined against the key objectives of:

- Protecting and enhancing the continued use of social housing resources for those people most in need of assistance.
- Capturing the potential for growth in social housing opportunities.

The supply-side mechanisms and non-government sector options to increase the supply of social housing in Victoria to be explored include PPPs, development projects, community housing stock transfer / leverage and other models. These options are explained in further detail in section 4.

This study has been conducted in light of the Victorian Government's commitment to reform elements of the public housing system. The key focus of this reform is making sure that Victoria's public housing system is allocated to those most in need, whilst achieving financial sustainability.

2.2 Overview of social housing provision in Victoria

2.2.1 Definitions

Public housing is owned and managed by the Victorian Government (through the Director of Housing. DHS is responsible for public housing, including the management of applications, allocations, asset management and procurement and tenancy management.

Community housing is housing owned by non-government organisations (such as community or not-for-profit groups).

Social housing encompasses the public housing sector and the community / transitional housing sector. Table 2-1 provides definitions of the types of social housing in Victoria.

Table 2-1: Types of social housing

Housing type	Description	Dwellings	Residents
Public housing	Housing owned and managed by the State through the Director of Housing. The Director of Housing acts as the landlord to public housing tenants.	65,000[14]	127,000[15]
Community housing	Housing managed by not-for-profit registered housing agencies and housing providers for affordable housing purposes.	14,000[16]	16,000[17]
Transitional housing	Transitional housing owned by the State but managed by the community housing sector (i.e. not-for-profit groups).	4,000[18]	N/A
Social housing	The term used to describe public, community and transitional housing.	83,000[19]	143,000 (Approximately)

[14] As at June 2011, source: Victorian Auditor-General (2012) Access to Public Housing, Victorian Auditor-General's Report, March 2012
[15] Internal Department of Human Services data
[16] As at 30 June 2011, source: Victorian Housing Registrar (2011) *Housing Registrar Report*, 2010-11
[17] As at 30 June 2011, source: Victorian Housing Registrar (2011) *Housing Registrar Report*, 2010-11
[18] Internal Department of Human Services data
[19] Department of Human Services (2011) *Annual Report 2010-11*

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To provide community housing, not-for-profit organisations currently work in partnership with the Victorian Government to develop, own and manage rental housing for those on low incomes. These groups include:

- **Housing associations** – Housing associations manage and expand new housing and manage rental properties. These groups may specialise in providing services for specific groups, such as people with disabilities or the elderly.[20]
- **Housing providers** – Housing providers primarily manage long-term and short-term rental housing portfolios and other services. These could be housing cooperatives (co-ops) which are groups of people who work together to maintain and manage housing for its members.

Throughout the remainder of this discussion paper, 'housing associations' and 'housing providers' will collectively be referred to as Community Housing Providers (CHPs).

To remain financially viable, CHPs often have a more diverse mix of tenants than public housing, although they still house up to 50 per cent of clients who would otherwise be eligible to be on the public housing waiting list.[21]

2.2.2 The role and purpose of social housing

Social housing in Victoria is designed as a safety net through which the Government and not-for-profit sector provide housing assistance and support to low income and socially disadvantaged Victorians. It is intended to support those most in need, specifically those who cannot afford the private rental market at a particular time.

The Victorian Government's objective is to ensure that there is equitable access to public housing in Victoria and that those most in need are accorded priority.

As there is greater demand for social housing than there is housing supply,[22] the Victorian Government has created a segmented waiting list for public housing that is intended to help allocate public housing to those most in need. A further explanation of the public housing system is included in section 2.2.3.

History

Public housing

The Victorian Government began providing public housing in the 1930s as a way of regenerating and rebuilding Melbourne's inner-city suburbs. Following the Second World War, the role of public housing evolved as a way of meeting the needs of Victoria's growing economy.[23] By the 1960s and 1970s, public housing was a vital way of providing Victoria's workers and their families quality, affordable homes in Victoria's new manufacturing suburbs and regions.

In the 1980s, the role of public housing changed further, with the composition of residents evolving from working families to households largely dependent on Commonwealth Government social security benefits.[24]

During the 1990s, reforms were also made to disability service delivery. This involved relocating those with a disability from large, government institutions to smaller homes in the community. Since then, public housing has increasingly been called on to respond to the housing needs of those with a disability. As a result the proportion of public housing

[20] Housing associations are a form of legal structure (separate to housing providers) that are meant to invest in housing. Housing providers manage Department of Human Services (DHS) houses and are held to a lower level of incorporations (for example, they can be housing co-ops).
[21] Internal Department of Human Services data.
[22] As indicated by the fact that there are currently more than 38,000 on the waiting list for public housing in Victoria.
[23] Australian Housing and Urban Research Institute (2010) "What future for public housing: A critical analysis", *Final Research Report Number 151*, September 2010
[24] Commonwealth Government income support is the primary source of income for around 86 per cent of Victoria's public housing tenants. *Source: Internal Department of Human Services data.*

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tenancies allocated to households with special needs has increased from around 35 per cent in 2001-02, to more than 60 per cent in 2010-11.[25]

Today, public housing is essentially heavily subsidised housing for those people largely reliant on Commonwealth Government income support.

Community housing

Community housing in Victoria evolved from the establishment of a Community Housing Programme to fund community-managed regional housing councils in 1982. This measure increased the number of social housing tenants in the 1980s.

Amendments to the *Housing Act 1983 (Vic)* and increased government funding have significantly increased the number of community houses in Victoria in recent years. To boost the community housing sector and increase the supply of affordable housing, the Victorian Government transferred 575 public housing properties (valued at more than $155 million) to eight registered housing associations in 2008.[26] The expectation of this transfer was that the associations would then expand their portfolios by a minimum of 15 per cent of the value of the properties transferred. This would be achieved by enabling the Housing Associations to leverage off their property portfolios to build more homes.

During the 1990s, the Commonwealth Government introduced the Commonwealth Rental Assistance (CRA) scheme for people on low incomes living in the private rental market. Tenants living in community housing are able to access this scheme to help them pay rent.

2.2.3 Social housing tenants

In the 1960s and 1970s, public housing was built to accommodate predominantly working families who would use the housing as a transitional measure. Correspondingly, many of the houses and apartments were built with around three or more bedrooms.[27]

Today, around 55 per cent of households consist of either single parents with children or elderly singles.[28] Children aged under the age of 12 represent the largest age cohort living in public housing, followed closely by people aged over 65. Furthermore, the number of elderly people in public housing is expected to increase significantly in future years as the population ages.

Commonwealth Government income support is the primary source of income for almost 86 per cent of Victoria's public housing tenants.[29] The disability pension and the aged pension represent the two largest sources of income for public housing tenants in Victoria. The number of tenants relying on a disability pension as their primary source of income has increased by almost 65 per cent over the last 10 years.[30]

2.2.4 Rental revenue

Public housing tenants make a contribution to the rent based on the amount of income of all members of the household. There are two types of rent for public housing – market rent or rebated (subsidised) rent. Market rent is calculated using the value of the house being rented and is written into the tenancy agreement. The amount contributed is reviewed annually and may change as a result of this review.

All public housing tenants can apply to pay a reduced amount of rent based on their household income. This reduced rent is known as rebated rent and is based on a tenant's base income (i.e. from a job or Centrelink payments), their concessionally treated income (such as family payments and child maintenance payments) and exempted income (such as

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[25] Steering Committee on the Review of Government Service Provision 2007, 2010, 2012, Report on Government Service Provision, Data attachments table 16A.3 (2007), 16.A.2 (2010) and 16.A (2012), Productivity Commission, Canberra available at pc.gov.au, accessed 16 April 2012

[26] Victorian Auditor-General's Office (2010) *Access to Social Housing*, June 2010

[27] Around 40 per cent of Victoria's public housing stock has three bedrooms or more. Source: Internal Department of Human Services data

[28] Internal Department of Human Services data

[29] Internal Department of Human Services data

[30] Internal Department of Human Services data

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veterans' payments).[31] In general, tenants pay around 25 per cent of their base income and 15 per cent of their concessionally treated income. Due to the complexity of the various payments and arrangements however, tenants rarely actually pay 25 per cent of their base income in rent.

Tenants in community housing pay their rent to CHPs and use a different rental model to public housing. Tenants in community housing can pay different amounts of rent, with CHPs seeking to attract a proportion of tenants who pay more in rent than very low income earners. This helps offset the cost of housing for those on lower incomes and creates a viable financial model. In addition, tenants in community housing are also eligible to receive Commonwealth Rent Assistance (CRA), meaning higher rents can be charged.

2.2.5 Demand and supply of social housing dwellings in Victoria

Demand for social housing dwellings

Around 127,000 people live in public housing dwellings in Victoria. As with other states in Australia, demand for public housing in Victoria far exceeds the supply of appropriate stock available. As at March 2012, there were 37,887 people waiting to be allocated a public housing dwelling in Victoria.[32]

The waiting list for public housing in Victoria is segmented into four segments to help allocate public housing to those most in need. The different waiting list segments and the number of people waiting for each segment are included in Table 2-2 below.

Table 2-2: Number of people on the waiting list by segment type as at March 2012

<table>
<tr><th>No.</th><th>Segment</th><th>Description</th><th>No. waiting</th></tr>
<tr><td>1</td><td>Homeless with support</td><td>People with a history or high risk of homelessness.</td><td rowspan="3">10,544</td></tr>
<tr><td>2</td><td>Supported housing</td><td>Coordinated housing for those with a disability or long-term health problems who need modifications made to their houses and / or personal support to live independently.</td></tr>
<tr><td>3</td><td>Special housing needs</td><td>Provides access to people whose current housing is unsuitable and who are unable to obtain more appropriate housing in the private rental market.</td></tr>
<tr><td>4</td><td>The 'General List'</td><td>Housing for low income households who might benefit from assistance but who do not have an urgent need for housing.</td><td>27,343</td></tr>
<tr><td>Total</td><td></td><td></td><td>37,887</td></tr>
</table>

Applicants who meet one of the criteria for segments one, two or three are afforded priority over those on the general waiting list. In 2010-11, the average waiting time for those on segments one, two and three of the waiting list was at least nine months.[33] Those on the fourth segment of the waiting list can wait many years to be allocated a public housing dwelling or may never offered a place at all.

Supply of social housing dwellings

As at 2010, there were almost 83,000 social housing dwellings in Victoria,[34] making up 3.8 per cent of Victoria's total housing stock.

Of the social housing stock, almost 70 per cent is located in metropolitan Melbourne and 30 per cent in regional Victoria. Around 41 per cent of stock is housing with more than three bedrooms.

[31] These payments are exempt from income because of previous arrangements with the Commonwealth or previous Housing Ministers' decisions
[32] Internal Department of Human Services data
[33] Department of Human Services (2011) Annual Report 2010-11
[34] Internal Department of Human Services data, *Summary of Housing Assistance 2009-10.*

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In relation to the community housing sector in Victoria, there are:

- Eight registered housing associations which own, develop and manage rental housing.
- 33 registered housing providers which primarily manage rental housing portfolios.[35]

There are around 14,000 community houses in Victoria, of these, 8,800 are managed by the eight housing associations.

2.2.6 Legislation and governance

Social housing in Victoria is governed by the *Residential Tenancies Act 1997* (RTA) and the *Housing Act 1983*. The RTA sets out the rental agreements between a tenant and landlord and defines the rights and duties of all landlords and tenants (for both the private rental market and social housing sector).

The *Housing Act 1983* sets out the responsibilities and powers of the Minister for Housing and the Director of Housing. In 2005, the *Housing Act* was amended to introduce a regulatory framework for non-profit rental housing agencies to provide low-cost rental housing for low-income tenants. Amendments to the Act also established the Registrar of Housing Agencies to review and monitor the performance of housing agencies and the community sector as a whole. The amendments also acknowledged that while public housing would provide the mainstay for low-cost rental housing for low-income Victorians, the community housing sector would provide tenants with an alternative to public housing.[36]

2.2.7 National regulatory framework for community housing

The Council of Australian Governments (COAG) has established a *National Partnership Agreement on Social Housing* to establish a regulatory framework for social housing.

The COAG agreement contributes to the overarching objective of the National Affordable Housing Agreement which states that “all Australians have access to affordable, safe and sustainable housing that contributes to social and economic participation”.[37] The specific objectives of the Agreement are to:

- Increase the supply of social housing through new construction.
- Provide increased opportunities for persons who are homeless or at risk of homelessness to gain secure long-term accommodation.
- Develop options for reform that will address supply shortfalls and propose possible funding assistance for social housing through means such as CRA.[38]

2.2.8 One DHS

In 2010-11 DHS established its ‘One DHS’ agenda to lead, support and coordinate a change programme across the Department to reorientate operations to “put clients at the centre of everything we do”.[39] The One DHS agenda is focused on:

- Performance – improving service delivery to benefit clients.
- Leadership – developing the capability of staff as leaders.
- Client focused culture – listening and learning from clients about what is important to them.
- Governance and accountability – ensuring clear oversight of the service system and responsibilities.

One DHS involves delivering better client outcomes which bring personal and social value to the Victorian community. These principles and this approach will be at the forefront of service delivery and policy of public housing in Victoria in the future.

[35] Internal Department of Human Services data
[36] Minister for Housing (2004) Minister’s Guidelines for the Exercise of the Registrar of Housing Agencies Powers
[37] COAG, *National Partnership Agreement on Social Housing*, p. 3
[38] COAG, *National Partnership Agreement on Social Housing*
[39] Callister, G. (2010) “Message from the Secretary”, http://www.dhs.vic.gov.au/about-the-department/our-organisation/annual-reports/department-of-human-services-annual-report-2010-11/message-from-the-secretary

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3 Key Drivers and Issues for Social Housing

The Victorian social housing sector faces a number of key challenges to its current operations and financial sustainability. The sections below outline some of the key issues facing the social housing sector.

In March 2012, the VAGO reported on *Access to Public Housing*. It highlighted that the situation for public housing was "critical"[40] and the system faced significant challenges including:

- An unsustainable operating model and asset management approach, putting the long-term provision of this public service at risk.
- A lack of an overarching direction for public housing and a lack of a strategic, comprehensive approach to managing its portfolio.
- An unviable operating model with costs increasingly exceeding revenues.[41]

Further, in October 2010, the Parliament of Victoria's Family and Community Development Committee completed its *Inquiry into the Adequacy and Future Directions of Public Housing in Victoria*. It highlighted significant structural problems within the sector including:

- A lack of strategic direction for public and community housing in Victoria.
- Poor procedures around access to public housing and its allocation.
- Challenges in funding financial maintenance and renewal of public housing.[42]

Following the announcement of this report, the Minister for Housing announced the Victorian Government would develop a strategic framework for public and community housing. The goal of the framework would be to review policy settings with the objective of ensuring community housing was fair and financially sustainable.

3.1.1 A financially unsustainable sector

The cost of subsidising rents and utilities, coupled with reduced rental revenue and maintaining a large and ageing stock has resulted in a current and projected structural deficit for public housing in Victoria.

The forecast structural deficit (as a result of spending being greater than revenue collected from rent) is expected to double from $56.4 million in 2011 to $115.1 million in 2015.[43] Public housing is also facing a cash crisis, with all cash reserves "expected to be exhausted during the 2012-13 financial year"[44] based on current budget estimates and if policy settings remain unchanged.

Figure 3-1 shows that over the past decade, there has been a considerable increase in the amount each dwelling costs in Victoria (direct outflows) and only a minor increase in the amount of rent revenue collected per dwelling (net rent). This is due to a number of factors including the changing demographics of public housing tenants. In 2011, there was a 42 per cent deficit in the amount spent per dwelling and the amount of rent collected.

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40 Victorian Auditor-General's Office (2012) *Access to Public Housing*, March 2012
41 Victorian Auditor-General's Office (2012) Access to Public Housing, March 2012
42 Victorian Parliament (2010) *Inquiry into the Adequacy and Future Directions of Public Housing in Victoria*, Family and Community Development Committee
43 Victorian Auditor-General's Office (2012) Access to Public Housing, March 2012
44 Victorian Auditor-General's Office (2012) Access to Public Housing, March 2012, p. 10

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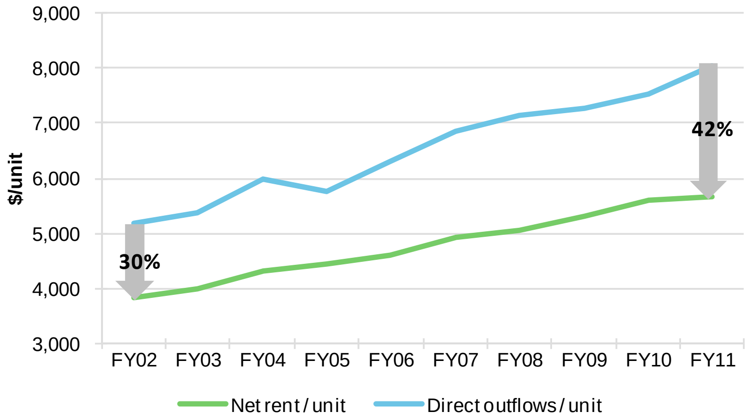
***Figure 3-1: Shortfall from rental incomes in Victoria 2002 – 2011*[45]**



3.1.2 A significant maintenance backlog

A continual operating deficit in public housing has led to a large maintenance and liability backlog and a deterioration of the asset base.[46] Forty-two per cent of Victoria's public housing stock is more than 30 years old and in need of repair or replacement.[47] In 2011, it was estimated that around $600 million would be required for portfolio maintenance over three years.[48]

In 2007, it was reported to the Victorian Auditor-General that:

- Three per cent of stock (more than 2,000 properties), was in 'poor' condition.
- Almost 30 per cent of stock was in 'fair' condition.[49]

In 2007, almost one third of stock had maintenance requirements costing between $5,000 and $20,000.[50]

3.1.3 A long waiting list

As at March 2012, there were 37,887 people on the waiting list for public housing in Victoria. As the waiting list is segmented into four sections to help allocate public housing to those most in need, some people on certain segments of the list may wait many years to be allocated a public housing dwelling or may never be offered a place at all.[51] In 2010-11, those who were deemed the highest priority on the waiting list waited an average of at least nine months for a dwelling.[52]

Contributing to the increased waiting list is the fact that turnover in public housing has steadily decreased in recent years as people who have been allocated a public housing dwelling stay longer. This is due to multiple reasons, but is in part due to the fact that there is no implementation of eligibility reviews of those in public housing and that leases are effectively open-ended. As Figure 3-2 shows, in 1999-2000, the average length of tenancy in public housing was around seven years, whereas by 2009-10 it was more than nine years.[53] This trend decreases the opportunity for those in need to move into public housing.

[45] Victorian Auditor-General's Office (2012) Access to Public Housing, Victorian Auditor-General's Report
[46] Parliament of Victoria (2010) *Inquiry into the Adequacy and Future Directions of Public Housing in Victoria*, Family and Community Development Committee, September 2010
[47] Internal Department of Human Services data
[48] As noted in a 2011 Budget submission by DHS. Source: Victorian Auditor-General (2012) Access to Public Housing, March 2012
[49] Victorian Auditor-General's Office (2007) *Follow up of Selected Performance Audits tabled in 2003 and 2004*, Victorian Auditor-General's Report
[50] Parliament of Victoria (2010) *Inquiry into the Adequacy and Future Directions of Public Housing in Victoria*, Family and Community Development Committee, September 2010
[51] As at March 2012 there were 27,343 people on the 'general' segment of the public housing waiting list. This segment of the waiting list is for low-income households that might benefit from assistance but who do not have an urgent need. Those on other segments of the waiting list will be allocated public housing before those on the 'general' waiting list.
[52] Department of Human Services (2011) *Annual Report 201-11*
[53] Internal Department of Human Services data

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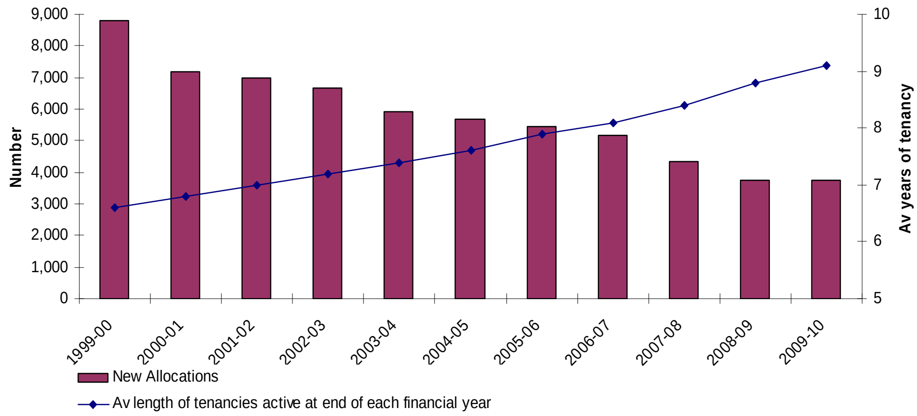
Figure 3-2: New public housing allocations and length of tenancies in public housing 1999-00 to 2009-10[54]



3.1.4 A mismatch in demand and supply

The changing role of public housing from assistance for larger working families to predominantly elderly singles, single-parent families or those reliant on a disability pension, has also changed the type of housing stock required by public housing tenants. Instead of large three-bedroom homes or apartments, tenants require smaller units or apartments (ideally not located in difficult to access, high-rise apartments).

As at 2011, there were 20,000 people waiting for a one-bedroom public housing dwelling and only 17,500 of this type of dwelling in the total stock.[55] Similarly, there were 25,000 three-bedroom dwellings and 6,000 people requesting this type of housing. Almost 80 per cent of demand is for a one or two-bedroom house and yet these types of dwellings make up just 53 per cent of total stock.

[54] Internal Department of Human Services data
[55] Internal Department of Human Services data

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4 Options for the Supply of Social Housing

As discussed in the previous section, the Victorian social housing sector faces significant demand and supply issues. This is against a backdrop of a financially unsustainable system.

The focus of this discussion paper is to explore some of the options available to the Victorian Government to increase the supply of quality social housing in Victoria. These options are derived from three broad categories which are described as follows:

- **Development Models** involve participation by the non-government sector to develop new social housing stock.
- **Transfer Models** involve the transfer to the non-government sector of responsibilities related to the ownership, management and / or operation of the public housing stock.
- **Financing Models** involve mechanisms to achieve financial outcomes that do not provide a direct increase in supply but provides this indirectly via the achievement of financial benefits.

A summary of the options considered in this report is outlined in Table 4-1 overleaf.

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Table 4-1: Supply-side models

Development	**Development Model 1 – Development PPP** A Development PPP model involves contracting with the private sector for the design, construction, financing, operations and maintenance of infrastructure. This model involves an element of public housing stock transfer with the intention that the transferred stock be redeveloped within the commercial framework of the PPP.
	Development Model 2 – CHP Development Agreement Community housing organisations with the capacity to participate in rapid growth can enter into financial partnerships with the private sector to undertake socially mixed housing development projects.
Transfer	**Transfer Model 1 – Community Housing Stock Transfer** This model involves the transfer of legal title and other rights / responsibilities over the State's housing stock to the CHPs. The value of this stock and its appearance on the balance sheet of the CHP allows the acquisition of new properties from any net positive cashflow and borrowings secured against the value of the transferred assets.
	Transfer Model 2 – Shared Equity / Ownership This model is aimed at providing an alternative home ownership opportunity to public housing tenants. Tenure forms where the resident and another investor (public, community or private) jointly owns the property. The State would then provide financing mechanisms to improve home purchase affordability, including shared equity vehicles and direct mortgage financing.
	Transfer Model 3 – Outsourcing of Maintenance / Management This option involves the private sector maintenance of existing, new and refurbished public housing. The private sector will deliver tenancy, relocation, communication, consultation, community renewal and other services to public housing tenants and other community members. While this option does not in itself result in an increase in supply, the cost benefits of efficient operation would enable any savings to be re-invested into additional supply.
Financing	**Financing Model 1 – Securitisation** Securitisation is a form of financing that utilises future cashflow streams to repay debt issued to finance an investment in another asset. This model works by recognising and securitising the rental receipts from social housing tenants and the Victorian Government over an extended period. The proceeds from the securitisation can then be used to re-invest in the acquisition or development of new housing stock.
	Financing Model 2 – Loan Guarantees Government guarantees can reduce risks to financial institutions of commercial loans taken out by CHPs. Passed on to the CHPs, the reduction in the cost of private finance will enable these organisations to increase their borrowing potential and free up capital to allow a greater investment in housing stock.
	Financing Model 3 – Bond Issues This option involves the State Government acting as an intermediary to sell bonds to private investors to leverage capital for new social housing dwellings. This has the potential to lower the cost of debt and improve access to finance from the private sector.
	Financing Model 4 – Sale and Leaseback In its most basic form, the sale and leaseback model involves the sale of property to an investor that in turn leases the property back to the original owner pursuant to a long-term lease. The transaction permits the seller (the Victorian Government) to liquidate its equity in the property while creating a stable investment opportunity for the investor. Furthermore, it transfers a level of risk and responsibility for the properties condition to the new owner.

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5 Evaluation Framework & Value Drivers

The purpose of this section is to provide an overview of some of the key issues and drivers relevant to the assessment of the supply-side models. As part of this, the section provides details of the proposed evaluation criteria to be used for the assessment of options, the issues relevant for each criterion and a framework for evaluation.

Further detail on each of the supply-side options to be considered, including an evaluation of each option against the evaluation criteria, is included in subsequent sections.

5.1 Evaluation criteria overview and evaluation framework

The following table provides details of the evaluation criteria used to assess each of the supply-side models.

Table 5-1: Evaluation criteria

Criteria	Description
Increase in supply	The extent to which the model increases the supply of new social housing in Victoria or replaces old stock that is no longer fit for purpose.
Operational efficiency	The model's ability to achieve operational efficiencies in excess of those achievable by the Government.
Customer experience / quality	The model's effectiveness in improving the experience of tenants and the quality of their accommodation.
Flexibility to change	The model's level of flexibility in circumstances of change.
Risk transfer	The extent to which the model facilitates the transfer of risk to the private sector.
Financial statement impact	The extent to which the model minimises the impact on the Government's financial statements including reduced asset values being recorded in the balance sheet.
Ability to leverage	The model's effectiveness in enabling private sector finance to be utilised to fund the development and acquisition of housing stock.
Tax / subsidies impact	The degree to which the model enables taxation benefits to be realised.
Contractual complexity	The ability of the model to minimise the level of complexity involved in the arrangement.

Further detail on each of these criteria and their relevant issues are provided in section 5.2 below.

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In the assessment of each option, the following evaluation framework is utilised to assess the model's suitability relative to the criteria described in the table above.

Table 5-2: Evaluation framework

Criteria	Description
✓✓✓	Option is extremely effective in satisfying the requirements of the criterion
✓✓	Option is effective in satisfying the requirements of the criterion
✓	Option just satisfies the requirements of the criterion
×	Option is ineffective in satisfying the requirements of the criterion

5.2 Value drivers

The evaluation criteria above were selected on the basis that each criterion relates to a 'value driver' that impacts on the ability to increase the supply of housing stock. Further information on each of these criteria, some of the relevant issues and, where applicable, the relevant research / evidence is provided below.

5.2.1 Increase in supply

This value driver is particularly important and aligns to the DHS objective of capturing the potential for growth in housing opportunities to increase the supply of social housing.

The significance of this driver should be considered with reference to the demand for social housing in Victoria, which far outstrips supply. As stated in section 2.2.5, with approximately 127,000 people currently living in public housing dwellings in Victoria, a further 37,887 people are on the waiting list for public housing allocation.

It should be noted that this criterion is focused on the increase in supply of new housing and therefore relates not only to the total increase in the size of the portfolio, but also the increase in the volume of new stock i.e. via replenishment of the existing assets.

Furthermore, each model's ability to increase the supply of social housing will be heavily influenced by other value drivers considered within the evaluation.

5.2.2 Operational efficiency

The recurrent cost incurred by the State in providing social housing includes:[56]

- Administration costs – the cost of the administration offices of the property manager and tenancy manager.
- Operating costs – the costs of maintaining the operation of the dwelling, including repairs and maintenance, rates, the costs of disposals, market rent / leasehold payments and interest expenses.

The Victorian State Government's recurrent expenditure on housing assistance was approximately $1.586 billion in 2010-11 (including Australian Government expenditure of $683 million for CRA). The Victorian Government's net recurrent expenditure on social housing was therefore $903 million in 2010-11, this compares to $1.0 billion in 2009-10 (2010-11 dollars). However, in addition to the CRA contribution, the Australian Government also provides housing assistance to State Governments through the National Affordable Housing Specific Purpose Payment (NAH SPP) and related National Partnership agreements (accounted for in the $903 million net recurrent cost incurred in 2010-11).

Efficiency in the delivery of operating and maintaining social housing should therefore form a central focus for the State Government. Each dollar saved by eliminating cost overruns and inefficiencies can be used to reduce the maintenance backlog and invest in new housing stock.

[56] Productivity Commission (2012)

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Global experience in competitive models of service outsourcing has shown that significant cost savings can be achieved. A recent study from the UK showed that typical savings of 10 to 15 per cent are available through traditional operating and maintenance (O&M) outsourcing contracts in social housing.[57] Collaborative models are able to deliver a greater level of savings, typically 15 to 25 per cent.[58] A further step is to move to a transformational model of outsourcing, [59] where the opportunities for savings are greater still (20 to 35 per cent).[60]

There is some national statistical data collected on the management performance of the public housing and community housing sectors, however there are many limitations and qualifiers on the comparability of this data over time and between the public and community housing sectors. This is primarily due to differences in data collection methods.

Victoria's public housing stocks are ageing. However, maintenance, repair and replacement costs are increasing, whilst available resources for public housing are shrinking.[61] The net recurrent operating costs per dwelling (in 2010-11 prices) for public housing in Victoria was $5,658 in 2010-11, having increased from $4,788 in 2005-06. A significant maintenance backlog is also known to exist. Furthermore, tenant survey reports in Victoria show a high level of dissatisfaction with the quality of public housing conditions and maintenance outcomes compared to that of the community housing sector.[62]

Data from the Productivity Commission (2012) indicates that recurrent operating costs (in 2010-11 prices) per community housing dwelling in 2010-11 were $8,445, having increased from $7,784 in 2005-06. While this prima facie appears to be higher than the public housing costs above, comparisons with community housing cost data is problematic because of the variation across the sector. These variations include the level of service and quality of asset maintenance being achieved. If these factors were taken into consideration, it is possible that the cost differential would be reversed.

Despite the prima facie higher costs, it is generally recognised that community housing models can provide a level of operational efficiency / increase in service quality when compared to public sector management. Some of the factors impacting this ability to achieve operational efficiency / increase in service quality include:

- CHPs can offer flexible responsive asset management linked to lifecycle and client needs.
- CHPs have the potential to realise reductions in procurement costs and ongoing costs through tax benefits.
- CHPs have the capacity to provide a range of housing opportunities for a wider range of target groups under various rental policies.
- CHPs can display an entrepreneurial approach to corporate and asset planning driven by an interest in improved responsiveness to client needs.
- CHPs have improved opportunities to partner with the private sector to create additional social housing outcomes.
- CHPs have a greater potential to access third party contributions (e.g. the National Rental Affordability Scheme (NRAS) and charitable donations).

Research also suggests that economies of scale can assist CHPs in managing risks which enable cost effective operations. However, there is no consensus on the optimal size of a CHP required to achieve economies of scale, though it is recognised that very small organisations with less than 20 properties have constraints in terms of achieving economies of scale that are able to deliver cost savings.

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[57] Traditional O&M outsourcing is an activity based arrangement where the provider undertakes activities prescribed by the Government and the Government manages demand and end-users

[58] Collaborative O&M outsourcing is an end-to-end management and process improvement arrangement where the Government / Provider agree inputs, activities and outputs with joint management of demand and end-users

[59] Transformational O&M outsourcing is an end-to-end management and process improvement arrangement with whole asset transfer / collaborative asset management. Government / Provider agree outputs, the Provider decides inputs and activities and the Provider manages demand and end-users

[60] Credo Research Paper, *Tougher Times, Smarter Ways, Social Housing: The Missed Savings Opportunity (2011)*

[61] Kenley, R, Chaizor, M, Heywood, C, and McNeilis, S (2009) *Towards Best Practice Public Housing Management,* AHURI Swinburne

[62] AIHW, *Public rental housing 2008–09*

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5.2.3 **Customer experience / quality**

This value driver relates to the experience of the tenant which directly correlates to the quality of accommodation being provided and the associated services. Key to this driver are whether the needs of the residents are being met, whether the environment is being used by its occupants in the ways designers envisioned, and to what extent the environment has contributed to the residents' quality of life experience.

Whilst there is no consensus on a universal definition of good or quality housing, it is generally accepted that good housing should fulfil the various functions which housing should provide, the important ones being shelter, family life, economic stability, family participation and access to community facilities (United Nations, 1977).[63]

The quality of housing that each model delivers will broadly correlate to the age of the housing, with newer housing recognised as providing a better environment to live and improved amenity. For example, prior to redevelopment, many of the units on Victoria's Kensington estate were 'walk ups' which impeded accessibility and required many residents to walk up numerous flights of stairs to reach their unit. Newer dwellings also benefit from improved design and efficient utilisation of space, better building materials and structural integrity, energy efficiency, improved aesthetics, and improved functionality, which covers aspects such as electrical service, storage space and safety features.

In addition to the quality of the interior dwelling, there are a number of community factors that play a critical role in influencing the experience of residents. Examples might include the proximity of the housing to urban centres and job markets, proximity to transport links, community cohesion and crime rates, the social mix of the community and the provision of public amenities such as parks, clinics and schools.

Each model considered in this paper affects the tenants' experience and quality of accommodation in different ways. However, it is widely recognised that there are significant problems in relation to the poor quality and age of public housing stock Victoria.[64] By virtue of this fact, models that provide for new and / or refurbished housing will score more highly on this criteria. Furthermore, as mentioned in the previous section, tenant survey reports in Victoria show a high level of dissatisfaction with the quality of public housing conditions and maintenance outcomes compared to that of the community housing sector.[65] This would suggest that those models which propose a transfer of ownership or management responsibility to CHPs have a greater potential to improve the customers' experience.

5.2.4 **Flexibility to change**

This value driver relates to the Government's ability to respond to change. The models evaluated in this paper each require varying degrees of State control to be relinquished to the non-government sector or specific contractual arrangements to be entered into. This has an inverse relationship with the Government's ability to respond to change and can ultimately affect the Government's future capacity to balance supply and demand.

A key parameter for this value driver is whether legal title of public housing is transferred to the non-government sector. Whist this can provide a range of benefits in relation to other value drivers, with a reduced ability to exercise control over the assets, the Government's flexibility to drive outcomes and respond to change is potentially diminished.

This issue is illustrated in the VAGO report (2010) which states that while housing associations provide housing services which meet tenant needs, equity of access to this housing is not assured.[66] For example, despite the housing associations having a target for how many applicants they are required to accommodate from the public housing waiting list, the reduced flexibility is highlighted by the fact that the housing associations are not required to take those from the top of the list. It is also noted that housing associations

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[63] Sourced from: Noor Sharipah *Quality Affordable Housing: A Theoretical Framework for Planning and Design of Quality Housing,* Journal of Techno-Social (no date)

[64] AHURI Research and Policy Bulletin, *What future for public housing?,* Issue 135 (2011)

[65] AIHW, *Public rental housing 2008–09*

[66] Victorian Auditor-General's Office. (2010) Access to Social Housing, Victorian Auditor-General's Report. Victorian Government Printer

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have greater flexibility in determining rent than public housing and are financially incentivised to house higher-income tenants. However, these issues are primarily driven by the regulatory framework in which the CHPs operate.

Whilst flexibility to change is an important issue for government, it should not undermine the critical role played by CHPs in delivering social housing. The relative importance of this issue is better understood in relation to the volume of transfers being considered for each model, the optimal balance between the status quo model of public housing delivery and the use of other models being considered, and the regulatory framework which governs the provision of community housing in Victoria.

5.2.5 Risk transfer

Risks refer to uncertain outcomes which have a direct effect either on the provision of services or the financial viability of an entity or project.

At a systemic level, risks are largely centred on the increasing demand for social housing (and changing patterns of demand) relative to the supply. Systematic risks in this context include:

- *Macroeconomic risks* – including variables such as inflation, capital growth or contraction rates, rental yield, unemployment and income growth or contraction, changes in nominal and real interest rates, and construction cost escalation rates.
- *Natural disasters* – such as landslip, earthquake, fire, flood, lightning, wind and weather.

There are also risks which are project specific or relevant to individual properties

- *Structural and financial risks* – including funding sources, ownership, residual risks to the Victorian and Federal Governments (especially in respect of a CHP), any non-government involvement, contractual risks and procurement planning.
- *Agency or issue specific risk* – including changes in the political environment, project management, project delivery (contract selection, tendering, negligence etc.), human error, organisational (including industrial relations, resources shortage, management, work practices etc.) and systems (including communications failure, hardware and software failure, etc).

The historic model of public housing provision in Victoria involves significant risk retention by the Victorian Government. However, the different models discussed in this paper offer the opportunity for various levels of risk transfer to CHPs and other non-government organisations.

This is particularly relevant to partnership arrangements between the Government and non-government sectors, which offer significant scope for risks to be managed by non-government parties. Risk negotiation between parties within a partnership demands an open and transparent understanding of all risks and costs associated with those risks, with optimal risk allocation largely depending on the following factors:

- The party that has the greatest capacity (expertise & authority) to manage the risk effectively and efficiently (and thus charge the lowest risk premium).
- The party that stands to reap the most benefit from accepting the risk.
- The level of premium that is rewarded to the party accepting the risk.

It can be argued that the public sector is better able to manage systematic risks that affect not just the specific properties or project, but the market as a whole. Non-systematic risks have an impact on the specific property or project the partnership is responsible for, and can thus be managed effectively and efficiently by non-government partners.[67]

Risk transfer is at the heart of any model that seeks to contract with the non-government sector. The key risk categories that the Government will generally aim to transfer may include the following:

[67] Loosemore, M. & Ng, A. (2006) Risk Allocation in Public Private Partnerships (PPP), International Journal of Project Management

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- *Construction risks* – The State can transfer the risk of construction and would therefore not be obliged to support any cost overruns that may be incurred. In models where private finance is also involved, there is significant incentive for completion and capital at risk to incentivise this outcome.
- *Revenue structure* – Certainty of revenue is a key issue for any model where this risk is transferred. In models where private finance is involved, this is particularly relevant. However, it is important to note that the historical default rate on collection of rental income is very low, with a rental receipt rate of approximately 99 per cent for public housing and 98 per cent for community housing.[68] Furthermore, this risk is further mitigated by the fact that the source of the substantial majority of revenue is directly or indirectly from the Commonwealth or State Government.
- *Operating risk* – The transfer of operating risk is closely linked with the whole-of-life approach to building and maintaining the housing stock. The integrated management structure offered by many models enables a focus on the whole-of-life performance of the asset. To this end, the non-government entity is incentivised to design housing that produces the best whole-of-life outcome in relation to the overall maintenance and operating strategy. Furthermore, the arrangement can provide very strong mechanisms and incentives for the maintenance of the housing stock to an appropriate standard.

5.2.6 Financial statement impact

Subject to the commercial structure utilised, each supply-side model may have a different accounting treatment and thus impact on the State's financial statements. In principle however, there are three primary accounting treatments that are commonly relevant to housing models. These are outlined as follows:

Title transfer

Options that involve the transfer of title in the housing stock from Government to the non-government sector will generally result in a reduction in the asset base of the State. To the extent that such transfer is undertaken on a less than market value basis (as is commonly the case), this would usually result in the decrease in value of land and the properties being recorded in its Income Statements.

In the context of a financially constrained environment, from an accounting perspective, the transfers for nil (or less than market value) consideration may adversely impact the Victorian Government's financial statement.

Long-term lease

Another option that could be utilised involves the transfer of responsibility for the stock via a long-term lease. This option does not involve the transfer of legal title and therefore at the expiry of the lease, the responsibility for the assets reverts to Government.

Options that involve a long-term lease would be considered as a finance lease. As such, the land and the properties would be derecognised from the Victorian Government's balance sheet and a finance lease receivable would be recognised in its place. However, given that in the majority of cases the level of rental is peppercorn (or substantially below market), it is also likely that the value recognised as a finance lease receivable by the Victorian Government would be negligible. This would result in the majority of the decrease in value of land and the properties being recorded in its Income Statement as an expense at inception of the lease – thereby facing similar challenges to the title transfer model discussed above.

Service concession / PPP

A further option is for the arrangement to be structured as a service concession / PPP, where the Government controls or regulates what services the private sector must provide with the assets, to whom and at what price and also controls any residual interest in the assets at the end of the service concession period.

[68] 2009-10 data sourced from the Productivity Commission (2012)

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We note that there is no Australian Accounting Standard or Interpretation that specifically applies to public sector entities accounting for PPP arrangements and practice varies. Historically, in the Victorian public sector such arrangements are accounted for as finance leases. The International Public Sector Accounting Standards Board (IPSASB) has recently issued IPSAS 32 *Service Concession Arrangements: Grantor*, which sets out the accounting for service concessions by the public sector. The accounting treatment largely mirrors the requirements of Interpretation 12 *Service Concession Arrangements* (AI 12), for the private sector. IPSAS 32 has not been adopted in Australia at the date of writing this paper.[69] There is however, a strong expectation that it will drive the shape of an Australian future standard in this area.

In the absence of a specific Accounting Standard or Interpretation, the current emerging practice is to apply AI 12 for the private sector, by analogy. We believe this approach is appropriate through the use of the hierarchy principles in Australian Accounting Standards Board (AASB) 108 *Accounting Policies, Changes in Accounting Estimates and Errors*.

AI 12 / IPSAS 32 use a control based framework, which is more likely than the risks and reward framework to result in a public sector entity recognising an asset of the PPP arrangement on its balance sheet for arrangements within the scope.

Summary

The accounting treatment of the various supply-side models may materially vary. Furthermore, subject to the commercial structure and accounting interpretation, some models may result in an adverse impact on the State's financial statements.

5.2.7 Ability to leverage

A leading benefit of community housing, as opposed to public housing, is its capacity to leverage other sources of finance and to generate its own growth over time. Well managed CHPs with a strong balance sheet and operating at scale, have a capacity to attract further private investment which can ultimately be used to increase their housing stock.

In Victoria, the strategic policy framework supports the expansion of supply of social housing stock owned by housing associations. The Victorian programme encourages CHPs to leverage equity (up to 25 per cent of the value of new assets) to meet growth supply targets. In addition to providing significant new capital funding, significant ownership of public properties has transferred to CHPs over recent years. This came with a requirement that they increase their portfolios equal to 15 per cent of the $155 million value of these assets.

Under the title transfer arrangements, all transferred capital properties can be used as security for financing purposes. However, a VAGO report (2010) suggested that whilst these strategies for increasing the supply of affordable housing owned by housing associations were successful, there was no evidence to suggest that the leveraging rationale for transferring ownership was realised. A key factor for this was that housing associations primarily determine their level of borrowings based on their income, not on the value of their assets. Furthermore, housing associations did not deliver the required 15 per cent leverage on assets transferred within the required time frame of June 2010, and only three of eight CHPs used the transferred assets as security for their borrowing requirements.

The availability and cost of raising new finance are major impediments to increased leverage in the sector. Banks that are willing to lend typically use higher risk premia, while private investors are often reluctant to accept the risk / return profile associated with social housing.[70] This is also evident where development PPP models have been used to develop social housing projects.

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69 24 April 2012

70 Croce C. (2010) Alternative Housing Models: a view from the ground, SGS Housing Forum. Community Housing Federation of Australia

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Typically, bank lending in PPP models is highly leveraged. For example, social infrastructure PPP projects whose cashflows are based on availability payments, will typically obtain gearing ratios ranging between 80 and 90 per cent. However, community housing development PPP projects attract a higher risk premia, which is evident in the debt service cover ratios that are required by lenders and the focus on asset based lending. While two times operational cashflow is usually required in the community housing market (as a debt service cover ratio), only 1.2 times is required in typical social infrastructure PPPs. The interplay between this ratio and the borrowing capacity of a project means that rather than achieving an 80 to or 90 per cent gearing ratio, only approximately 30 to 50 per cent is able to be achieved in community housing development PPP projects.

Community housing is not widely understood by banks as it is not a mature market. In the event that some of the conservative borrowing requirements were able to be amended, there would be a significant potential to increase the level of leverage.

The ability to leverage clearly has the potential to drive an expansion of supply in the community housing market and the degree to which each model is able to achieve this will be explored in subsequent sections.

5.2.8 Tax / subsidies impact

The ability of each model to maximise efficiencies in relation to taxes and access to subsidies or concessions will depend on its commercial structure. To the extent that such efficiencies can be realised, more efficient use of resources (e.g. potential cost savings) will be available to be reinvested in the social housing stock.

Tax efficiencies can be achieved at the State and Federal levels and each will require detailed analysis and implementation at the time of entering into specific arrangements. In addition to these, availability of subsidies and grant schemes should be considered.

In evaluating each model, all CHPs are assumed to be endorsed gift-deductible, tax exempt entities.

5.2.8.1 Federal taxes

At the federal level, the model's tax efficiency will be impacted by income tax and goods and services tax (GST).

Income tax

Charitable taxation status

Many of the models rely on participating CHPs obtaining charitable status. Charitable taxation status broadly exempts qualifying entities from Federal income tax (and GST, see below). The charity rules are currently subject to review with two major reform aspects being:

- Charitable entities will be subject to Federal income tax on unrelated commercial activities not directed back to the charity's altruistic purpose.
- Charitable entities will no longer have access to fringe benefits tax (FBT) exemptions / rebates, GST or deductible gift recipient (DGR) support for unrelated commercial activities.

Broadly, these changes may have the impact of increasing the cost for a CHP participating under the various models. Whilst these proposed changes will not necessarily be fatal to the models proposed in this paper, care will need to be taken when implementing the proposed models to ensure that contributions from charitable entities fall within the revised permitted charity guidelines. The date from which these proposed rules will take effect is uncertain.

A statutory definition of 'charity' is also proposed to be introduced. Whilst this new definition should not impact charities previously qualifying for charitable status, it may impact upon new charitable organisations and entities set-up specifically to assist with community housing under the proposed models.

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'Preferred use assets'

Where an entity or organisation does not have charitable status, it will prima facie be subject to Federal income tax. The tax implications in such cases can be complex. One of the specific risks when managing the transfer of assets from Government to the private sector is the impact of tax laws surrounding 'preferred use assets'. These rules broadly apply to deny certain deductions which would not have been available if the asset remained Government owned. Accordingly, under certain models considered in this paper, the pricing and feasibility of private sector contributions may be severely impacted if these rules are not properly addressed. Consideration of these rules prior to implementing a preferred structure is essential.

National Tax Equivalent Regime (NTER) and competitive neutrality

Certain wholly owned government enterprises are subject to the NTER, which broadly operates to apply income tax laws as they would apply to privately held counterparts. The primary objective of the NTER is to promote competitive neutrality.[71] Potential breaches of competitive neutrality principles should be considered in the context of the suggested models. Where it is found that competitive neutrality principles are breached,[72] it may be necessary to include the relevant government entity in the NTER, thereby subjecting it to income tax laws. In due course, consultation should be undertaken with the appropriate Government Agency to manage this issue.

Prospective tax reform – Designated infrastructure project (DIP) losses

On 26 October 2011, the Federal Government released a discussion paper proposing to introduce new rules for tax losses that are attributable to DIPs. Broadly, under the proposed rules, qualifying projects will be able to uplift the value of carry forward tax losses by the 10-year Government bond rate.

Whilst legislation in respect of the DIP loss rules have not been passed to date, it is expected that qualifying projects will be subject to a minimum capital expenditure threshold of $100m. Depending on the scale and nature of projects undertaken, private stakeholders may potentially benefit from these proposed rules, when introduced. This in turn may assist in realising tax efficiencies.

Goods and services tax

The default GST position in relation to the leasing of residential accommodation is that no GST is chargeable on rent. However, there is limited recourse to GST credits on construction and / or operational costs. The effect is that there will be some GST leakages.

GST efficiencies may, however, be achieved where a housing provider is able to access exemptions under the GST law. Relevantly, GST-free supplies are not subject to GST and do not result in a denial of GST credits on inputs. In effect, GST has no cost to the supply. A supply of accommodation is GST-free if:

- It is provided by an endorsed charitable institution, an endorsed trustee of a charitable fund, an endorsed gift-deductible entity or a government school.
- Consideration for the accommodation is less than 75 per cent of the GST inclusive market value or of the cost of providing the accommodation.

5.2.8.2 ***State taxes***

At the State level, Victorian duty will apply on sales of land. Additionally, annual land tax can be payable on investor owned housing. Exemptions from land tax and duty are available where the taxpayers are government bodies, charitable bodies or co-operatives with primary activities of providing community services. Land tax does not apply where owners occupy the premises as their principle place of residence.

[71] Manual for the National Tax Equivalent Regime, January 2008 (Version 6)
[72] Competitive Neutrality Policy Victoria (2000), prepared by the Department of Treasury and Finance

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5.2.8.3 *Subsidies and grants*

At both the Federal and State level, opportunities exist for financial support through subsidies and government grants. Government grants are specifically tailored support packages which allow the Government to drive investment into key priority sectors. It should be noted that subsidies and incentives are often entitlement based, whereas grants are competitive in nature and require a strong business case for funding success. The landscape for subsidies and grants is constantly changing, depending on national priorities.

Grants may have an impact by providing capital investment for community infrastructure, including accommodation. Many grant programmes are focused on indigenous people, social inclusion and reducing homelessness. The Department of Regional Australia, Local Government, Arts and Sport - Regional Development Australia Fund provides funding of up to $25 million for local government bodies and not-for-profit organisations for investment in priority infrastructure projects identified to provide long term social and economic benefits to the community. Eligible first home buyers may also be entitled to claim First Home Owners Grants (FHOG).

NRAS is a key federal grant programme which is currently open to investors, property developers and CHPs. The programme provides financial incentives to eligible persons providing approved dwelling rented to eligible low and moderate income households at a rate that is at least 20 per cent below the prevailing market rate.

5.2.9 Contractual complexity

The different models will involve varying degrees of contractual complexity. The level of interface between parties and the management of risk within contractual arrangements will add to this complexity. For example, it is not uncommon for PPP contracts to be complex due to the aligning of interests and management of interface risk between multiple stakeholders including the Government, construction developers, O&M contractors, debt and equity providers and subcontractors. Such contractual arrangements aim to optimise the allocation of risks (and rewards) to those parties most capable of managing them. It should therefore be noted that despite the added complexity, value for money benefits can be achieved through the integrated and single contract management structure that relieves interface risks.

In addition, 'tried and tested' arrangements where standard contractual precedents exist will inevitably involve significantly less complexity than those that are largely untested in the market.

While this criterion does not directly impact on the supply of social housing, it is nonetheless important in relation to the practical ability of DHS to achieve the stated objectives.

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6 The 'Status Quo' Model

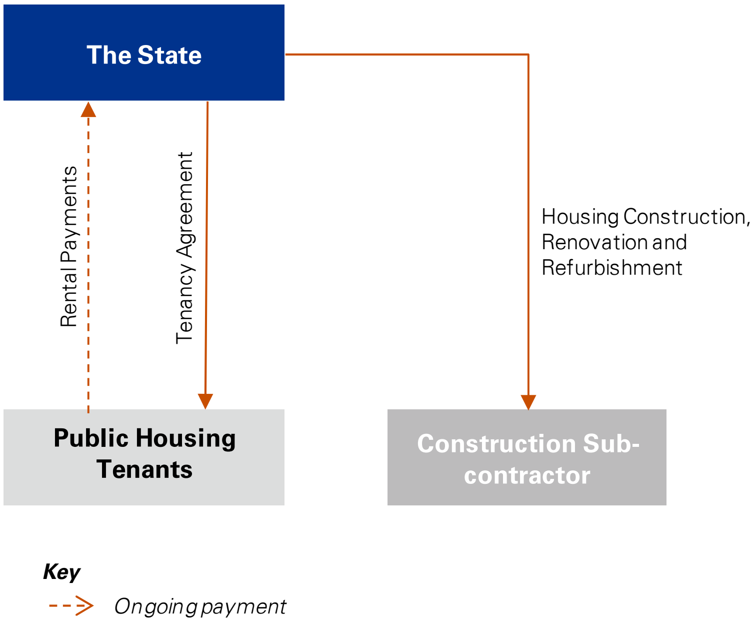
6.1 Outline of model

The Status quo model has been included here as a point of comparison for the supply-side options explored later in this discussion paper.

Although it is recognised that DHS works in partnership with not-for-profit housing agencies in their delivery of community housing for low and medium income Victorians, the Status quo model relates specifically to public housing which is directly funded, operated and delivered by DHS.

This model therefore involves the retention of ownership and landlord responsibilities by DHS. This is illustrated in the commercial structure diagram in Figure 6-1 below, with the tenancy and facilities management of the public housing being administered by DHS.

Figure 6-1: Commercial structure of the Status Quo model



The key features of this commercial structure are presented in Table 6-1 below:

Table 6-1: Key features of the Status Quo model

Commercial Structure Features	Applicability to Model
Title transferred to private sector	No
Residual land value risk allocated to private sector	No
Contractual term	N/A
Responsibility for operations transferred to private sector	No
Responsibility for maintenance transferred to private sector	No
Direct increase in supply of housing stock	No
Utilisation of private sector finance	No
Nature of the housing stock	Existing

As can been seen in the diagram and table above, the Government retains substantially all of the risks associated with the public stock of social housing.

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6.2 Evaluation of model

Table 6-2: Status Quo evaluation matrix

Criteria	Rating	Description
Increase in supply	-	Without additional funding, the supply of public housing stock will not increase under the current model.
Operational efficiency	-	Operational efficiency remains constant.
Customer experience / quality	-	Consumer experience and the quality of housing stock will remain constant if sufficient recurrent funding is provided that maintains the properties to their current standard.
Flexibility to change	-	Flexibility to change remains constant.
Risk transfer	-	No additional risks are transferred from government.
Financial statement impact	-	There are no impacts on the State's financial statements.
Ability to leverage	-	There is no improvement in the ability to leverage.
Tax / subsidies impact	-	The impact of taxes remains constant.
Contractual complexity	-	The level of contractual complexity remains unchanged.

Summary of evaluation

The Status quo model has been included here as a point of comparison for the supply-side options that are evaluated in the sections that follow.

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Development Models

involve participation by the non-government sector to develop new social housing stock

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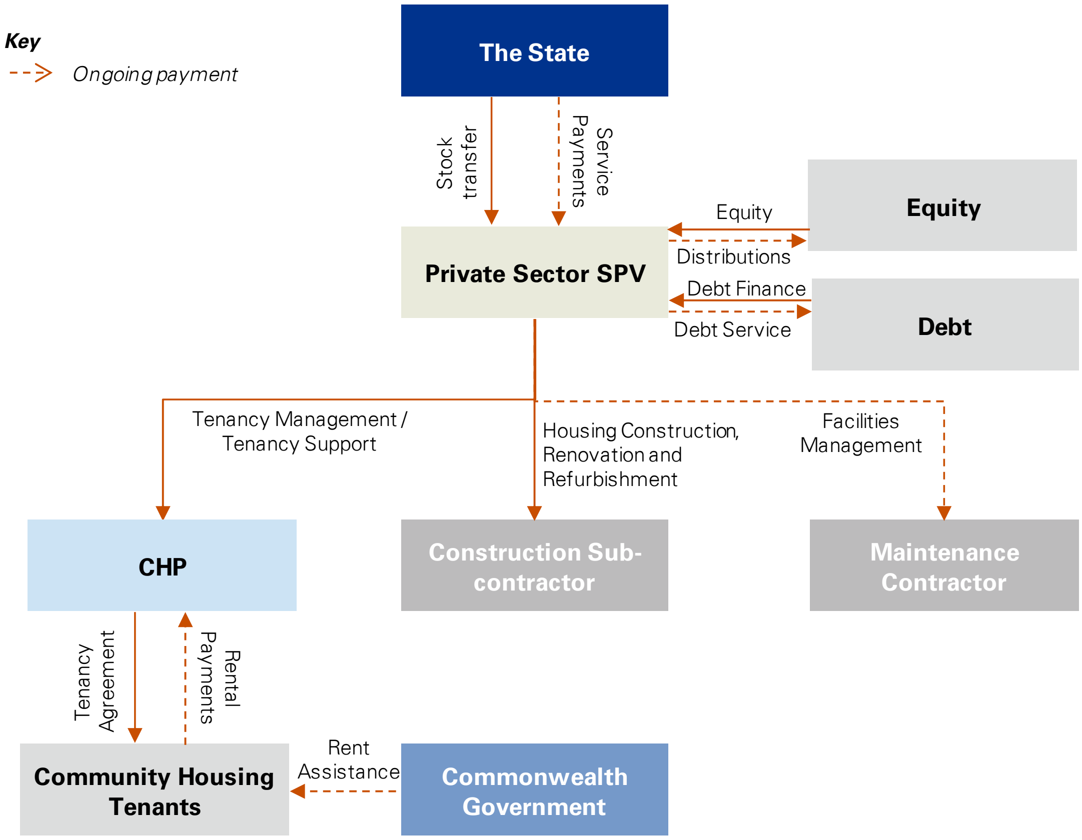
7 Development Model 1 – Development PPP

7.1 Outline of model

A development PPP model involves contracting with the private sector (via a Special Purpose Vehicle (SPV)) for the design, construction, financing, operations and maintenance of social housing. This model could also involve an element of public housing stock transfer, the intention of which is that the transferred stock be redeveloped or refurbished within the commercial framework of the PPP (with no loss in the number of social housing dwellings). Therefore, the existing social housing stock can either remain as public housing in government ownership or transfer to a CHP as community housing. This model could also include a subsidy from government or payment to government depending on the commercial arrangements of the project.

The commercial structure of this model is presented in Figure 7-1 below:

Figure 7-1: Commercial structure of the Development PPP model



The key features of this commercial structure are presented in Table 7-1.

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Table 7-1: Key features of the Development PPP model

Commercial Structure Features	Applicability to Model
Title transferred to private sector	Yes
Residual land value risk allocated to private sector	Yes
Contractual term	≈ 25-30 years+
Responsibility for operations transferred to private sector	Yes
Responsibility for maintenance transferred to private sector	Yes
Direct increase in supply of housing stock	Yes
Utilisation of private sector finance	Yes
Nature of the housing stock	New and existing

As can be seen in the diagram and table above, a combination of title transfer of public sector housing stock and private sector finance is utilised to redevelop existing stock as well as developing new stock. At the end of the contract term, the land and housing assets may remain the responsibility of the CHP and not be transferred back to the public sector.

The benefits of PPPs have been recognised for a number of years with further research being recommended by the National Housing Strategy since 1991. Despite a number of initiatives in this area, private sector involvement has been limited. Until recently, co-operation between the public and private sector extended to little more than cases of swapping government land for affordable housing construction by the private sector.

The PPP model has the potential to provide access to the financial resources of the private sector, enabling an increase in the supply of affordable rental housing. Institutional investment in affordable rental housing is constrained by the inability of private investors to achieve satisfactory risk-adjusted rates of return without some degree of subsidy. Any given quantum of public funding, used to leverage private investment in the low-rent housing market, will generate substantially more additional stock than public funding alone.[73]

[73] Australian Council of Trade Unions (2007), *Affordable Housing; Issues, Principles and Policy Options,* Affordable Housing Summit, Canberra

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7.2 Case study

Table 7-2: The Bonnyrigg PPP case study

The Bonnyrigg project

Location	NSW, Australia
Description	• The project is revitalising an 81-hectare housing estate within the western Sydney suburb of Bonnyrigg. • The project is valued at approximately $733 million and will see the replacement of 833 existing social housing dwellings that are in poor condition with 2,330 new homes (70 per cent of which are private homes and 30 per cent social homes). • The project will reduce the concentration of social housing within the estate from the original 89 per cent to the target 30 per cent with the aim to create a more socially inclusive community. • It is expected that the estate will be delivered over 14 years. • The operating period is over 30 years.
Key Features	• Housing NSW contracts with Bonnyrigg Partnership, a private sector SPV, via a project deed. • The contractual obligations of the Bonnyrigg Partnership can be divided into two functions, development and facilities management. They are delivered by two separate SPVs – development (Bonnyrigg Developments) and management (Spotless). • In return for the development and management services, Housing NSW makes monthly performance-based payments to the SPV. These payments are to fund part of the project delivery cost. • All forecast funding requirements of the project would be met by the SPV through a combination of debt and equity. Westpac and Becton Property Group are the equity investors in the project. Westpac is also the lead debt financier and agent for the project. • Bonnyrigg Developments is the building contractor and provides: – Design and construction of both infrastructure and financing – Marketing and sales for the project's privately owned properties • Housing NSW is entitled to agreed proportions of the income from the private dwelling sales. • Spotless is the Facilities Management Contractor. It is obliged by the SPV to provide specified facilities management, tenancy, community renewal, communication consultation, management and integration service. • The St. George CHP has the following two roles: 1. Facilities Management Contractor's subcontractor for the provision of tenancy services to the project's social housing tenants. 2. Tenancy manager. The CHP would enter into an associated side contract with Housing NSW and obtain a ground lease from Housing NSW to act as landlord of tenancy agreements with social housing tenants.
Benefits	• A competitive tendering process shortlisted three respondents to submit detailed proposals. • The PPP delivery model reduced the property and tenancy management requirements and risks to Housing NSW over an extended period of time. • Significant transfer of risks from government. The private sector is well placed to manage the whole-of-life risks associated with the development of such a complex project and the sale of a significant volume of private housing. • The private housing component of the project and the attractive revenue stream associated with this enabled the project to draw private sector funding (including both debt and equity). • Value for money was represented by a 6.3 per cent cost saving relative to traditional public sector procurement.

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The Bonnyrigg project

	• Relative to traditional procurement, the NSW government benefitted from making a lower up-front capital contribution, with the Government contribution primarily consisting of monthly service payments over the 30 year operating period. • Bundling of development and facilities management services provides strong incentives for all parties in the consortium to perform. For example, the commercial pressure imposed by the need to sell private dwellings provides an incentive to ensure good quality tenancy management.
Issues / challenges	• The model is extremely complex and will generally only be suitable for large-scale projects of this nature. • The level of private sector involvement is substantial and these parties seek a profit margin on their investment. • 14 years is a significant timeframe for the development phase of the project. • Although the suburb will benefit from new homes and a better social mix, the project will not result in a net increase to the total number of social housing units.

7.3 Evaluation of model

Based on the evaluation criteria and framework outlined in section 5, we have undertaken an evaluation of the model as follows.

Table 7-3: Development PPP evaluation matrix

Criteria	Rating	Description
Increase in supply	✓✓✓	Leveraging from both asset and cashflow security, private sector finance is utilised to develop new social housing. Although dependent on the size and scale of the project, this model has the potential to develop additional new housing stock that could either directly increase supply or replace old stock that is no longer fit for purpose.
Operational efficiency	✓✓✓	The 'whole-of-life' approach to building and maintaining the facility is fundamental to the PPP. The integrated management structure offered by a PPP develops a focus on the whole-of-life performance of the asset. The housing is designed with the objective of long-term efficiency in the delivery of housing services.
Customer experience / quality	✓✓✓	The newly developed accommodation will be of significantly superior quality compared to existing public housing. The tenants' experience is also likely to improve as developments of this nature are likely to have a reduced concentration of social housing which enables more socially inclusive communities.
Flexibility to change	✓	In PPP models involving title transfer of public housing, the Government's flexibility to react to changing circumstances in the future could become more restricted. Whilst there are additional challenges concerning the contractual structure of PPP projects, which can be viewed as being less flexible in certain circumstances, it should be noted that there is generally an inverse relationship between contractual simplicity and the level of risk that is transferred to the non-government sector.

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Criteria	Rating	Description
Risk transfer	✓✓✓	Risks associated with the design, build, finance, operation and maintenance of the social housing are transferred contractually to the party that is best able to manage them. However, the risk (or reward) of residual land and property values is also transferred in this model.
Financial statement impact	✓	Options that involve the transfer of title in the housing stock from Government to the non-government sector will generally result in a reduction in the asset base of the State. To the extent that such transfer is undertaken on a less than market value basis (as is commonly the case), this would usually result in the decrease in value of land and the properties being recorded in its Income Statement.
Ability to leverage	✓✓	This model is effective in its ability to provide additional leverage. Private sector finance can be obtained with future cash flows used as security (the PPP element), as well as providing the ability of securitising the transferred housing stock for further leverage. There would be significantly more potential to increase the level of leverage if some of the conservative borrowing requirements seen in community housing projects were able to be amended.
Tax / subsidies impact	✓✓	GST concessions may be available to CHPs to reduce GST costs on construction and operational expenses. Private Sector SPVs will be liable for net GST on the sale of housing built or substantially renovated within 5 years of sale. Victorian duty may apply on the transfer of housing stock to the Private Sector SPV, which would be ineligible for exemptions. Land tax may also apply. These may increase the cost of the project. Where the Private Sector SPV is not exempt under Federal tax, special care will be required to ensure the availability of tax deductions in respect of costs of the SPV. This is due to the 'tax preferred use' rules which operate to deny certain deductions where assets are transferred from Government to the private sector. Failure to address this issue may result in higher pricing, or the model becoming commercially unfeasible.
Contractual complexity	✓	PPP contracts tend to be relatively complex due to the aligning of interests and management of interface risk between multiple stakeholders including the Government, construction developers, O&M contractors, debt and equity providers and subcontractors.

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Summary of evaluation

The primary benefit of the Development PPP model is the ability to allocate risk to the party most qualified to bear or manage that risk. In turn, this incentivises the non-government partner to develop a focus on the whole-of-life performance of the asset. An appropriate payment and abatement regime implemented by government will therefore incentivise the achievement of operational efficiency while limiting incentives that could compromise the quality of outputs.

Another benefit of this model is its ability to provide additional leverage. This is in terms of both future cash flows and asset security (where the commercial framework includes stock transfer). Furthermore, the transfer of residual value risk may provide an additional upfront financial benefit to Government, based on a view to (and ability to capture) the future value of land and property.

However, unlike other social infrastructure PPPs, community housing is not widely understood by banks as it is not a mature market – it therefore suffers from conservative borrowing criteria which reduces the ability to achieve leverage. An option for this model would be for the Government to provide an implicit or explicit guarantee on the rent (see Financing Models), with occupancy risk remaining with the Government. Currently, the source of the substantial majority of revenue is directly or indirectly from the Commonwealth or State Government which further mitigates this risk. In addition, as noted earlier, the historical default rate on collection of rental income is very low with a rental receipt rate of approximately 99 per cent for public housing and 98 per cent for community housing. These facts should be considered when attempting to alleviate the conservative borrowing requirements currently expected in community housing development projects. This therefore provides significant potential for the level of leverage to increase.

Despite the notable drawbacks relating to the impacts on the Government's financial statements and the issue that contractual arrangements can be complex, this model has the potential to address the under supply of social housing in Victoria for areas requiring large scale redevelopments or new greenfield areas.

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8 Development Model 2 – CHP Development Agreement

8.1 Outline of model

Community housing organisations with the capacity to participate in rapid growth can enter into financial partnerships with the private sector to undertake a socially mixed housing development project.

An example includes the Glebe project in NSW with City West Housing delivering and managing the affordable housing component and Bridge Housing developing and managing the social housing component.

The stock transfer model can be structured in a variety of ways to achieve the desired outcome. The following descriptions and diagrams illustrate how the stock transfer model can be modified to involve the CHP in the private sector development of an existing site.

There are already some indications that Australian housing developers / owners are moving in the direction of undertaking some commercial activity. Brisbane Housing Company has diversified into commercial land development and mixed use residential and commercial development with private sector developers. It has also contracted out its development expertise to the housing market. The proceeds of these activities subsidise its core affordable housing mission. This strategy was explicitly determined to overcome the viability and growth constraints faced by the organisation due to limited rental returns.[74] Community Housing Canberra (now CHC Affordable Housing), as part of its business model, undertakes commercial development of moderate income housing, including the market sale of affordably priced properties, with development proceeds being reinvested into affordable rental housing.[75]

Other entities, such as City West Housing in Sydney, have previously expressed interest in expanding into market rental opportunities to increase their revenue and growth prospects, but pointed to taxation and government policy as barriers to pursuing these strategies.

In the United Kingdom, there has been a significant increase in social housing providers redeveloping and selling property to increase their surpluses. In 2000, the sector-wide surplus from asset sales was £109 million. In 2008, this rose to £577 million. A third of all housing associations reported surpluses over £1 million from asset sales in 2008.[76]

The commercial structure of this model is presented in Figure 8-1.

[74] See Milligan, V. Gurran, N. Lawson, J. Phibbs, P. and Phillips, R (2009), Innovation in Affordable Housing in Australia: Bringing Policy and Practice for Not for Profit Housing Organisations together, AHURI. p. 179 and (2005) Evaluation of Brisbane Housing Company

[75] Milligan, V et al (2009)

[76] UK Tenant Services Authority (2009) 2008 Global Accounts of Housing Associations: Landlords Financial Health

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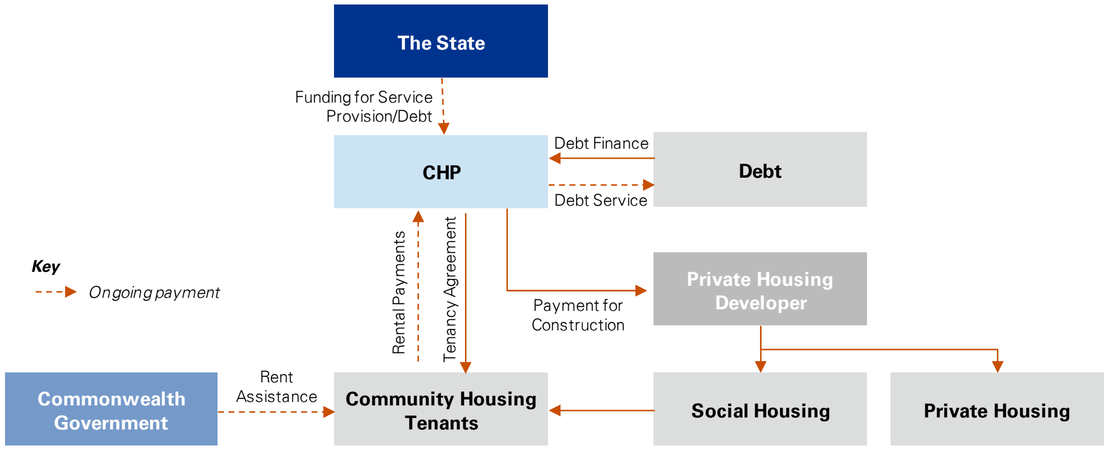
Figure 8-1: Commercial structure of the Development Agreement model



The key features of this commercial structure are presented in Table 8-1 below:

Table 8-1: Key features of the CHP Development Agreement model

Commercial Structure Features	Applicability to Model
Title transferred to private sector	Yes
Residual land value risk allocated to private sector	Yes
Contractual term	Contract permanently transfers freehold ownership of the Private component to a third party
Responsibility for operations transferred to private sector	Yes
Responsibility for maintenance transferred to private sector	Yes
Direct increase in supply of housing stock	Yes
Utilisation of private sector finance	Yes
Nature of the housing stock	Existing and new

As can be seen in the diagram and table above, ownership of some housing stock is retained by the CHP with the remainder of the housing stock transferred to the private developer. Operational and maintenance responsibility for the community housing stock remains with the CHP. The CHP is the primary contact for the State and their role is the management of the community housing as well as property and development agreement negotiations.

Development agreements with corresponding levels of risk transfer and profit sharing potential can take different forms. The greater the degree of collaboration within the agreement, the greater the opportunity make cost savings via improved operational outcomes. However, it is worth noting that this structure is likely to hold more risk because of the limited experience that CHPs have in a large development type role.

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8.2 Case study

Table 8-2: The Kensington redevelopment case study

The Kensington redevelopment project

Location	Victoria, Australia
Description	• The Kensington estate was originally built in the 1960s and consisted of 850 dwellings on a 6.5 hectare site, comprising of three high-rise towers and fifteen blocks of 'walk up' (four-storey) flats. • Demolition of the walk-up flats on the estate (which contained 378 public dwellings) commenced in the late 1990s. • Work on the redevelopment took place over 10 stages between 2002 and 2011 at a cost of $150 million. The Victorian Government contributed $47 million, with the remainder coming from the private sector. • DHS took responsibility for upgrading 217 public dwellings in the two high-rise towers that were not demolished as part of the project. Upgrade work to these towers is continuing and will include new lifts, refurbished foyers, renovated apartments, a larger common room, improved security systems, and green technology such as solar heating and rainwater collection. • Becton was contracted to build 210 new public housing units, 497 new privately owned units and 15 new social housing units. • The resulting 442 public and 497 private units totals 939 dwellings on the estate in a public-private mix of 47:53. • The public housing tenancies, facilities and common areas are privately managed.
Key Features	• The State transferred public land to the developer for the purpose of demolishing the old public housing and constructing new public and private housing. • The cost of the transferred land was deducted from the total amount paid to the developer, with the subsequent sale of the private housing constituting part of the developer's return. • Non-profit housing company, Urban Communities, is contracted to provide: – Management of the public tenancies. – Management of the private tenancies as requested by owners. – Management of the owners corporation for the private investors and owner-occupiers. – Facilities management, including management of trust fund for maintenance work. – Management of common and community facilities and infrastructure. – Community-building activities.
Benefits	• The relative success of the Kensington Redevelopment Project is currently being evaluated in an implementation review by the University of Melbourne in partnership with DHS. However, actual and intended benefits of this project can be summarised as follows: – Lower maintenance costs including vacated maintenance, building and grounds maintenance. Furthermore, Kensington public housing residents are employed by Urban Communities to maintain common areas. – Leveraging of additional investment into the community from both the public and private sectors. – Lower crime rate, low police call out rates and a safer environment due to an immediate response and team approach to anti-social behaviour and safety issues. – An improved social mix with private dwelling accounting for 49 per cent of the dwellings – New public housing by type, size, form and design better fits the demand profile in Victoria and aligns to DHS objectives on the optimal housing mix – The 'place management model' implemented on this project aims to drive a partnership-driven, customer-focused approach to public and social housing.

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The Kensington redevelopment project

	– The architecture of the new buildings is noticeable for its lack of institutional design. – A more personalised approach to tenant relationships based on trust and respect with greater awareness of and responsiveness to tenants' housing needs.
Issues / challenges	• The private developer required an adequate return on investment. In the initial stages the returns to the developer were lower because the mixed private / public model was yet to be proven. By the middle stages, the returns had increased. • As mentioned above, a review of the project is currently being undertaken. More details on the issues and challenges of this project will be known as the project develops.

Primary Sources:

– *DHS and University of Melbourne Evaluation Methodology paper (December 2011)*

– *Media release, The Hon Wendy Lovell MLC, Minister for Housing, Minister for Children and Early Childhood Development (11 April 2012)*

8.3 Evaluation of model

Based on the evaluation criteria and framework outlined in section 5, we have undertaken an evaluation of the model as follows:

Table 8-3: Development Agreement evaluation matrix

Criteria	Rating	Description
Increase in supply	✓✓	Leveraging from land and / or transfer of legal title of stock can enable access to private financing. However, although newly developed properties are introduced to the social housing system, the increase in supply largely depends on the specifics of the deal and the proportion of private housing within the development.
Operational efficiency	✓✓✓	This model provides the opportunity for operational efficiency as responsibility for the community housing is transferred to the CHP.
Customer experience / quality	✓✓✓	As with PPPs, CHP developments provide tenants with new accommodation which is of superior quality to the ageing stock which currently dominates the public housing supply. The tenants' experience is also likely to improve as developments of this nature have a reduced concentration of social housing which enables more socially inclusive communities.
Flexibility to change	✓	As with PPPs, CHP development projects where title and / or land is transferred, may not provide significant flexibility for change,
Risk transfer	✓✓	This option transfers risk to the private and not-for-profit sectors. Subject to the level of commercial returns, the structure may require direct funding / subsidy and / or rental guarantee from the Government.
Financial statement impact	✓	Options that involve the transfer of title in the housing stock from Government to the non-government sector will generally result in a reduction in the asset base of the State. To the extent that such transfer is undertaken on a less than market value basis (as is commonly the case), this would usually result in a decrease in value of land and the properties being recorded in its Income Statement. The ultimate accounting treatment will be influenced by the degree of transfer of the majority of risks and rewards and an assessment of whether the State controls the stock through managerial involvement usually associated with ownership.

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Criteria	Rating	Description
Ability to leverage	✓✓	The transfer of legal title to the stock should enable the private sector to access private sector finance to fund increase / replacement of stock. However, the current conservative borrowing conditions provide a limitation on the private sector's ability to fully leverage the assets.
Tax / subsidies impact	✓✓✓	GST concessions may be available to CHPs to reduce GST costs on construction and operational expenses. Exemptions from Victorian duty should be available on the transfer of housing stock to CHPs. Exemptions from land tax may also be available to the CHPs. Similar to Development Model 1, care should be taken to ensure that the 'tax preferred use' rules are not triggered, as this may impact upon the pricing and feasibility of private sector contributions. The Private Sector SPV may also be ineligible to claim GST credits and may incur Victorian duty.
Contractual complexity	✓✓	The contractual complexity of this model is, from a State perspective, moderate to low due to the limited need for ongoing contractual arrangements to ensure service provision.

Summary of evaluation

The experience of not-for-profit, socially oriented organisations undertaking market activities in Australia is not new and was considered by the Henry Review of the Future of Australia's Taxation System and the Productivity Commission review of the contribution of the not-for-profit sector. The key issues have concerned the impacts that commercial activities have on competitive neutrality and the overall charitable status of organisations and their associated taxation exemptions. Currently, if an entity's purpose is solely charitable, it can take other activities that are purely incidental to, and in advancement of, its charitable purpose, including commercial activities.

The current consideration of the taxation regime that applies to not-for-profit organisations includes whether commercial activities undertaken by not-for-profit organisations should affect their tax exempt status. The Productivity Commission has also considered whether there are unnecessary impediments for the not-for-profit sector, and to examine the tax treatment of the sector and the impact of current arrangements on competitive neutrality.

In summary, this model provides for a range of benefits including operational efficiency, access to private finance and the ability to utilise commercial profit streams as a means to funding community housing operations. The potential changes to taxation may, however, impact on the ability to fully benefit from such commercial proceeds

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Transfer Models

involve the transfer to the non-government sector of responsibilities related to the ownership, management and / or operation of the public housing stock

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9 Transfer Model 1 – Community Housing Stock Transfer

9.1 Outline of model

This model involves the transfer of legal title and / or other rights over the State's capital stock to the CHPs. The value of this stock and its appearance on the balance sheet of the CHP allows the acquisition of new properties from any net positive cashflow and borrowings secured against the value of the transferred (and new) assets. The CHP typically provides eligibility assessment, allocation of housing, tenancy management and lifecycle maintenance.

In some instances a charge on the title may be included which restricts the sale of the property without the consent of the State. Nevertheless, it is generally understood that CHPs which fully own the assets are in a more effective position to integrate asset management and housing procurement with their corporate directions and planning processes. These organisations are better able to manage and reconfigure their housing portfolios in response to changing client needs and investment opportunities through a combination of sale and acquisition or redevelopment, disposing of poorly performing and / or unsuitable stock where appropriate.

In this model, the value of the capital stock transferred appears as an asset on the CHP's balance sheet. The CHP can then secure finance against the value of the existing properties using the positive net operating cashflow from operations to "leverage" and therefore procure or develop new dwellings. The free cashflows are generated from a rent model that charges an income based rent and attracts a rent subsidy from the Commonwealth – i.e. CRA. In some instances there may also be a capital contribution from Government (e.g. a capital subsidy to address the maintenance backlog or otherwise support the arrangement).

From the Victorian Government's perspective, the key advantage of this model is that it provides for the properties to continue to be used for social housing, creates 'growth' through leverage and removes certain costs associated with Government ownership – namely maintenance and asset renewal.

In order to ensure appropriate standards of service delivery, a regulatory framework is required. However, it is noted that this framework is already established in Victoria.

The commercial structure of this model is presented in Figure 9-1.

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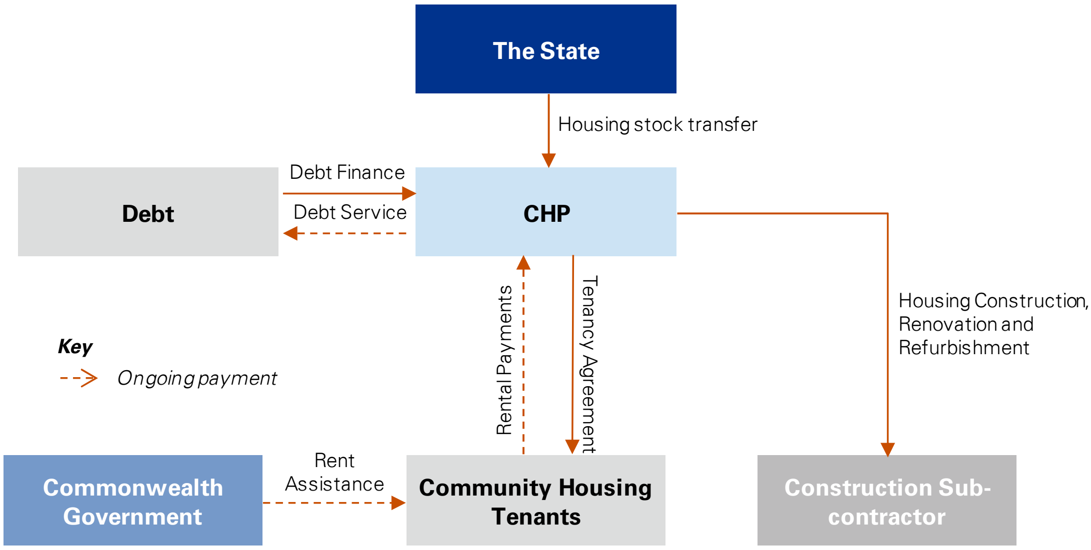
Figure 9-1: Commercial structure of the CHP Stock Transfer model



The key features of this commercial structure are presented in Table 9-1 below:

Table 9-1: Key features of the CHP Stock Transfer model

Commercial Structure Features	Applicability to Model
Title transferred to private sector	Yes
Residual land value risk allocated to private sector	Yes
Contractual term	Contract permanently transfers freehold ownership of the housing stock to the private sector
Responsibility for operations transferred to private sector	Yes
Responsibility for maintenance transferred to private sector	Yes
Direct increase in supply of housing stock	Yes (via the ability to 'leverage' the value of the transferred properties into new stock)
Utilisation of private sector finance	Yes
Nature of the housing stock	Existing and New

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9.2 Case study

Table 9-2: Victoria CHP Stock Transfer case study

Victoria CHP stock transfer

Location	Victoria, Australia
Description	• In 2007–08, 1,152 State-owned community housing units across a range of former programmes were converted to Housing Association arrangements, with ownership vested in registered housing agencies.
Key Features	• Housing associations were already managing the properties transferred from the State, so were already receiving the rental income. • Ongoing liability for maintenance and other ownership costs of the housing stock were also transferred to the housing associations, with a number of transferred properties requiring extensive maintenance. • Under the title transfer arrangements, all transferred capital properties could be used as security for financing purposes. • The State's expectation was that the associations would expand their portfolios by a minimum of 15 per cent of the value of the properties transferred by leveraging off the transferred properties.
Benefits	• A number of CHPs utilised the transferred stock to leverage other sources of finance and to generate their own growth over time. • Tenant survey reports in Victoria show a high level of dissatisfaction with the quality of public housing conditions and maintenance compared to that of community the housing sector.
Issues / challenges	• There was no evidence to suggest that the leveraging rationale for transferring ownership was realised with housing associations not delivering the required 15 per cent leverage on assets transferred within the required time frame by June 2010. In addition, only three of eight CHPs used the transferred assets as security for their borrowing requirements. • There is concern that the leveraging benefits of stock transfers will not play a major role in the provision of additional housing in the short to medium term if the stock transfers do not occur quickly enough or on a large enough scale. • Depending on the stock transferred, there may be a perception that the State is 'outsourcing the backlog' problem to CHPs by transferring housing stock that is predominantly aged stock.

Primary source: DHS Annual Report (2007-08)

9.3 Evaluation of model

Based on the evaluation criteria and framework outlined in section 5, we have undertaken an evaluation of the model as follows:

Table 9-3: Stock Transfer evaluation matrix

Criteria	Rating	Description
Increase in supply	✓	Leveraging the transferred housing stock provides a moderate capability to increase the housing supply. In addition, it is likely that the benefits of leveraging would take a number of years to materialise.
Operational efficiency	✓✓✓	This model provides the opportunity to achieve improvements in operational efficiency through private sector provision of services. The ability to leverage into new stock further increases the ability to achieve efficiencies.

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Criteria	Rating	Description
Customer experience / quality	✓✓	Customer satisfaction surveys by the Australian Institute of Health and Welfare (AIHW) show that community housing tenants have a higher level of satisfaction with their property than those residing in public housing.
Flexibility to change	✓	Since legal title is transferred to the CHP, there is only limited flexibility to change.
Risk transfer	✓✓✓	As the legal title on ongoing responsibility for housing is transferred, this option transfers all risks to the non-government entity.
Financial statement impact	×-✓	Options that involve the transfer of title in the housing stock from Government to the non-government sector will generally result in a reduction in the asset base of the State. To the extent that such transfer is undertaken on a less than market value basis (as is commonly the case), this would usually result in a decrease in the value of land (i.e. a de-recognition from the State's balance sheet) and the properties being recorded as a loss on disposal in the State's Income Statement. This is subject to the transfer of the majority of risks and rewards to CHPs and no managerial involvement of the State going forward.
Ability to leverage	✓✓	The transfer of legal title to the stock should enable the private sector to access private sector finance to fund the increase / replacement of stock. However, the current conservative borrowing conditions provide a limitation on the private sector's ability to fully leverage the assets.
Tax / subsidies impact	✓✓✓	The tax status of CHPs provides for taxation benefits both in relation to construction and operation to be achieved. Relevantly, GST concessions may be available to CHPs to reduce GST costs on construction and operational expenses. CHPs may also be eligible for Victorian duty and land tax exemptions.
Contractual complexity	✓✓	The contractual complexity of this model is moderate to low due to the limited need for ongoing contractual arrangements to ensure service provision.

Summary of evaluation

In summary, this model is perceived as positive in relation to its ability to achieve risk transfer, operational efficiency, ability to leverage, access to tax efficiencies and the overall increase in the volume of quality housing. However, this is partially offset by the accounting write down in asset value and the impact on the Government's financial statements.

Subject to the nature of the assets transferred and the scale of such transfers, there is some evidence to suggest that the overall impact on supply will be limited. The approach to stock transfers that has been employed in Victoria and Australia to date indicates that incremental transfers are unlikely to drive economies of scale or significantly increase supply. However, an option where a large volume of stock is transferred to the non-government sector has significantly greater potential to provide an increase in the volume of quality social housing.

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10 Transfer Model 2 – Shared Equity / Ownership

10.1 Outline of model

What is shared equity / ownership?

Shared equity (often used interchangeably with shared ownership) aims to assist social housing tenants with low to moderate income to purchase a share in the property they currently occupy.[77]

A shared 'equity' scheme involves tenants purchasing a minimum share of the property (in many instances this equates to no less than 60-70 per cent share of the property value) or a larger share depending on the tenant's capacity to afford a larger share.

The remaining share of the property will be owned by the State Government and / or a CHP. Tenants are not charged rent for the use of the remaining share of the property under a shared equity scheme.

A shared 'ownership' scheme is slightly different in that tenants make repayments on the mortgage component and pay rent on the remaining portion owned by the State Government and / or CHP.

Shared ownership is generally regarded as an early approach to shared equity, reflecting policies aimed at providing public housing tenants opportunities to own a part-share in their property while paying rent on the remaining share. Funds released through owning a part-share in the property may then be used to fund new social housing to be sold on a part-share basis to other selected target groups.

Shared ownership enables tenants to gain from market growth, as is the case with shared equity mortgage arrangements, but also provides a mechanism for minimising the need for a subsidy and preserves general affordability in the property.

Upon the sale of properties where the value has increased, a proportion of public subsidy may be recouped for reuse in subsidised programmes. However, capital gains can be seen to accrue disproportionately to the tenant at the expense of achieving a 'fairer share' of that initial subsidy to help preserve ongoing affordability or 'community equity'.

It is possible for the returns of private equity partners to be increased via subsidies, tax concessions, and similar mechanisms implemented by government. Such incentives may be offered through individual homebuyers, or to developers undertaking multi-unit or estate developments.

What are the objectives of shared equity?

In broad terms, a shared equity scheme aims to:

- Provide opportunities for **home ownership** for social housing tenants.
- Provide flexibility for housing providers to more effectively **target housing** towards high-need tenants.
- Release funds and assets to facilitate **increased supply** through refurbishment of existing stock, acquisitions and / or construction of new stock.

Shared equity schemes may reduce the up-front costs facing aspiring first homebuyers and enable potential first-time buyers to enter the market.

[77] Whilst DHS has existing shared equity schemes that are currently being would up, the models discussed in this section are differentiated in a range of ways and are therefore not directly comparable.

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How does a shared equity scheme work?

A shared equity scheme generally involves an agreement between the State Government and / or CHP and a social housing tenant (the applicant).

This agreement will reflect specific shared equity policy parameters which may vary across jurisdictions.

Where applicants require third party finance to purchase a share of the property, applicants will need to satisfy the lending criteria of the finance provider in order to secure finance to purchase a share of the property.

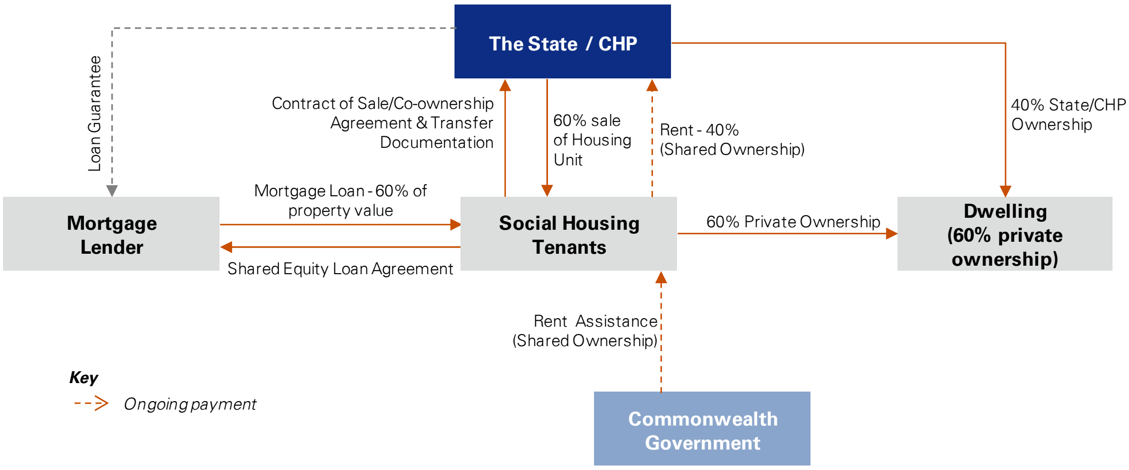
In some instances, a shared equity mortgage provider may be appointed / nominated by the State Government / CHP pursuant to consumer credit provisions on a jurisdiction by jurisdiction basis, whereby:

- Security by way of a mortgage may be taken over the property or loan guarantee provided for the equity mortgage; and / or
- The applicant may pay reduced interest on funds borrowed during the term of the mortgage agreement; and / or
- The lender may be entitled to a percentage of any increase in property value during the term of the mortgage agreement.

Applicants are generally not eligible for a shared equity loan if they are assessed as being capable of affording to borrow 100 per cent of the property value.

The commercial structure of this model is presented in Figure 10-1 below:

Figure 10-1: Shared Equity / Ownership model



The key features of this commercial structure are presented in Table 10-1.

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Table 10-1: Key features of the Shared Equity / Ownership model

Commercial Structure Features	Applicability to Model
Title transferred to private sector	Yes (partially)
Residual land value risk allocated to private sector	Yes (partially)
Contractual term	Until sale of property
Responsibility for operations transferred to private sector	No
Responsibility for maintenance transferred to private sector	Potentially (depending on the specifics of the arrangement)
Direct increase in supply of housing stock	No – however, an indirect increase can be achieved via the re-investment of sale proceeds into new / replacement stock
Utilisation of private sector finance	Yes (on the basis that the purchase proceeds are financed by private finance)
Nature of the housing stock	Existing

The size of an applicant's share of the property and shared equity mortgage and repayments may be determined by a number of factors:

- The fair market value of the rental property.
- An applicant's current and expected future income and costs of living.
- The amount of the deposit paid by the applicant and the cost of funds (prevailing interest rate).

Under a shared equity mortgage agreement, repayments may not be more than a minimum share of a tenant's income (in most instances this equates to no more than 30 to 35 per cent of an applicant's gross household income).

Repayments may be calculated on a case-by-case basis depending on the amount borrowed, prevailing interest rates and costs of living.

Can tenants increase their share in the property?

A key difference between shared ownership and shared equity arrangements reflects the parties' ongoing interest in the property at the time of sale.

As with shared equity schemes, shared ownership traditionally has enabled tenants to 'staircase' their equity share in tranches to outright ownership when they wished to, at a price based on market values at that time.

Staircasing is commonly used to describe the ability of purchasers to acquire further increments from the State Government / CHP under shared equity arrangements.

Minimum incremental amounts are typically stipulated (for example 5 per cent), and the cost of that increment will be at prevailing market values. Staircasing suggests that households may achieve an increased share in the property with the potential to 'step up' to full ownership over time.

Under a shared equity scheme, tenants are generally not able to borrow additional funds to finance renovations or home extensions or for personal use. Tenants may purchase additional shares in the property which may be achieved through increasing a shared equity mortgage.

Shared equity schemes are not intended to assist property investors and tenants must remain living in the property while the State Government and / or CHP owns a share of the property.

Tenants may sell the property subject to the specific terms of the shared equity scheme. In these circumstances the State Government and / or CHP would be entitled to claim the value of the share it owns in the property at the time of sale. This will include a share of any capital gain (or loss) realised at the time of sale.

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Table 10-2: Example (household income $60,000 per annum)

Initial property value	$300,000
Value of 1% share at time of purchase	$3,000
Amount able to borrow	$190,000
State Government share	$110,000
Deposit from savings	$2,000
Tenant's share of property (including deposit)	64%
Loan repayments*	$1,379 per month or $637 per fortnight

** Calculated on a standard variable home rate of 7.3% subject to variation)*

Table 10-3: What happens if the value of the dwelling increases?

Initial property value	$300,000
Sale price achieved for property	$350,000
Tenant share at sale	$224,000 (64%)
State Government share at sale	$126,000 (36%)
Value of 1% share at time of purchase	$3,000
Value of 1% share at time of ale	$3,500
Value of share increase in property at sale	$32,000 (tenants share of $50,000 value increase)

In this example the fair market value of the property has increased between the time of purchase to the time of sale by $50,000. The value of the tenant's share of the property at time of sale in this instance has increased by $32,000 and the value of a 1 per cent share at the time of sale is $3,500.

Table 10-4: What happens if the value of the dwelling decreases?

Initial property value	$300,000
Sale price achieved for property	$280,000
Tenant share at sale	$179,200 (64%)
State Government share at sale	$100,800 (36%)
Value of 1% share at time of purchase	$3,000
Value of 1% share at time of ale	$2,800
Value of share increase in property at sale	$12,800 (tenants share of $20,000 value decrease)

In this example the fair market value of the property has decreased between the time of purchase to the time of sale by $20,000. The value of the tenant's share of the property at time of sale in this instance has decreased by $12,800 and the value of a 1 per cent share at the time of sale is $2,800.

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What shared equity products exist in Australia?

There are a number of shared equity products that currently exist in Australia. These are essentially based on three parameters: maximum household income, maximum property value and maximum proportion of equity share that can be held by another partner.

Table 10-5: Shared equity products existing in Australia

Jurisdiction	Provider / Financier	Shared Equity Products
Australian Capital Territory (ACT)	DHCS (ACT Disability, Housing and Community Services), IMB Limited	The ACT Affordable Housing Action Plan
Queensland	Queensland Department of Housing	Pathways Shared Equity / Pathways Loan
New South Wales	No current providers	No current schemes
Victoria	Places Victoria / Burbank Homes	Ownhome
Western Australia	Keystart Home Loans	Step Up Scheme (from 2010, consolidating previous Goodstart, Access and Aboriginal Home Ownership schemes)
South Australia	HomeStart Finance	Breakthrough
Northern Territory	Territory Housing	Equity Start

Source: Australian Housing and Urban Research Institute, Issue 124 April 2010

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10.2 Case study

South Australia, Western Australia and the Northern Territory have continued to offer 'assisted' government loans and have been the most proactive in the development of shared equity initiatives.[78]

Table 10-6: Step up home ownership scheme (SUHOS) case study

Western Australia SUHOS

Location	Western Australia
Description	• SUHOS is run by Keystart, a government-backed agency. KeyStart is the Western Australian government's low-deposit scheme that was established as a statutory authority in 1989. Since then, it has helped more than 65,000 residents into homes in Western Australia, accounting for $6.8 billion in home loans. • The GoodStart shared-equity loan scheme was specifically designed to provide an affordable process for Department of Housing and Works (DHW) public housing tenants to purchase equity in their current rental property. • SUHOS is a shared equity home loan scheme that in 2010 consolidated the following three previous schemes: – Aboriginal Home Ownership – Access – Goodstart • SUHOS is designed to help low to moderate income first homebuyers into home ownership and is targeted at: – Aboriginal and Torres Strait Islander people – People with permanent disabilities – DHW public housing tenants – Sole parents looking to retain their family home • Under SUHOS, eligible first home buyers may purchase or build a home in conjunction with Keystart and the Department of Housing.
Key Features	• Depending on the income and household size of the buyer, the Department of Housing will co-own up to 40 per cent of the property with applied conditions. Later, when the buyer can afford it, they can purchase all or part of the Department of Housing's share. • The scheme provides an affordable process for public housing tenants to purchase equity in their current rental property. To qualify, the applicant must: – Be a current Department of Housing tenant and have income within the eligibility limits of the scheme. – Be over 18 years of age. – Not have any debts owing to the Department of Housing or Keystart. – Have a satisfactory rental and credit history. – Be able to demonstrate the capacity to meet the required repayment. – Not own or part-own another property or land in Australia. – Not be currently bankrupt or discharged from bankruptcy within 2 years of the date of the application. • Applicants on the public housing waiting list or those who are eligible to apply for the list can also benefit from the scheme and purchase 70 per cent or more equity in refurbished ex-rental public housing properties in selected areas. • The SUHOS loan has the following features: – Maximum property value $412,000 ($500,000 in some areas)

[78] Whilst DHS has existing shared equity schemes that are currently being would up, the models discussed in this section are differentiated in a range of ways and are therefore not directly comparable.

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Western Australia SUHOS

	– Low deposit, $2,000 or 2 per cent of the purchase price (whichever is greater) – The FHOG can be used towards both the deposit and fees – No lenders mortgage insurance and account keeping fees – The maximum income limits depend on the family situation (e.g. number of dependents) and varies between $60,000 and $80,000 • The Department of Housing does not charge rent or interest on the portion of the property it co-owns. • The buyers become responsible for all outgoings such as rates and maintenance on the property. The Department of Housing does not contribute towards these costs. • Buyers are able to increase their ownership in the property whenever they can afford it. However, at any one time, a minimum of 5 per cent equity must be bought and statutory fees and charges apply. As an incentive for borrowers to own as much of the property as soon as possible, stamp duty concessions apply on the share being purchased from the Department of Housing if it is bought within 10 years of the initial purchase. • If the buyer wishes to sell the property, a valuation will be conducted to determine the current market value and minimum sale price. • The Department of Housing has the first option to purchase the property but if it does not take up this option, the buyer can sell the property on the open market. • On sale, any capital improvements made to the property since the initial purchase is credited to the buyer and taken into consideration when calculating the value of the Department of Housing's share of the sale price.
Benefits	• SUHOS has provided a response to growing housing affordability constraints in Western Australia. • SUHOS has not only provided assets for the buyers, but has also provided buyers with guaranteed security of tenure. • In particular, KeyStart is seen as a viable, profitable and longstanding intermediary assisting lower income households enter and sustain homeownership. • KeyStart has been able to access funds at favourable rates, borrowing funds from the WA Treasury Corporation and issuing paper to sell-on their debt to the markets. They issue term fixed rate funds, and then swap these into floating arrangements, which enables them to take advantage of spreads against the bank base rate.
Issues / challenges	• SUHOS takes account of circumstances of negative equity where parties to the agreement share the loss if property values fall and the value of the property becomes less than the purchase price. • Although working with financial markets through the Treasury Corporation, Keystart is bound by the extent to which Treasury is willing to respond to demand and lift borrowing limits. • Given the underlying demand for social housing, shared equity arrangements have limited scope and scale and can therefore only be positioned as one of a range of options. • The shared equity sector could potentially benefit from private sector involvement and innovation. However, clear policy direction will likely be required before the private sector focuses on product development in this sector. • Shared equity schemes are yet to get a substantial track record in Australia's eastern states. This is partly because of negative experiences with some low start loans schemes in the early 1990s.

Primary sources:
- *Australian Housing and Urban Research Institute (AHURI) Final Report No. 137 (2009).*
- *The KeyStart 'Products' web page: http://www.keystart.com.au/Products_Metro2.php (accessed on 30 March 2012)*
- *AHURI Bulletin, Issue 124 April 2010*

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10.3 Evaluation of model

Based on the evaluation criteria and framework outlined in section 5, we have undertaken an evaluation of the model as follows:

Table 10-7: Shared Equity / Ownership evaluation matrix

Criteria	Rating	Description
Increase in supply	✓	Relative to the scale and scope of existing schemes, the reinvestment of sales proceeds into new housing stock provides limited potential to increase supply.
Operational efficiency	×-✓✓✓	In itself, this model does not provide for any increase in operational efficiency. However, if combined with a transfer to a CHP this would enable efficiencies as with other models discussed above.
Customer experience / quality	✓	With the 'pride of ownership' that is associated with shared equity schemes, the tenant is encouraged to take better care of the property which has the potential to improve the tenant's experience. However, it is existing housing stock that is sold to tenants which provides little scope for significant improvement.
Flexibility to change	✓	Since legal title is transferred to investors, only a limited flexibility for change is provided under a shared equity agreement.
Risk transfer	✓	This model transfers a level of risk in relation to movement in property values to tenants. However, as the Government remains a partial owner of the asset, a level of this risk remains. This could be mitigated in the event that title and responsibility for the asset is transferred to a CHP.
Financial statement impact	✓-✓✓	It is difficult to assess the financial statement impact of this option as it depends on many variables including the level of ownership by Government and whether responsibility for assets is transferred to a CHP. In general, although the legal title transfers to the purchaser, Government would retain a significant risk in relation to the illustrative 40 per cent equity interest i.e. it is exposed to the market price in relation to 40 per cent of the value of the property to be obtained through a future sale. Reducing Government equity interest to 10 per cent or below would result in de-recognition of the underlying properties from its balance sheet as the level of risk would be considered insignificant.
Ability to leverage	✓	This model provides for a level of leverage as a result of the direct borrowing by the tenant. The proceeds from this leverage can be used by Government or the CHP to re-invest in additional housing stock
Tax / subsidies impact	×	The tenant will be liable for duty on the portion of the housing acquired, although FHOG could be made available to offset the duty. Any future increase in equity by the tenant will attract further duty. Sale of units wjthin 5 years of construction / substantial renovation may have a net GST cost to the Government.
Contractual complexity	✓	The level of contractual complexity is medium to high. Lenders have developed a wide spectrum of mortgage products in recent years: including more flexible products; a wider spectrum of products to reflect different credit histories; interest-only, reduced deposit requirements; and family contributions are all ways in which the traditional financial has adjusted to 'the squeeze'.

Summary of evaluation

In summary, this model provides moderate benefits against most criteria. However, if combined with a transfer to a CHP this model could enable the operational efficiencies associated with CHP management of dwellings.

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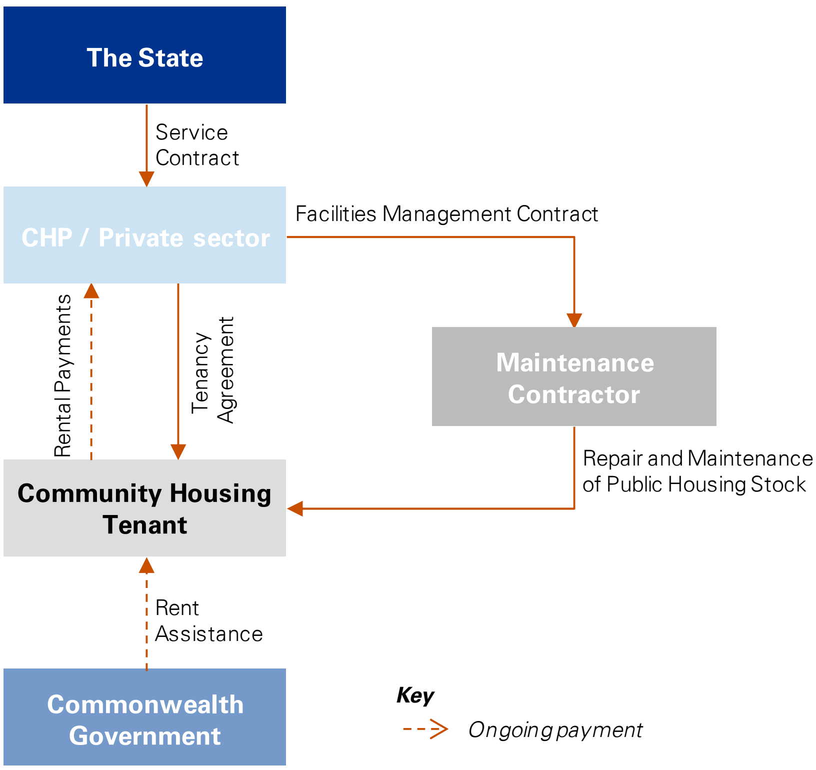
11 Transfer Model 3 – Outsourcing Maintenance / Management

11.1 Outline of model

The outsourcing of O&M option involves drawing on the services of non-government organisations (for example the not-for-profit sector or private sector) for the maintenance of the existing public housing stock. These organisations will deliver operations including tenancy arrangements, administration, relocation, communication and consultation, as well as maintenance and repairs. This model does not involve the creation of new stock or replacement of stock. However, cost savings from efficient operations can be used to invest in additional housing stock.

The commercial structure of this model is presented in Figure 11-1 below:

Figure 11-1: Commercial structure of the O&M Outsourcing model



The key features of this commercial structure are presented in Table 11-1.

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Table 11-1: Key features of the O&M Outsourcing model

Commercial Structure Features	Applicability to Model
Title transferred to private sector	No
Residual land value risk allocated to private sector	No
Contractual term	Opportunity for shorter term contracts (≈ 5-10 years)
Responsibility for operations transferred to private sector	Yes
Responsibility for maintenance transferred to private sector	Yes
Direct increase in supply of housing stock	No
Utilisation of private sector finance	No
Nature of the housing stock	Existing

As can been seen in the diagram and table above, ownership of the housing stock is retained by the Government with operational and maintenance responsibility transferring to the CHP. The CHP is the primary contact for the State and their role is focused on property and tenancy management, with maintenance and repairs likely to be outsourced by the CHP to a facilities management subcontractor.

Outsourcing can take different forms and the greater the degree of collaboration, risk transfer and length of contract, the greater opportunity there should be for cost savings and improved operational outcomes. The three main outsourcing models are described in Table 11-2 below:

Table 11-2: Three types of outsourcing for social housing

	Type of Outsourcing		
	Traditional	**Collaborative**	**Transformational**
Overview	• Activity based arrangement	• End-to-end management and process improvement	• End-to-end management and process improvement • Whole asset transfer / collaborative asset management
Roles	• Provider undertakes activities prescribed by the Government (i.e. specific maintenance task on certain properties – e.g. boiler replacement) • Government manages demand and end-users	• Government / Provider agree inputs, activities and outputs • Joint management of demand and end-users	• Government / Provider agree outputs (i.e the service level to be attained - based on Key Performance Indicators) • Provider decides inputs and activities • Provider manages demand and end-users
Performance Management	• Extensive set of performance indicators (PIs), mostly input-based	• Broad set of performance indicators (PIs), some output-based	• Smaller set of key performance indicators (KPIs), mostly output-based
Typical contract length	3-5 years	5-10 years	10 years +
Contractual flexibility	Low	Medium	High
Relationship	Often adversarial	More collaborative	Open and trusting
Cost of contract management	Medium	Medium / Low	Low

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	Type of Outsourcing		
	Traditional	**Collaborative**	**Transformational**
Costing	• Cost per activity	• Cost per activity • Some additional contractual sophistication to minimise perverse incentives – e.g. pain / gainshare	• Agreed upfront cost for an agreed set of outputs over contract length • Sophisticated approach to incentives
Drivers of value	• Increased productivity of existing set of processes and activities	• Increased productivity through end-to-end process improvement and innovation • Collaborative relationship	• Increased productivity through end-to-end process improvement and innovation • Significant supplier investment in early years • Asset management with contractual incentives to improve asset value • Partnership approach; aligned vision and objectives
Risk transfer to provider	Low / Medium	Medium	High

Primary source: Credo Research Paper, June 2011

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11.2 Case study

Table 11-3: Victorian CHP outsourcing case study

The Victorian CHP outsourcing model

Location	Victoria, Australia
Description	• The DHS has implemented the Outsourcing Model in Victoria. • Under this arrangement, O&M of the public housing dwellings are outsourced to the CHPs via Lease and Property Management Agreements. • The Lease and Property Management Agreement is a standardised contract that replaced the multitude of individual agreement between DHS and the CHPs that existed before its introduction in 2007. • Whilst DHS retains legal title and ownership of the dwellings, a significant proportion of operating risk is transferred to the CHPs. • Under this framework, DHS is able to stipulate tenancy priority groups so that accommodation continues to be provided to those most in need. • DHS also stipulates the rental mechanism so that rents charged to tenants remain within affordable limits.
Key Features	• The CHPs enter into a 5-year lease arrangement with DHS to provide community housing services to public housing tenants. • At the CHP's own cost, its key responsibilities under the agreement are summarised as follows: – Tenancy management and rent collection. – Soft facilities management services, including cleaning, waste management, and landscape gardening services. – The CHP is broadly responsible for general repairs and maintenance. However, there are two options available to the CHP related to the degree to which it assumes these maintenance responsibilities. – The CHP must endeavour to ensure the dwellings are consistently occupied during the term and that sub-leases are offered to tenants who fall into the 'greatest need categories' specified by DHS (for example, sufferers of developmental or physical disabilities). – The CHP must also undertake at least one community capacity and building project per year which is intended to improve access to social housing, increase sub-tenant participation and decision making and improve outcomes for sub-tenants. • The DHS retains responsibility for lifecycle replacement and structural repairs of the properties. • The DHS is entitled to conduct performance reviews of the CHPs at any time during the contract term. • The CHP charges rent to tenants based on a Maximum Rent Formula stipulated in the agreement. This is broadly based on the accessible income, family tax benefits, CRA and threshold rents of the tenant. • The CHP must make the following payments as stipulated in the contract: – *Rent* under the head lease agreement. – *Maintenance Fund Fee* is intended to cover the cost of maintaining the properties and is only payable where the CHP opts for DHS to retain maintenance responsibilities. This fee is not payable if the CHP opts to assume maintenance responsibilities. – *Asset Management Fund Fee* is payable by the CHP in order to meet the cost of lifecycle replacement and structural repairs incurred by DHS. • The Maintenance Fund Fee and the Asset Management Fund Fee are reviewed annually for the term of the contract to reflect changes in the Consumer Price Index (CPI).

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The Victorian CHP outsourcing model

Benefits	• As there were similar but unstandardised contracts prior to the introduction of the Lease and Property Management Agreement, the key benefits have been administrative. Agreements between DHS and the CHPs in terms of roles and responsibilities are now standardised and therefore more manageable by DHS. • The Agreement's provision for an Asset Management Fund Fee means that DHS is able to fulfil its maintenance obligations in a financially sustainable manner which can assist in preventing maintenance backlogs. • The framework of these agreements allows DHS to exercise control over the CHP's tenancy admissions and stipulate the targeted tenant groups. This ensures that the CHP only offers sub-leases to the 'greatest need categories' of tenants. • In comparison to government managed housing, CHPs have typically shown themselves to be more responsive to the needs of a diverse range of tenants.
Issues / challenges	• Five years have passed since the introduction of the Lease and Property Management Agreement and as yet a review has not not been conducted. • Without a review, it is difficult to highlight issues and challenges of the Lease and Property Management Agreement as the operational and financial impacts of the Agreement has not been evaluated.

Primary source: DHS internal documents

11.3 Evaluation of model

Based on the evaluation criteria and framework outlined in section 5, we have undertaken an evaluation of the model as follows.

Table 11-4: O&M Outsourcing evaluation matrix

Criteria	Rating	Description
Increase in supply	✓	Due to the cost benefits associated with this model, operational efficiencies should enable re-investment of such savings into new stock. However, since the focus of this model is on existing stock, it does not provide for a significant increase of supply or replacement of stock.
Operational efficiency	✓✓	Underpinned by a commercial framework that rewards performance, the model has an ability to achieve operational efficiencies in excess of those achievable by the Government. However, as this model is focused on the management of existing stock, the full potential of non-State management is unlikely to be achieved.
Customer experience / quality	✓	Customer satisfaction surveys (AIHW) show that community housing tenants have a higher level of satisfaction with their property than those residing in public housing.
Flexibility to change	✓✓	Since only the operation and maintenance is transferred under this model (rather than full legal title as in other transfer models), the model provides for a reasonably high degree of flexibility.
Risk transfer	✓	All service delivery aspects of social housing such as tenancy and asset management can be transferred to a non-government organisation. The State Government retains other risks that will typically include components of political risk and land and asset value risk.
Financial statement impact	✓✓✓	Outsourcing O&M maintains the current accounting treatment of the housing stock with asset values therefore retained on the Government's financial statements.

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Criteria	Rating	Description
Ability to leverage	×	This model is ineffective at enabling the CHPs to borrow against the value of the underlying property or cash flows.
Tax / subsidies impact	✓	Same as Status quo. Without stock transfer to the CHPs, access to tax efficiencies is reduced. Notably, the leasing of housing units will not be GST-free as it is not provided by eligible persons. There may be some additional GST leakage as the Government will not be able to recover GST paid to the CHP / Private Sector under the Service Contract.
Contractual complexity	✓✓	Outsourcing O&M will involve a moderate level of contractual complexity.

Summary of evaluation

In summary, this model provides a range of benefits in relation to the achievement of operational efficiencies, the transfer of risk and the avoidance of adverse accounting impacts. However, as the model is focused solely on existing stock, it does not provide for a significant increase of supply or replacement of stock.

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Financing Models

involve mechanisms to achieve financial outcomes that do not provide a direct increase in supply but provide this indirectly via the achievement of financial benefits

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12 Financing Model 1 – Securitisation

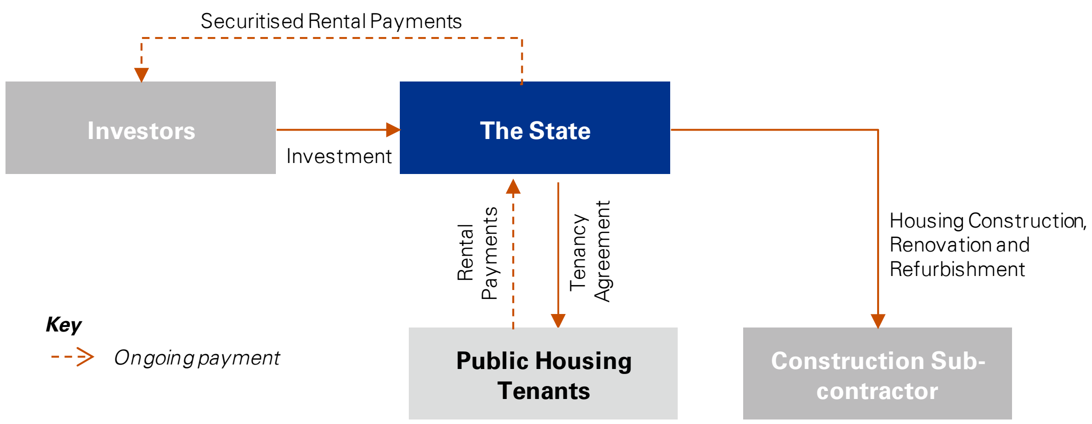
12.1 Outline of model

Securitisation is a form of financing that utilises future cashflow streams to repay debt issued to finance an investment in another asset. This model works by recognising and securitising the rental receipts from social housing tenants and the Government over an extended period. The proceeds from the securitisation can then allow for a greater investment in the housing stock.

In this model, the State may be required to directly pay, or otherwise guarantee the rental stream to the investors.

The commercial structure of this model is presented in Figure 12-1 below:

Figure 12-1: Commercial structure of Securitisation model



The key features of this commercial structure are presented in Table 12-1 below:

Table 12-1: Key features of the Securitisation model

Commercial Structure Features	Applicability to Model
Title transferred to private sector	No
Residual land value risk allocated to private sector	No
Contractual term	≈ 25-30 years
Responsibility for operations transferred to private sector	No
Responsibility for maintenance transferred to private sector	No
Direct increase in supply of housing stock	No – however, an indirect increase would be achieved via the utilisation of proceeds
Utilisation of private sector finance	Yes
Nature of the housing stock	Existing

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12.2 Case study

Table 12-2: Securitisation of state housing loans case study

Securitisation of state housing loans in Finland

Location	Finland
Description	• Social housing in Finland is financed either with state loans or interest subsidised commercial loans. • The Housing Fund of Finland (ARA) is a fund for social housing loans and is able to grant loans and approve interest subsidies for social housing. It also monitors the need for social housing and renovation, allocates grants, chooses the projects and carries out cost and quality control of state subsidised housing. • Traditionally, ARA financed its outlays via the following three sources: – The receipt of interest on its existing loans. – Appropriations from the Government budget. – Borrowing in its own name in the bond market. • The economic recession in Finland in the first half of 1990s led to rapidly increasing public debt and appropriations from government dried up after 1993. • In order to grant state housing loans, a new source of funding was therefore required during the 1990's. As there were considerable assets in the form of outstanding state housing loans for social rental housing in the Fund, the solution was to securitise them in order to provide a source of funds that could keep up the social housing production.
Key Features	• The ARA grants housing loans with the following attributes: – The loan covers a maximum of 90 - 95 per cent of building costs and price of the plot. – The loan term is approximately 35 years. – The debt service payments are index linked to CPI. • The first securitisation operation, via an SPV called Fennica I, was carried out in 1995. • Collateral is provided by loans issued at least three years previously, with credit risk diversified by ensuring that the pool has a geographic spread of loans, and a variety of loan sizes. • Risk was also reduced by taking loans with good payment records, loan-to-value ratios less than 95 per cent at origination, and from areas with low vacancy rates. • Credit enhancement is provided by a reserve fund of 1 per cent of the value of the loan balances. • The housing that is being financed is not state-owned.
Benefits	• By 2001, 6 Fennica operations had raised a total amount of €2.8 billion from securitising social housing loans. • It is believed that the securitisations have widened the investor base and provided the ARA with experience in raising a new form of financing. • The securitisations offered investors a new and highly rated alternative to government bonds and were favourably received by investors. • The funds from securitisation do not score as public expenditure as the SPVs are the borrower, rather than the state, and there is no state guarantee on the securities issued. • Since the housing being financed is not state-owned, the Housing Fund has maintained a programme of subsidised housing development without recourse to further public subsidy, with new state loans and interest subsidies financed almost entirely by loan repayments and securitisation.

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Securitisation of state housing loans in Finland

Issues / challenges	• Complicated to administer, both in terms of structuring and drawing up contracts. This criticism can be levelled at secured financing as much as securitisations in particular. • High fixed costs with more one-time expenses than normal borrowing. In addition to underwriting fees on bond sales, planning and developing the securitisation process will incur additional costs such as legal fees, advisor fees, and costs to obtain a credit rating.

Primary source: Securitizing Funds for Social Housing, Teuvo Ijas and Harri Hiltunen, no date

12.3 Evaluation of model

Based on the evaluation criteria and framework outlined in section 5, we have undertaken an evaluation of the model as follows:

Table 12-3: Securitisation evaluation matrix

Criteria	Rating	Description
Increase in supply	✓	Utilising the payment made by investors, this model has a modest potential to increase supply. An issue that should be noted is that future rental income is foregone, which could create future challenges in relation to future recurrent costs that need to be met.
Operational efficiency	✗	This model does not provide the opportunity to achieve improvements in operational efficiency.
Customer experience / quality	✗	Unless any financial benefits achieved by the model are used to invest in the improvement of the existing public housing stock (which is not the main purpose of this model), the tenants experience will not improve.
Flexibility to change	✓✓	Legal title and operational responsibility is retained by government providing a degree of flexibility.
Risk transfer	✗	This option is unlikely to transfer any material level of risk to the non-government entity. Securitisation may require the Government to directly pay, or otherwise guarantee the rental stream.
Financial statement impact	✓✓-✓✓✓	Depending on the structure of the securitisation, there are a number of effects on the public sector financial statements in relation to a financial and rental income stream, which have to be carefully considered. It is likely that the properties will remain on Government's balance sheet.
Ability to leverage	✓✓	Securitisation can lead to higher leverage than traditional mortgage bank financing as higher loan to value ratios can be achieved, particularly where the investor base is sourced from the capital markets. In addition, due to the transaction structure, the overall interest rate could be lower than for traditional mortgage loans.
Tax / subsidies impact	✓	Without any transfer of housing stock, this model does not provide for the receipt of tax efficiencies. There may be some additional GST cost as the Government will not be able to recover full GST on expenses associated with the securitising of rental receipts.
Contractual complexity	✗	The contractual complexity of issuing securitised products and underwriting revenue is likely to be significant.

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It should be noted that if securitisation of public housing rentals was to occur, the potential variability of this revenue stream (due to revenue being set as a percentage of household income), may create some challenges and / or a requirement for a revenue floor.

A variant of the model is also available in which the securitisation is of rental to be received by a non-government entity. This variant is more similar to the above noted case study and would have a range of alternative advantages and disadvantages.

Summary of evaluation

While this model enables the net proceeds of the securitised rental payments to be invested in an increase in stock, there is a significant complexity to the arrangements. Furthermore, as rental income is foregone during the securitisation period, there is a need for future funding in order to be able to meet future recurrent costs. However, it should be noted that unlike the sale and leaseback model, ultimate ownership of the assets is retained, which may avoid certain negative accounting treatments. The use of this model in combination with other models (such as stock transfer) would result in a variety of alternative advantages and disadvantages.

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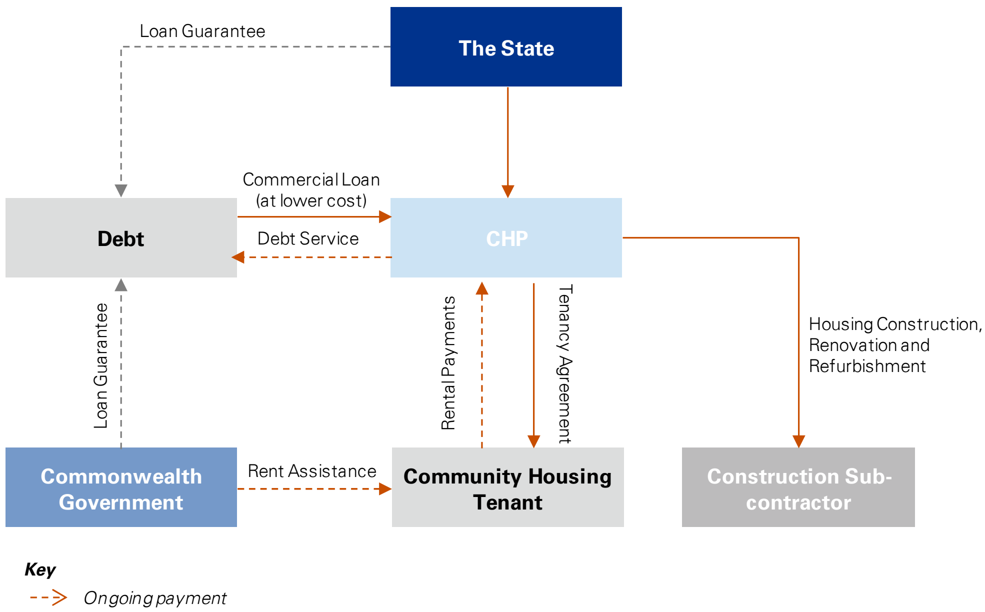
13 Financing Model 2 – Loan Guarantees

13.1 Outline of model

The commercial structure of this model involves the State or Commonwealth Government guaranteeing loans provided to CHPs by commercial lenders. The high credit rating of the State and / or Commonwealth Governments means that the Government guarantee reduces the risks to the financial institutions. This lower risk profile enables more favourable borrowing terms to be achieved. This ultimately enables an increased borrowing potential and freeing up of capital to allow for a greater investment in housing stock.

The commercial structure of this model is presented in Figure 13-1 below.

Figure 13-1: Commercial structure of the Loan Guarantee model



The key features of this commercial structure are presented in Table 13-1 below:

Table 13-1: Key features of the Loan Guarantee model

Commercial Structure Features	Applicability to Model
Title transferred to private sector	No – although this option can be combined with other models
Residual land value risk allocated to private sector	No – although this option can be combined with other models
Contractual term	Loan life
Responsibility for operations transferred to private sector	No – although this option can be combined with other models
Responsibility for maintenance transferred to private sector	No – although this option can be combined with other models
Direct increase in supply of housing stock	No – although indirectly the increase in borrowing should enable a greater investment in housing stock
Utilisation of private sector finance	Yes
Nature of the housing stock	Existing

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Government guarantees can free-up capital and allow the CHP to access greater levels of finance that could support an expansion of services offered, particularly in relation to tenancy management functions, but more critically in relation to the supply of housing.

Unlike options that involve title transfer, this model is a more direct avenue for property owners to access funding and negotiate with banks for more favourable terms. It is also the case that financial institutions, particularly in relation to social housing loans, are more concerned with the ability of an owner to make repayments rather than exercising their right to take control of an asset in the event of default.

However, consideration should be given to the potential administrative costs to government of providing loan guarantees, which may include:

- The potential future cost of any providers failing and the Government needing to meet that liability, as well as a higher level of regulation of housing providers to mitigate this risk and increase certainty that providers and projects are viable and therefore guarantees will not be called on.
- The cost of any additional government subsidies that could be required to make entities or projects sufficiently viable for private investors or to minimise the financial risks to government of providers failing.

13.2 Case study

Table 13-2: Loan Guarantee case study

Loan Guarantee model: the Netherlands

Location	The Netherlands
Description	• Housing associations in the Netherlands focus on providing respectable and affordable housing for low to middle income households (those unable to access housing in the private market). • At present, no publicly funded housing supply programmes exist in the Netherlands. • Guaranteed loans have therefore become a mechanism with which housing associations are able to develop and maintain the supply of social housing.
Key Features	• These guaranteed loans are provided by a financial institution, but are backed by the national Social Housing Guarantee Fund which is funded by fees from social landlords and supported by central and local governments. • The Fund has a AAA credit rating, allowing housing associations to access financing at reduced interest rates. • The guaranteed lending is used for the development of new social housing and the refurbishment of existing housing. • The Government is required to provide unrestricted interest-free loans to replenish the Fund's capital when requested. The Government must, however, utilise the committed capital from participating housing associations to fulfil this requirement. • Banks are offered triple underwritten guarantees on loans by the Fund, backed by the central government, local governments and the stock of the sector. • To be eligible for a loan guarantee, housing associations are evaluated against the Fund's assessment criteria, which involves examining the following: – The project development and regeneration policies and strategies relative to the actual performance of the association. – The housing association's stock management practice and conformity to capital adequacy requirements. • The majority of loans are obtained from two public institutions, the Bank Nederlandse Gemeenten and Nederlandse WaterScahapsbank, which specialise in providing private finance to the social housing sector.

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Loan Guarantee model: the Netherlands

	• For those associations in financial difficulty or that do not meet the requirements necessary to obtain the Social Housing Guarantee Fund, the Central Housing Fund provides financial assistance. • The Central Housing Fund is financed by mandatory fees paid by housing associations and provides interest-free loans or lump-sum payments to housing associations, as well as implementing agreed re-organisation plans. • For both the Social Housing Guarantee Fund and the Central Housing Fund, the Government stipulates that social landlords finance new construction with capital-market loans and their own resources. • The income-generating capability of housing associations has been inhibited by various political measures, including the following: – Homes are to be allocated to low income households and increases in rent have been restricted to the level of inflation. – A corporate tax and a regeneration levy have been introduced by the central government. • Government regulations permit housing associations to do the following: – Deliver high-rent or owner-occupied housing. – Provide dwellings for target groups other than those on low incomes. – Sell dwellings (with sales proceeds often driving the social landlord's reinvestment strategies).
Benefits	• The Social Housing Guarantee Fund has been cost effective and influential in the improvement of access to credit markets for approved social housing developments. • Coverage of the loan guarantee scheme has been high, with 80 per cent of loans in the housing sector guaranteed by the Government. • The risk is shared between parties with a vested interest in the financial stability of autonomous housing associations. • The Social Housing Guarantee Fund has been an essential component of social housing development in the Netherlands recently, particularly as banks are reluctant to provide long-term credit.
Issues / challenges	• There is no reduction in rent under the Loan-Guarantee model, as there is no prescribed and regulated relationship between cheaper finance and lower rental prices. • The model is not necessarily equitable, as the guarantee of the Social Housing Guarantee Fund only applies to dwellings under a prescribed cost limit. • The strategy in place in the Netherlands is largely dependent on the publicly funded foundations of the past. • The importance of cost savings associated with Loan-Guarantee models should be considered in the context of increasing construction costs in the Netherlands. This has been accentuated by the introduction of new standards to reduce carbon dioxide emissions.

Primary source: Gilmour, T., Lawson, J. & Milligan, V. International measures to channel investment towards affordable rental housing. Australian Housing and Urban Research Institute, May 2010.

13.3 Evaluation of model

Based on the evaluation criteria and framework outlined in section 5, we have undertaken an evaluation of the model as follows:

Table 13-3: Loan Guarantee evaluation matrix

Criteria	Rating	Description
Increase in supply	✓	The reduced cost of finance should provide an ability to achieve an increase in the level of supply. However, subject to the size of the arrangements, this would at least partially be offset by administrative costs.

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Criteria	Rating	Description
Operational efficiency	✗	This model does not provide the opportunity to achieve improvements in operational efficiency.
Customer experience / quality	✗	This model will have a negligible impact on the experience of tenants and the quality of housing.
Flexibility to change	✓✓	Legal title is retained by government which provides a degree of flexibility. However, operational responsibility is transferred to the CHP which detracts from the Government's ability to adapt to change. Furthermore, the cost to government of guaranteeing the loans could tie up capital that might have been used for other purposes, which inherently detracts from the model's ability to provide a flexible solution.
Risk transfer	✗	This option fails to transfer any risk to the private and not-for-profit sectors. Indeed, loan guarantees would require the Government to accept credit risk of the CHPs. Currently, this risk is absorbed by the CHPs themselves and is reflected in a higher cost of finance in relation to their commercial loans.
Financial statement impact	✓✓	Depending on the structure and scale of the loan guarantee arrangement, there is likely to be some impact on the public sector financial statements. For example, payments to compensate lenders in the event of CHP default will need to be accounted for. In addition, in some circumstances the terms of the guarantee may require a provision in the accounts. The properties are expected to remain on State's balance sheet (unaffected by the transaction).
Ability to leverage	✓✓	This model provides for an increased ability to leverage and therefore invest in additional housing stock. However, the level of additional investment is likely to be modest as the debt is still prima facie required to be serviced by the CHP.
Tax / subsidies impact	✓	This model is substantially similar to the Status quo as there is no transfer of housing stock. There may, however, be some additional GST leakage on expenses associated with the commercial loan.
Contractual complexity	✓✓	With the Government effectively acting as an intermediary between lenders and CHPs, a moderate level of contractual complexity is likely to exist in order to align the interests of all parties involved.

Summary of evaluation

The key advantage of a loan guarantee scheme is that it is an effective mechanism for improving lending terms between CHPs and commercial banks and therefore lowering the cost of finance to CHPs.

However, research suggests that the cost savings that will be achieved by CHPs will only have a limited effect on their ability to increase the supply of community housing. A 2010 KPMG Report for the Department of Families, Housing, Community Services and Indigenous Affairs (FaHCSIA) found that over a 5-year period, the number of dwellings may increase by approximately 1.1 per cent.

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14 Financing Model 3 – Bond Issues

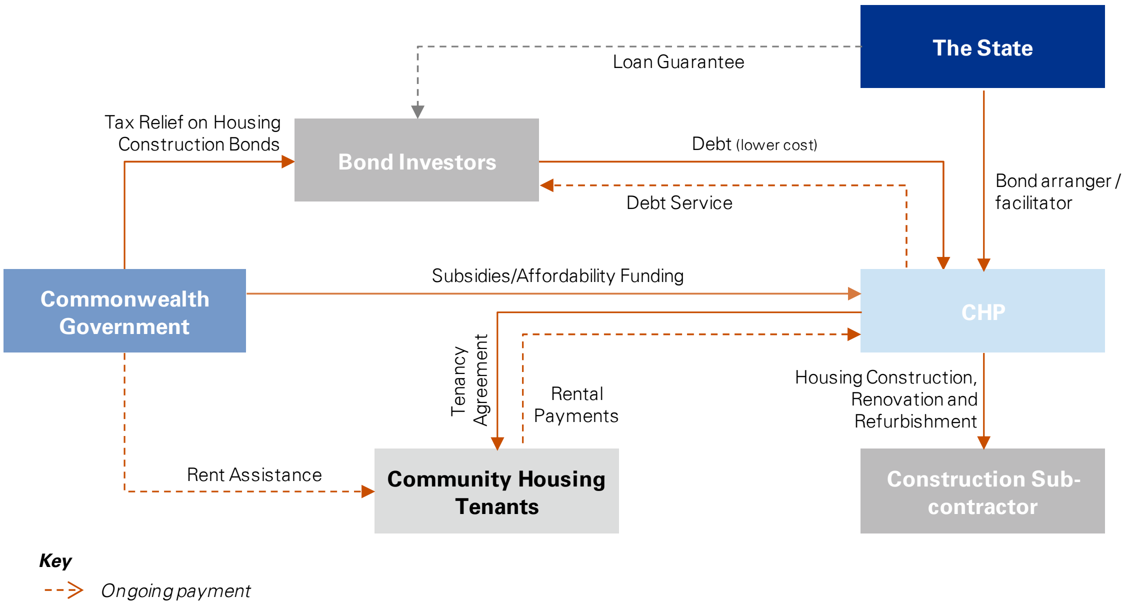
14.1 Outline of model

This option involves the State Government selling bonds to private investors and providing the proceeds of this borrowing to CHPs.

To make the investment viable for private investors, the Commonwealth Government is assumed to offer taxation rebates on the interest earned by investors on the bonds, effectively providing a subsidy to enable market rates of return. In addition, the State would be required to provide a loan guarantee in a similar manner to that described in section 13 above, in order that the cost of finance be reduced commensurate to the State's credit rating.

The commercial structure of this model is presented in Figure 14-1 below:

Figure 14-1: Commercial structure of the Bond Issue model



The commercial structure depicted above implies that the bond issues could fund "housing construction, renovation and refurbishment". In reality, the bond issue model could also be used to assist funding for development schemes in conjunction with private sector property developers as described in section 8 above.

The key features of this commercial structure are presented Table 14-1.

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Table 14-1: Key features of the Bond Issue model

Commercial Structure Features	Applicability to Model
Title transferred to private sector	No – although this option can be combined with other models
Residual land value risk allocated to private sector	No – although this option can be combined with other models
Contractual term	Term of the bond finance
Responsibility for operations transferred to private sector	No – although this option can be combined with other models
Responsibility for maintenance transferred to private sector	No – although this option can be combined with other models
Direct increase in supply of housing stock	No – however, the proceeds provided to CHPs would enable investment in additional housing stock
Utilisation of private sector finance	Yes
Nature of the housing stock	Existing

Government bond issues have the potential to provide CHPs with greater access to finance. The loan guarantee element would also mean that the cost of capital for CHPs is reduced.

However, the potential administrative costs to government of issuing bonds could include:

- The potential future cost of any providers failing and the Government needing to meet that liability, as well as a higher level of regulation of housing providers to mitigate this risk and increase certainty that providers and projects are viable and therefore guarantees will not be called on.
- The cost of any additional government subsidies that could be required to make entities or projects sufficiently viable for private investors or to minimise the financial risks to government of providers failing. Given the low margins generated by CHPs, the cost to government in this context could be substantial.

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14.2 Case study

Table 14-2: Housing construction convertible bonds case study

Housing construction convertible bonds: Austria

Location	Austria
Description	• Rather than focusing on demand management to match supply and demand of social housing, the Austrian government predominantly focuses on the provision of low-cost housing to drive an increase in supply. • Social housing is developed by limited-profit organisations that benefit from public loans. However, these loans are subject to strict maximum rent levels which need to cover the overall project costs (including financing). This approach drives providers to seek the most efficient and cost-effective mix of finance. • Promoted by tax incentives, commercial finance is raised via the sale of bonds to low risk investors which is then provided to social housing projects at a lower cost.
Key Features	• Financing for social housing relies on conditional public loans that are only available in conjunction with private sector funding (such as owner's equity, tenant equity or debt finance). • Bond-financed loans cover an increasing proportion of total construction costs (currently around 50 per cent), with the balance met by housing subsidies and provider contributions. • Housing Construction Convertible Bonds (HCCBs) are sold by banks to individual and institutional investors to raise finance for social housing projects (most purchasers are small-scale individual investors). • The Austrian Tax Office requires that funds raised through the sale of HCCBs are used to finance social housing projects with the following key features: – High-volume housing. – New housing and refurbishment projects. – Accommodation units of modest size (up to 150m^2 depending on household size). – Within defined rent limits. – The tax benefits associated with HCCBs enable housing associations to borrow at up to 1 per cent below market rates. • From the investors perspective, HCCBs have the following key tax features: – Initial cost of the bond is income tax-deductible (with varying deduction rates according to household income – with the highest income bracket not eligible) – Exemption from capital gains tax for the first 4 per cent of returns for all individual investors (regardless of household income) and some public sector bodies (e.g. councils). • Regulations require limited-profit housing associations to borrow at interest rates at a defined basis point limit above the Euro Inter Bank Offer Rate (EURIBOR).
Benefits	• Take-up from individual investors has been widespread with involvement from an estimated 300,000 households (Schmidinger 2009). • Housing Bank Austria (2008) has claimed that for every €1 of foregone tax, €19 of investment has been committed to affordable housing production. • Bond financing has promoted interest rate stability and helped match the long-term deposit needs of banks. • Low return bonds have been made attractive to investors by the tax privileges that have allowed for low interest loans at up to 1 per cent below market rates. • With 50 per cent of total construction costs financed by HCCBs, their capacity to reduce financing costs is significant. • Competition is generated between private banks utilising HCCBs which drives further cost efficiencies.

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Housing construction convertible bonds: Austria

Issues / challenges	• HCCBs have been estimated to cost the Government €120 million in foregone revenues per year (Schmidinger 2009). • The need for HCCBs is largely driven by the declining role of public loans amid rising construction costs. • The Government does not provide a formal guarantee to the banks in the case of default by housing providers. The provision of a guarantee on regular savings products during the global financial crisis (GFC) has therefore drawn investors to supposedly safer investment products.

Primary source: Gilmour, T., Lawson, J. & Milligan, V. International measures to channel investment towards affordable rental housing. Australian Housing and Urban Research Institute, May 2010.

14.3 Evaluation of model

Based on the evaluation criteria and framework outlined in section 5, we have undertaken an evaluation of the model as follows:

Table 14-3: Bond Issue evaluation matrix

Criteria	Rating	Description
Increase in supply	✓	With only modest financial benefits expected, the impact on the overall supply of social housing is likely to be limited and broadly in line with that of Loan Guarantees above.
Operational efficiency	×	This model does not provide the opportunity to achieve improvements in operational efficiency other than via the provision of finance to CHPs for their operation.
Customer experience / quality	×	This model does not provide the opportunity to achieve improvements in operational efficiency.
Flexibility to change	✓✓	Legal title is retained by government which provides a degree of flexibility. However, operational responsibility is transferred to the CHP which detracts from the Government's ability to adapt to change.
Risk transfer	×	This option fails to transfer any risk to the private and not-for-profit sectors. Indeed, loan guarantees would require the Government to accept credit risk of the CHPs. Currently, this risk is absorbed by the CHPs themselves and is reflected in a higher cost of finance in relation to their commercial loans.
Financial statement impact	✓✓	Depending on the structure and scale of the loan guarantee arrangement, there is likely to be some impact on the public sector financial statements. For example, payments to compensate lenders in the event of CHP default will need to be accounted for. In addition, in some circumstances the terms of the guarantee may require a provision in the accounts. The properties are expected to remain on State's balance sheet (unaffected by the transaction).
Ability to leverage	✓✓	This model provides for an increased ability to leverage and therefore invest in additional housing stock. However, the level of additional investment is likely to be modest as the debt is still prima facie required to be serviced by the CHP.
Tax / subsidies impact	✓	This model is substantially similar to the Status quo as there is no transfer of housing stock. However, there may be some additional GST leakage as the Government and bond investors may not be entitled to recover the full GST on expenses associated with the sale of bonds.
Contractual complexity	✓✓	With the Government effectively acting as an intermediary between lenders and CHPs, a moderate level of contractual complexity is likely to exist in order to align the interests of all parties involved.

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Summary of evaluation

As for loan guarantees in section 13, the key advantage of issuing government bonds is that a lower cost of finance can be achieved for CHPs. It is also likely that to some extent, bond issues will increase the availability of finance, as the sources of funds (i.e. bond investors) are not currently being utilised in the social housing market in Victoria.

However, the high administrative costs incurred by government under this model may be significant and will at least partially offset the benefits. An Australian Housing and Urban Research Institute (AHURI) analysis of private sector financing options undertaken in 2002 considered such an option. To make the investment viable for private investors, the Commonwealth Government was assumed to offer taxation rebates on the interest earned by investors on the bonds, effectively providing a subsidy to enable market rates of return. This analysis found that, for a programme to raise $1 billion in new capital through bonds, the cost to the Australian government would be $220 million in subsidies (foregone taxation revenue), which would deliver around 7,500 new dwellings.

If the benefits of government tax rebates and subsidies were to be excluded, the potential to increase the supply of community housing would primarily be based on the reduced cost of financing that the bond issue could provide. This indicates that likely benefits in this respect would be broadly similar to those offered under the Loan Guarantee model described in section 13 above. Excluding tax rebates and subsidies, the CHP's ability to increase the supply of community housing would therefore be modest under the bond issue model.

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15 Financing Model 4 – Sale and Leaseback

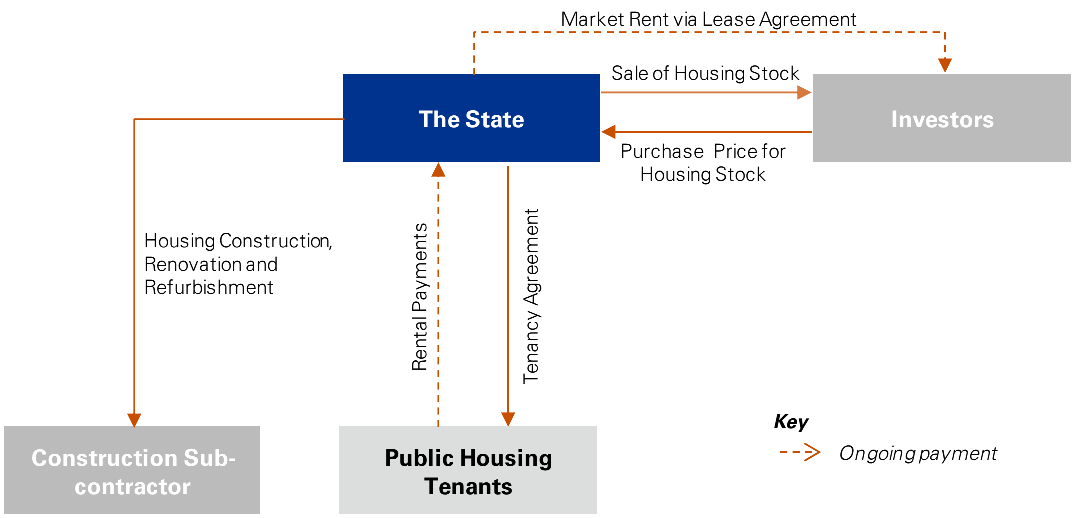
15.1 Outline of model

In its most basic form, the sale and leaseback model involves the sale of property to an investor that in turn leases the property back to the original owner pursuant to a long-term lease. The transaction permits the seller (the Victorian Government) to liquidate its equity in the property while creating a stable investment opportunity for the investor.

In this model, Government would be required to directly pay, or otherwise guarantee the lease stream to the investors.

The commercial structure of this model is presented in Figure 15-1 below:

Figure 15-1: Commercial structure of Sale and Leaseback model



The key features of this commercial structure are presented in Table 15-1.

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Table 15-1: Key features of the Sale and Leaseback model

Commercial Structure Features	Applicability to Model
Title transferred to private sector	Yes
Residual land value risk allocated to private sector	Yes
Contractual term	Contract permanently transfers freehold ownership of the housing stock to the private sector. The period of leaseback could vary
Responsibility for operations transferred to private sector	No – although could be undertaken in conjunction with a transfer of responsibility to a CHP
Responsibility for maintenance transferred to private sector	Yes
Direct increase in supply of housing stock	No – however, an indirect increase can be achieved via the re-investment of sale proceeds into new / replacement stock
Utilisation of private sector finance	Yes (on the basis that the purchase proceeds are financed by the investor)
Nature of the housing stock	Existing

15.2 Case study

Table 15-2: Defence Housing Australia case study

Defence Housing Australia

Location	Australia
Description	• Defence Housing Australia (DHA) provides good quality, affordable rental housing for Department of Defence families throughout Australia. • DHA has developed a sustainable sale and leaseback model that provides advantages for both the DHA and investors. Although the focus of this case study is on defence housing, the financial and operational parameters of this model can provide some valuable insights into how the social housing sector can attract private investment via the sale and leaseback model. • The aim of the sale and leaseback programme is to reduce the capital requirements of the organisation by getting investors to purchase dwellings and lease them back to the organisation via a long-term lease. • In 2009, DHA had a portfolio of over 17,000 dwellings valued at over $7 billion that were owned by a mix of public, private individual and institutional investors. • The DHA sale and leaseback programme now covers more than 60 per cent of its stock.
Key Features	• An investor can purchase a DHA property on the condition that they lease the property to DHA for a period of between six and twelve years. • Investors are paid market rent during the lease period (even if the property is vacant). • Rent is independently reviewed annually to align to market rates and is guaranteed to a minimum level so it cannot drop below the starting rent. • The investor is charged a management fee of 16.5 per cent of rental income that is inclusive of routine maintenance. • DHA repaints the house and provides new floor coverings at the end of the lease, with the investor expected to cover rates and other landlord outgoings. • The leases also incorporate a minimum rental guarantee, which means that the weekly rent cannot drop below the starting rent.

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Defence Housing Australia

Benefits	• DHA markets the opportunity to investors with reference to the following investor benefits: – The rent is based on market valuations and guaranteed by Government and based on market valuations, therefore providing a low risk investment. – Investors do not have to deal directly with tenants and real estate agents as in normal property investments. – Tenants are considered disciplined and reliable. – Hand back conditions stipulated with repainting and new flooring. • The model has allowed DHA to 'scale up' without the need for additional capital or taking on significant debt. • The model has allowed DHA to generate sales in a number of different operating environments and build up a considerable programme of stock.
Issues / challenges	• The sale and leaseback model has generally proved successful for DHA. However, there are a number of issues and challenges that might make the model less applicable to the social housing sector: – The size of the DHA programme meant that significant economies of scale could be achieved. Without stock transfers, the same scale of economies might be difficult for CHPs achieve as they currently operate at a significantly smaller scale to public housing. – Will only be available for public housing provision and not community housing. – Lower rents in the social housing sector might require additional subsidies in order for operations to break even. – Defence personnel are viewed by investors as more reliable rent payers. – Rental payments would require an explicit guarantee from government.

Primary source: Peter Phibbs and Bronwyn Hanna, Lessons of Defence Housing Australia for affordable housing provision, Australian Housing and Urban Research Institute, 2010

15.3 Evaluation of model

Based on the evaluation criteria and framework outlined in section 5, we have undertaken an evaluation of the model as follows:

Table 15-3: Sale and Leaseback evaluation matrix

Criteria	Rating	Description
Increase in supply	✓	In the short-term, the sale proceeds can be reinvested into new social housing stock. However, it should also be noted that when the leasehold expires, the investors have the right to sell the properties which would result in a reduction in the social supply at that point in time.
Operational efficiency	×	This model does not provide the opportunity to achieve improvements in operational efficiency as the services continue to be provided by Government.
Customer experience / quality	×	Since the State retains operational control of the housing and tenant management, there is little scope for improving the tenants' experience.
Flexibility to change	✓	Since legal title is transferred to investors, only a limited flexibility for change is provided under the lease agreement.

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Criteria	Rating	Description
Risk transfer	✓✓	This option transfers long-term maintenance and residual value risk to the non-government entity. As a result of the sale, the Government loses long-term ownership of the property and becomes subject to reversionary risk if leases are not renewed upon expiry. Furthermore, the lease back arrangement would require the Government to directly pay, or otherwise guarantee the lease stream
Financial statement impact	✓- ✓✓✓	Depending on the structure of the sale and leaseback model, there are likely to a number of effects on the public sector financial statements. The sale will result in a de-recognition of properties from Government's balance sheet, but if the lease back is a finance lease, it is possible that the properties will revert to Government's balance sheet. Changes to the lease standard may result in properties reverting to Government's balances sheet also in the operating lease back arrangement (subject the some uncertainty because the final amended leases standard has not yet been released).
Ability to leverage	✓✓	Equity in existing housing stock released through the process can be leveraged to construct or purchase new housing stock.
Tax / subsidies impact	×	This model does not provide for the receipt of tax efficiencies. Government will be liable for net GST on sale of housing built or substantially renovated within 5 years of sale. Investors will not be entitled to recover GST on expenses incurred in the sale and leaseback of housing stock. Investors may also be liable to duty and land tax on housing acquired. As discussed in Development Models 1 & 2, particular care should be taken to ensure that the 'tax preferred use' rules are not triggered as this may have a significant impact on investors' return under this model.
Contractual complexity	✓✓	The contractual complexity of sale and leaseback agreements is likely to be moderate to high.

Summary of evaluation

This model may provide for some up front proceeds that can be invested in an increase in stock. However, the model does not change the service delivery arrangements, other than in relation to maintenance, and is therefore in effect a financing mechanism to release the equity in the current housing stock. Furthermore, a range of reversionary risks are assumed by Government relating to the use of the assets post the lease period.

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16 Summary of Evaluation

16.1 Models considered

As outlined in the above sections, there are a range of different potential models that can be used to directly or indirectly address the supply-side issues. The models considered in this report are as follows:

Development Model 1	Development PPP
Development Model 2	CHP Development Agreement
Transfer Model 1	Community Housing Stock Transfer
Transfer Model 2	Shared Equity / Ownership
Transfer Model 3	Outsourcing Maintenance / Management
Financing Model 1	Securitisation
Financing Model 2	Loan Guarantees
Financing Model 3	Bond Issues
Financing Model 4	Sale and Leaseback

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16.2 Summary of Model Evaluation

As outlined in the above sections, each of the different models involve different elements and have addressed the evaluation criteria to varying degrees. A summary of the evaluation contained in the above sections is as follows:

Table 16-1: Summary evaluation of models

		Development		Transfer			Financing			
Criteria		**1**	**2**	**1**	**2**	**3**	**1**	**2**	**3**	**4**
	Status Quo	**Development PPP**	**CHP Development Agreement**	**Community Housing Stock Transfer**	**Shared Equity / Ownership**	**Outsourcing Maintenance / Management**	**Securitisation**	**Loan Guarantees**	**Bond Issues**	**Sale and Leaseback**
Increase in supply	-	✓✓✓	✓✓	✓	✓	✓	✓	✓	✓	✓
Operational efficiency	-	✓✓✓	✓✓✓	✓✓✓	×-✓✓✓	✓✓	×	×	×	×
Customer experience / quality	-	✓✓✓	✓✓✓	✓✓	✓	✓	×	×	×	×
Flexibility to change	-	✓	✓	✓	✓	✓✓	✓✓	✓✓	✓✓	✓
Risk transfer	-	✓✓✓	✓✓	✓✓✓	✓	✓	×	×	×	✓✓
Financial statement impact	-	✓	✓	×-✓	✓-✓✓	✓✓✓	✓✓-✓✓✓	✓✓	✓✓	✓- ✓✓✓
Ability to leverage	-	✓✓	✓✓	✓✓	✓	×	✓✓	✓✓	✓✓	✓✓
Tax / subsidies impact	-	✓✓	✓✓✓	✓✓✓	×	✓	✓	✓	✓	×
Contractual complexity	-	✓	✓✓	✓✓	✓	✓✓	×	✓✓	✓✓	✓✓

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16.3 Summary

The qualitative evaluation summary depicted in Table 16-1 illustrates that Development Models offer significant improvements in operational efficiency, customer experience, risk transfer and ability to leverage. Furthermore, the transfer of residual value risk may provide an additional upfront financial benefit to Government, based on a view (and ability to capture) that the future value of land and property will increase. Combining these factors with the fact that Development Models involve the direct construction of new social housing on a sizeable scale, means that these offer significant potential to increase the social housing supply in Victoria.

Table 16-1 illustrates that Transfer Models generally offer a moderate ability to increase supply. The community housing stock transfer model is perceived as positive in relation to the ability to achieve risk transfer, operational efficiency, ability to leverage and access to tax efficiencies. However, this is partially offset by the accounting write down in asset value and the impact on the Governments financial statements. The sale and leaseback model may provide for some up front proceeds that can be invested in an increase in stock, but the model does not change the service delivery arrangements and a range of reversionary risks are assumed by Government relating to the use of the assets post the lease period. Compared against the status quo, the shared equity model provides moderate benefits against most criteria. However, if combined with a transfer to a CHP, this model could enable the operational efficiencies associated with CHP management.

In addition to benefits in relation to the transfer of risk and the avoidance of adverse accounting impacts, the outsourcing maintenance / management model offers potential to achieve operational efficiencies. However, as with other transfer models, the focus is on existing stock and does not therefore provide for a significant direct increase of supply or replacement of stock.

The evaluation of the four Financing Models shows a broad level of consistency regarding their ability to meet the criteria. Benefits are derived from the improved ability to leverage, the flexibility to change and the impact on the Government's financial statements. The most notable benefit of these models is their ability to reduce the cost of finance in the market or provide a return on securitised cashflows. However, the administrative costs incurred by government under these models may be significant and will offset at least some of the benefits. This restricts the potential of these models to materially increase the supply of social housing in Victoria.

On balance, the Development Models outperform the other types of models against the majority of criteria considered, including operational efficiency, customer experience, risk transfer and ability to leverage. Of these, the PPP model appears to offer the greatest potential. This is despite the notable drawbacks relating to the impacts on the Government's financial statements and the issue that contractual arrangements can be complex. It should be noted however, that this model will only be relevant for specific potential projects / sites and that the specific commercial arrangement relating to each development project (particularly regarding stock and land transfer) can significantly impact on the additional supply of social housing brought to market. The Bonnyrigg project discussed in section 7.2 illustrates this point, with the project resulting in no net increase in the total number of social housing units. However, as for the Bonnyrigg project, the PPP model can deliver new social housing that replaces old stock that is no longer fit for purpose, as well as improving the overall quality of the environment for tenants and the broader community.

Each of these options have various advantages and disadvantages in the manner in which they may directly or indirectly increase the supply of housing. However, it is recognised that in order to materially address the challenge, the implementation of an appropriate combination of solutions will be required.

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17 Conclusion

Social housing in Victoria is designed as a safety net through which the Government provides housing assistance to those unable to afford or access the private housing market at a particular time in their lives. It is designed to provide assistance to those most in need. The Victorian Government's objective is to ensure there is equitable access to public housing in Victoria and that those most in need are accorded priority.

The key challenges that have set the context of this discussion paper include:

- The cost of subsidising rents and utilities and maintaining large and ageing stock has resulted in a current and projected structural deficit for public housing in Victoria. The forecast structural deficit (as a result of spending being greater than revenue collected from rent) is expected to double from \$56.4 million in 2011 to \$115.1 million in 2015.[79] Public housing is also facing a cash crisis, with all cash reserves "expected to be exhausted during the 2012-13 financial year" based on current budget estimates and if policy settings remain unchanged.[80]
- Forty-two per cent of Victoria's public housing stock is more than 30 years old and in need of repair or replacement.[81]
- Maintenance, repair and replacement costs are increasing whist available resources for public housing are shrinking. In 2007, almost one third of stock had maintenance requirements costing between \$5,000 and \$20,000.[82] In real terms, the net recurrent operating costs per public dwelling in Victoria have increased by 18 per cent between 2005-06 and 2010-11.
- An under-investment in public housing has created a large maintenance liability and backlog.[83] In 2011, it was estimated that around \$600 million would be required for portfolio maintenance over three years.[84]
- For every ten people living in public housing dwellings in Victoria, there are approximately three people on the public housing waiting list.[85] Contributing to this is the fact that turnover in public housing has steadily decreased in recent years as people who have been allocated a public housing dwelling stay longer. In part, this can be attributed to the fact that there are no eligibility reviews of those in public housing and that leases are effectively open-ended.
- The mix of housing types within the public housing stock is suboptimal and not aligned to the type of housing required by public housing tenants. For example, almost 80 per cent of demand is for a one or two-bedroom house and yet these types of dwellings make up just 53 per cent of total stock.

The incremental approach applied in recent years has been ineffective in increasing supply to match the increased level demand and the sustainability challenges have intensified. This report provides an overview of a range of potential options that could be utilised to assist in increasing the supply of quality housing in Victoria. Each of these have various advantages and disadvantages in the manner in which they may directly or indirectly increase the supply of housing. However, it is recognised that in order to materially address the challenge, the implementation of an appropriate combination of solutions will be required.

The optimal combination will be dependent on a number of factors including the inter-related benefits or challenges between sets of options and their overall ability to address the

[79] Victorian Auditor-General's Office (2012) Access to Public Housing, March 2012
[80] Victorian Auditor-General's Office (2012) Access to Public Housing, March 2012, p. 10
[81] Internal Department of Human Services data
[82] Parliament of Victoria (2010) *Inquiry into the Adequacy and Future Directions of Public Housing in Victoria*, Family and Community Development Committee, September 2010
[83] Parliament of Victoria (2010) *Inquiry into the Adequacy and Future Directions of Public Housing in Victoria*, Family and Community Development Committee, September 2010
[84] As noted in a 2011 Budget submission by DHS. Source: Victorian Auditor-General (2012) Access to Public Housing, March 2012
[85] Around 127,000 people live in public housing dwellings in Victoria. As at March 2012, there were 37,887 people on the waiting list for public housing in Victoria. (Internal Department of Human Services data.)

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key issues facing the social housing sector in Victoria. The implementation of a combined set of solutions will also need to consider the size and scale required by each option to make them viable. For example, an incremental approach regarding the transfer of stock to the non-government sector is not expected to have a material effect on supply. It is therefore suggested that both the scale and potential combination of options be considered.

Based on the evaluation of each model as outlined in this discussion paper, all options and variables warrant further investigation, but in particular it is suggested that further consideration of the following be undertaken:

- Identification of projects suitable for a development PPP.
- Stock transfers to the non-government sector.
- Implicit or explicit government guarantees.
- Further discussions with financiers in relation to the manner in which they assess lending in housing sector.

Applied with significant size and scale and as part of a long-term portfolio realignment strategy, an optimal combination of options should not only increase the supply of quality social housing and help to support a financially sustainable asset base, but it should also assist in rebalancing the supply and demand of social housing to better meet the needs of the community.

The optimal solution to drive an increase in the supply of quality social housing in Victoria must also be considered in the context of Victorian Government policies in the social housing sector. For example, if policy settings remain unchanged, a number of the options considered in this discussion paper will be unviable. A holistic approach is therefore required that considers the supply-side mechanisms in conjunction with their enabling policies.

In order to help shape the future of a sustainable social housing sector, the Victorian Government is currently undertaking a market consultation process to seek views on the issues and options outlined in this document.

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