Increasing affordable housing

How community housing providers in NSW could deliver more

Submission to the Affordable Housing Group by NSW Federation of Housing Associations – March 2016

nsw Federation of Housing Associations inc

Author: Wendy Hayhurst

NSW Federation of Housing Associations inc

ABN 86 488 945 663

Suite 301, 64-76 Kippax Street, Surry Hills NSW 2010

Telephone: (02) 9281 7144 Facsimile: (02) 9281 7603

Email: nswfha@communityhousing.org.au

www.communityhousing.org.au

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Executive Summary

NSW Federation of Housing Associations and the NSW Community Housing Sector

The NSW Federation of Housing Associations (the Federation) is the industry peak body for community housing providers in NSW. All tier 1 and tier 2 registered providers are Federation members. The organisation was founded in 1993 to provide support and resources for their further development. Since it was established, the Federation has expanded its business to anticipate and respond to the needs of its members and stakeholders, and to support the organisation's independence and viability.

The Federation is a leading member of the network of community housing industry peaks across Australia, working collaboratively to enhance services to members and to support the development of the industry. Many of the Federation's services are delivered across Australia.

Community housing providers in NSW manage over 32,500 tenancies, employ over 910 staff, have a capital base of circa $3 billion and have bank debt of $200M invested in new affordable housing.

A massive challenge

- Since 1996, only around 10,000 additional dwellings have been added to the NSW affordable housing stock
- Conservative estimates suggest that NSW needs between 30,000 and 67,000 more homes for low-income households right now
- Assuming build costs averaging $350,000 per home, the bill to make good this deficit is between $10.5 and $23.5 billion
- And then add what is required to meet forecast household growth.

Reliable, well priced and long term private finance is necessary, but insufficient to address the affordability challenge

The Federation believes that without other strategy and policy initiatives, none of the proposed financial models will work. The Federation would like to see

- Government leadership at both Commonwealth and State levels and the re-establishment of National Institutions such as the National Housing Supply Council

- Informed strategic plans at every level of government that integrate initiatives and which are underpinned by robust information about housing needs information

- Affordable housing targets cascading from the national to local levels

- A planning system that supports the delivery of affordable housing through- for example- inclusionary zoning and / or another value-sharing mechanism

- Reforming tax incentives and rebalancing subsidy between housing sectors to direct these towards affordable housing

- Optimising the use of government land to enable the delivery of affordable housing

- A long term affordable housing investment fund targeted at community housing providers to enable them to leverage additional private investment to deliver a pipeline of projects

- Government mechanisms to trigger large scale investment in new affordable housing

- The staged transfer of the (NSW) social housing portfolio to community housing providers

- A clear commitment from government to create an environment in which the community housing industry can achieve the best outcomes for tenants and communities.

Model 1 – Housing loan / bond aggregators

Housing loan and bond aggregators offer real potential to support and promote private investment in the community housing industry:

- The concept of Financial intermediaries is proven - Substantial work that has already been completed in this field and tried and tested models exist. They:

    - Build scale by aggregating debt requirements into regular bond issues

    - Reduce financing costs – addresses short term borrowing issues; negotiation burden and cyclical credit availability

- Bond that are an investment in a stable cash-flow (not in property):

    - Offer lower yields than for equity-based products

- Mean longer term security for tenants

Federation Financial Intermediary Project

This project will be:

- NSW-led, but applicable nationally

- A concise Business Case report, setting out preferable options for establishing the Intermediary

- An opportunity for stakeholder building throughout the project including extensive participation of key financial sector partners.

- Launch NSW Affordable Housing Conference on 28th and 29th July, 2016.

Not a silver bullet

Model 1 will be successful only if it is predicated upon stable, ongoing government support for affordable housing in a form that underpins institutional investor confidence.

- Strengthen regulation – make it national, revitalise the governance, make it visible and ensure its policy and practice evolves as the community housing sector develops

- Support the implementation of the Financial Intermediary through guarantees, a proof of concept stage and addressing the investor yield gap through combinations of operating subsidies and capital contributions such as government land

- Progressively transfer public housing to the community housing management and ownership

- Use the planning system to enable more affordable housing through inclusionary zoning

- Introduce a revolving construction debt facility.

Increasing affordable housing

How community housing providers in NSW could deliver more

nsw Federation of Housing Associations inc

NSW's prosperity and future growth is limited by the housing affordability crisis. Over half of low income renters and purchasers are in housing stress, and 60,000 households languish on the social housing waiting list. Home ownership rates are plummeting, especially for traditional first home buyers aged 25-35.

The NSW Federation of Housing Associations (the Federation) is the industry peak body for community housing providers in NSW. Since 1993 the organisation has provided leadership to the community housing industry, to provide support and resources for their further development, and has represented the aspirations and interests of the industry to all other stakeholders – government, partners, business and the wider community.

The Federation's purpose is to support the development of a not for profit rental housing sector which compares to any around the world, and which makes a difference to the lives of lower income and disadvantaged households across the state. The Federation seeks to ensure that community housing providers are active in all housing markets, providing a full range of housing products.

NSW community housing providers …

- Manage 32,500 tenancies
- Employ over 910 dedicated staff
- Run 64 local housing offices
- Rental income stream of $300 million p.a.
- Capital base of $3 billion
- $200M plus bank debt invested in affordable housing

Figures based on June 2015 financial statements of the largest 20 NSW based Tier 1 and 2 registered providers.

In NSW the State government has recently released its strategy to transform public housing, Future Directions. By 2026 through a range of initiatives including a social and affordable housing fund, the Communities Plus regeneration sites and around 30,000 property transfers to community housing providers, the government aims to increase affordable housing by around 9,500 homes. This is a great start but a drop in the ocean insofar as what is required to tackle housing unaffordability.

The Federation therefore welcomes the establishment of the Affordable Housing Working Group as a signal of the Commonwealth's re-engagement with housing affordability. The Federation hopes this presages the re-establishment of national institutions such as the Housing and Homelessness Ministers Advisory Council and the National Supply Council.

The Federation accepts the invitation to assist in the Group's objective to "identify potential financing and structural reform models that increase the provision of affordable housing for those on low incomes". That said, we find it somewhat disappointing that the consultation seeks responses to outline ideas rather than comments on substantive propositions already developed within (or on behalf of) the Government on the basis of the extensive body of evidence-based affordable housing policy proposals in the public domain. In particular, there is the canon of germane research directly funded by the Government itself via the Australian Housing and Urban Research Institute (AHURI). Of prime relevance to the Working Group's 'Model 1' – surely the prime contender as a scalable framework to facilitate substantial affordable housing investment are the studies by Lawson, Berry, Milligan and others (e.g. AHURI Final Reports 110, 188, 202, 215 and 220). While we are more than happy to take this opportunity to once more draw such evidence to the Government's attention, we are not convinced that this process will have offered the swiftest path to action on the ground.

About this submission

The Working Group has indicated its particular interest in submissions that can be used to develop viable financing models; four (non- mutually exclusive) options are included in the paper. The Federation notes that the Working Group is also open to receiving more general feedback. In our submission we have chosen to focus on Model 1 – Housing loan / bond aggregators. This is because the Federation believes it offers substantial scope to support and promote private investment in the community housing industry to deliver affordable housing and we are already undertaking work to build concrete proposals to take forward the substantial work that has already been completed in this field.

The Federation has not made substantive comments on the other Models. Our views are summarised below.

We believe social impact bonds have potential to increase investment, however they could be best described as niche products (valuable for projects to tackle specific issues such as youth homelessness) and therefore unlikely to unleash the resources that a bond aggregator model could.

Housing cooperatives are similarly, we believe, non scalable although to be encouraged as part of a diverse range of housing opportunities. They have proven to be a sustainable model and with home ownership rates declining, the cooperative model offers people the opportunity to participate in the management of the property and security of tenure. Housing cooperatives would of course be able to secure funding via the housing aggregator model.

In terms of Model 2 – the Housing Trust model- we would be pleased to provide feedback on proposals coming forward. We note that AHURI have carried out research into Community Land Trusts 'Principles and practices of an affordable housing Community Land Trust model' -(Crabtree, Phibbs, Milligan and Blunden) which suggests that "CLTs are worthy of further consideration in Australia. Both the Australian appetite for home ownership and the serious barriers to home ownership developing for low- to moderate-income households support this position. The expansion of the affordable rental sector in Australia highlights the need for entry-level ownership products that can facilitate the transition of households from such affordable rental to home ownership without full exposure to the housing market".

Our main concern would be a Trust model that essentially replicates a large public housing landlord and reduces what we believe is the strength of the community housing industry –its diversity. At the Sydney roundtable on 26 February the Trust model was described as potentially a "sophisticated Defence Housing Australia – DHA model". This could hold assets from a combination of sources - public sector, community housing providers and individual mum-and-dad investors. The Trust would engage property developers and tenancy / property managers to carry out its operational functions. The Federation notes that the key distinction with the bond aggregator model is the returns it would require to satisfy the enhanced risk associated with it being an equity model.

Notwithstanding, some discussion about how it could be structured to reduce the volatility inherent in the model, the disadvantage of higher return requirements together with uncertainty over security of tenure for tenants and potential unresponsiveness to strategic asset management challenges lead the Federation to be at best agnostic about the Trust model as described at the roundtable.

We would also caution against the assumption that aggregation of management activity is necessarily more efficient; though we note the Trust could decide to parcel up management and development packages.

Meeting the Affordability Challenge

1. Government leadership at both Commonwealth and State and reestablishment of National Institutions such as the National Housing Supply Council
2. Strategic plans every level of government that integrate initiatives and which are underpinned by robust housing needs information
3. Affordable housing targets cascading from the national to local levels
4. A planning system that supports the delivery of affordable housing through for example inclusionary zoning and / or another value sharing mechanism
5. Reforming tax incentives and rebalancing subsidy between housing sectors to direct these towards affordable housing
6. Optimising the use of government land to enable the delivery of affordable housing
7. A long term affordable housing investment fund targeted at community housing providers to enable them to leverage additional private investment to deliver a pipeline of projects
8. Government mechanisms to trigger large scale investment in new affordable housing
9. The staged transfer of the (NSW) social housing portfolio to community housing providers
10. A clear commitment from government to create an environment in which community housing industry can achieve the best outcomes for tenants and communities

While reliable, well-priced and long term private finance is necessary, on its own it is insufficient to address the challenge. We have therefore very briefly summarised the other strategy and policy initiatives the Federation believes are necessary and referenced key papers and submissions we have published on the subject.

In the submission we have also summarised the scale of investment required and also explained why the community housing industry should be the preferred partner to help government to deliver more affordable housing.

What is the size of the problem?

Since Government house-building investment was sharply cut in 1996, only around 10,000 additional dwellings have been added to the NSW affordable housing stock over and above public housing sales and demolitions. Conservative estimates based on a 2014 Swinburne University study suggest that NSW needs between 30,000 and 67,000 more homes for low-income households right now.

Assuming build costs averaging $350,000 per home, the bill to make good this deficit is between $10.5 and $23.5 billion. And that's just what it would cost to restore the scale of social housing provision that existed in 1996. Bringing the remaining homes up to a decent standard would come with another hefty price tag, let alone factoring in the costs of building the additional homes to meet demand in 2026.

It is time to recognise affordable housing as an economic issue; as critical infrastructure in the same way as roads, railways and utilities. Not only is more affordable housing a vital foundation for many people to stabilise their lives and gain social and financial independence, it also contributes to the efficiency of the entire economy. If people are forced away from where there are jobs they will in the best case add to costly traffic congestion or in the worst, push up unemployment.

Defining Affordability

The Commonwealth is expected to spend approximately $4.4 billion in Commonwealth Rent Assistance (CRA) serving 1.3 million households, or nearly one in three renters. The cost of CRA is rising at 7 percent per year, after adjustment for inflation. Even with that expenditure, representing a modest $282 monthly subsidy, 40 percent of CRA recipients still experience housing stress.

There is no common definition of affordable housing or what is an affordable rent or housing payment for either renters or owners in Australia, which presents challenges for assessing need and planning provision. It makes approaches such as requiring affordable housing contributions via the planning system very difficult.

The Commonwealth and State governments should be proposing a clear and consistent definition.

Meeting Needs

Simply increasing housing supply won't on its own solve housing unaffordability. This fails to address demand pressures coming from not only rising numbers of households but also investors and those wanting a second home. It also fails to take into account the type, size and location of housing needed to meet the needs of a diverse population. We recommend that the Commonwealth and State governments work together to establish and quantify housing need and future demand at the national, state, regional and local levels. This information should be routinely updated and made publically available. In this work the governments can draw on forthcoming AHURI research 'Modelling housing need in Australia to 2025' led by Curtin University.

Why community housing?

Not-for-profit community housing organisations have been providing high quality rental housing for people on low to moderate incomes for over three decades.

Community housing providers always had the commitment and now have the capacity and the proven track record. In less than a decade community housing providers have invested in and strengthened their organisations, enhanced their business systems, recruited and trained their workforce, taken on their first private finance loans and doubled their role in delivering new housing and tenant support services across NSW.

The sector has low rent arrears, minimal vacancy rates, and high tenant satisfaction. Community housing providers run services for tenants such as work programs, training and counselling. During 2015 at least 50 percent of NSW providers offered scholarships and / or work experience to their tenants.

Community housing providers offer a continuum of housing options including crisis, social and key worker (affordable) rentals. In future, we can work with rent-to-buy schemes and shared ownership. These innovations will provide a pathway towards home ownership for some tenants.

NSW community housing providers perform……
Over 85% tenant satisfaction with property condition
87% were satisfied with overall services
Over 80% satisfied with maintenance services
Just 2 percent rent outstanding.
Over 97% urgent repairs completed on time
Figures based on June 2015 regulatory and contractual performance data from 23 NSW based registered providers participating in the Federation's Housekeys benchmarking service

We can help leverage precious tax-payer funds, delivering more homes per dollar. Unlike public housing, community housing can use its asset base to attract private finance and build more homes. It is more financially sustainable than public housing because tenants are eligible for Commonwealth Rent Assistance. The sector's charitable status makes it exempt from GST, land tax and stamp duty and also helps attract philanthropic donations. It invests its surpluses back into new homes, better services and maintaining properties instead of paying private sector salaries or dividends to shareholders. One of the community housing industry's key strengths lies in its diversity and its responsiveness to local circumstances. The Federation anticipates that if opportunities to grow are presented, providers will diversify even more so. There will be a number of larger providers but as is the case in the UK, there will be many others who choose to develop and grow, but more slowly. They will achieve this where necessary through aggregating their development, financing and other procurement requirements or through formal partnerships.

We have already demonstrated the capacity to partner with developers and local government to expand affordable housing through the planning system. Throughout NSW and beyond there are many, many examples of community housing providers collaborating to build new homes. Community housing providers need to be hard-headed business managers because there are no public bailouts. Unlike public housing they are innovative and entrepreneurial, while also accountable to stakeholders through statutory regulation.

Community housing is also in it for the long haul. Developers build and flip, community housing providers manage their housing for the long term, so design matters, and so does quality. Some of the world's most cutting edge residential architecture and biggest innovations in sustainability are in the community and social housing space.

However, the community housing industry's potential is constrained by a number of factors and not least the cost and terms of loan finance.

Large Scale Investment in Affordable Housing Delivered by Community Housing Providers

The Affordable Housing Working Group Issues Paper notes the community housing industry is not viewed as a mature asset class and explains that it has experienced difficulty in building its balance sheet and cash flows to operate at the scale to secure finance for expansion. Our proposal - the NSW Financial Intermediary Project – is designed to address one aspect of the scale problem by aggregating the debt requirements of multiple community housing providers. While the project is initiated in NSW, the Intermediary concept is applicable at the national level.

As we have already noted the project is building on existing research which examined and evaluated successful aggregator models from across the globe. It needs to be emphasised this concept is proven and with the right policy framework and backing it will work.

First we explain why the Federation believes that Housing Bonds would enable more affordable housing and outline the conditions required to support their introduction.

Housing Bonds

Put simply, Housing Bonds are a means of **accessing the capital markets** that will be an important component in funding new supply of affordable rental dwellings. Community housing providers can pool debts to issue sizable repeatable transactions. They are privately issued bonds with government backing, but are not government-issued bonds.

Essentially, housing bonds are straightforward debt agreements, issued over a long term that match the profile of its underlying assets - bricks and mortar - and stable, secure cash flows which in social housing are primarily 'triple A rated' Federal welfare payments.

Why housing bonds?

Housing bonds are designed to expand and **improve upon the current bank loans** that have emerged to support private, social and affordable housing expansion as government funding has receded. Although these early commercial lenders have nobly supported the emergence of community housing's private funding capacity, these loans are individually negotiated, often of a short 3 - 5 year term, and require expensive interest rate hedges to mitigate future risk. This commercial lending has filled the limited opportunities for community housing expansion of the past decade, but larger-scale supply catch-up in the coming decade will be more efficiently served by pooled bonds. Critically, housing bonds would eliminate risks inherent with repeated refinancing.

Not only would housing bonds signal a maturing in community housing finance, but they would **expand the current means of funding Australian private rental housing** in general. Rental housing is currently funded by individual retail mortgages taken out by mum-and-dad investors who typically own fewer than five dwellings, with almost no securitisation of this massive asset class outside Defence Housing Australia.

What if there were better-diversified, sophisticated instruments like bonds in which mum-and-dads and institutional investors alike could invest that supported stable rental housing supply?

Housing bonds represent a policy direction towards rental housing as an investment asset class as is already the case in the UK. The bonds themselves, as a starting point, must be **large-scale**, **replicable** issues of debt supporting **high-quality** housing projects that would be contestably chosen based on feasibility and operational stability. The large scale of these regular bond issues will qualify for investment analysis by institutional investors, like super funds, and their annual replicability will provide some liquidity in an otherwise illiquid asset class.

How would they work?

The fundamental principle behind housing bonds is this: investment in rental housing is in a stable ***cash flow,* not in *property*** per se. When well-managed, rental housing has a secure annuity-style income profile rather than a speculative, higher-risk property gamble. This distinction is central because security of rental tenure is as important to a government's driver of workforce mobility/economic competitiveness as it is to the community housing industry's mission of achieving housing stability.

A major part of the solution

Housing bonds alone **cannot fund 100% of new rental housing**. They are not a 'silver bullet' that will work alone to address the state's rental housing backlog. They will provide debt that is sized to be supported by the given portfolio's cash flow profile, which may reflect varying targets for affordability relative to market.

The difference between this supportable debt and the total cost of the project is **the gap that must be funded by other sources**. In an affordable housing project, this would be a combination of government or non-profit equity that is invested in return for social outcomes; in a market-rate rental development this would be funded by a sponsor's commercial equity investment with conventional return expectations.

Government's role

The two main features that would jump-start a housing bond concept are the creation of a sophisticated Financial Intermediary and Government credit support in the form of a limited guarantee.

Substantial research has been done in Australia to arrive at our model, based both on overseas precedents for housing bonds as well as Australian settings.

The Financial Intermediary supports the fundamental concept of *pooling* upon which housing bonds are based: it would manage the portfolio composition and financial profile of eligible rental housing developments in order to achieve the diversification and transactional efficiency that are features of housing bonds.

The government **guarantee** or credit support is necessary to overcome initial new-market hesitance towards an asset class that has no track record of institutional investment. Because super fund asset advisors have no performance history of pooled rental housing assets to review and little familiarity with the in-built risk reduction of community housing's national regulation system, a government guarantee or similar credit support would be necessary to bridge this gap until a new asset class of housing bonds were established. Such a guarantee may only be needed for two to three years until the market takes off.

A government guarantee would reduce the risk of investing in the bonds and would therefore bring down their interest rate. A lower interest rate would mean a given rental cash flow could then support more bond debt, thus reducing the gap. Research has indicated that a well-structured, limited guarantee would not need to be reflected on government balance sheets, and consultation with ratings agency government risk analysts reveal that the magnitude of housing bond credit support proposed would not impact State or Commonwealth credit ratings.

The crucial link to be made is that **rental housing is key state infrastructure**, and should be planned and financed as such. The use of government guarantees for key economic infrastructure is well-documented and confirmed by the Commonwealth government in its the 2014 budget. The NSW government's understanding of available and affordable rental housing as key state infrastructure was confirmed earlier in 2015. Long-term debt instruments like bonds are therefore an appropriate step, together with other funding sources, in providing this much-needed infrastructure

The NSW Financial Intermediary Project

Outline

The Federation has been awarded funding for 2015/16 under the NSW Government Family and Community Services (FACS) Community Housing Industry Development Strategy to develop a business case for an industry-led affordable housing finance intermediary.

The project's two overall aims are to:

- enhance the industry's development and growth through efficient access to aggregated finance as the organic next step from current practice of individually-negotiated, short-term commercial bank loans

- To build awareness among key financial stakeholders of the industry's goals for efficient growth through aggregated, contested financing.

While the project is focused on NSW, it will consider the potential applicability (and desirability of extension) to the wider Australian context.

The project is building on the existing research and working examples from elsewhere. While models from other jurisdictions cannot be adopted in their entirety, many are essentially replicable in Australia. For example attributes of The Housing Finance Corporation (THFC) Model in the UK, a sophisticated non-profit aggregator with £33 billion in aggregated affordable housing debt under management, are likely to be relevant and feature in the business case put forward.

UK precedent THFC – Key Features

- An independent, specialist, not-for-profit Intermediary acts as principal and borrows in its own name. It on-lends immediately and only to registered housing.
- Funds itself through the issue of bonds to private investors and by borrowing from banks.
- A joint initiative in 1987 of the Housing Corporation (HC), at the time the UK government agency with both regulatory and funding roles and the National Housing Federation (NHF) – the peak industry body
- Nine-strong board drawn from the banking, financial and commercial sectors and representation from the HCA (the HC equivalent) and NHF, which helps keep THFC focused on the needs and risks of the HA sector.
- Held its A+ credit rating (stable) since 2004.
- Funds borrowed are on-lent on similar interest and repayment terms thus ensuring that THFC is protected against interest rate risk.
- THFC makes its own credit assessment of potential borrowers.
- All THFC loans are fully secured and THFC is legally bound to conservatively set covenants.

Once completed in July / August 2016 the Federation will offer a blueprint for operationalising this research. Key outputs from the work will be:

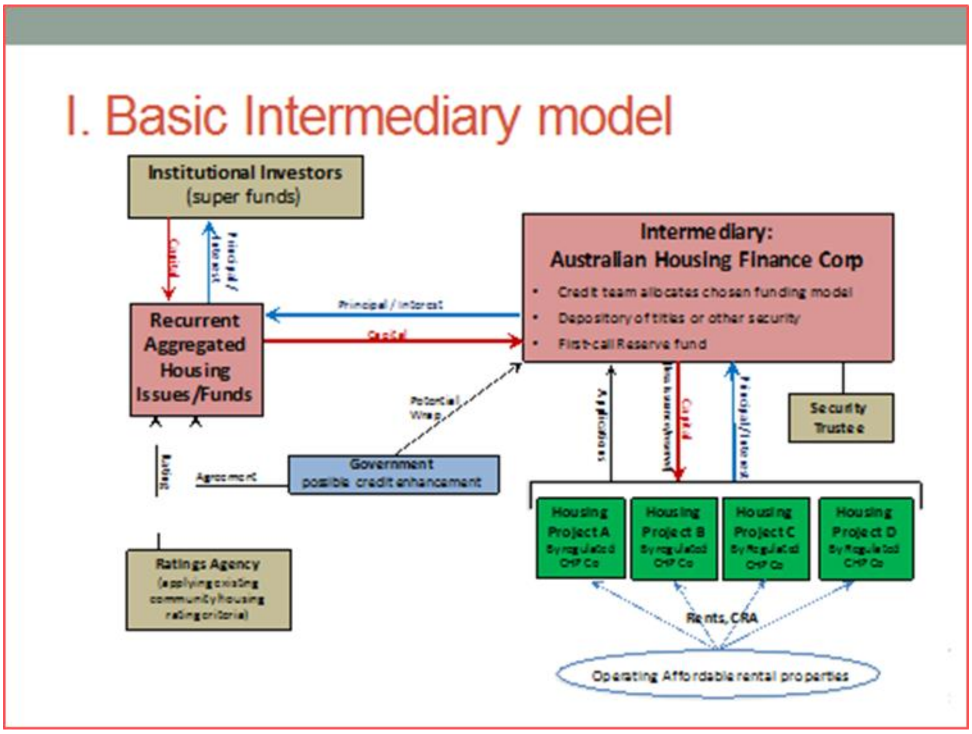
- An implementation plan setting out the next steps
- Costs associated with setting up the Financial Intermediary
- The government contribution (financial and other) required both in the Financial Intermediary's establishment and in the short to medium term.

In terms of progress, the background literature review has been completed and a project reference group drawing expertise from Federation members, academia, the legal profession, the banking and superannuation industry and government is being established.

As the project is underway we cannot at this stage respond to all the points in the Issues Paper. Suffice to say these questions are key to our work. **The Intermediary is only relevant once there is a reliable pipeline of government support to underpin activity in this industry and indeed to aggregate.**

A synopsis

A Financial Intermediary can help meet the current shortfall in affordable rental dwellings in NSW and provide a recurrent platform for meeting future demand to accommodate NSW's population growth. It could also conceivably assist in affordable projects operating under expiring programs like NRAS, accessing efficient finance to help preserve ownership by community housing providers. Though rental yield subsidies will cease, efficient lending margins should help preserve some NRAS dwellings. Likewise, the Intermediary is intended to be a recurrent pathway for finance that can accommodate dwelling replacement or refurbishment regardless of the point in the economic cycle. The basic intermediary model is illustrated below.



For government, the Intermediary facilitates the entry of significant private capital to supplement government investment in the sector. For institutional investors, it creates a pathway to a new asset class in secure rental housing cash flows at scale. It plays an essential market-making role in operationalising whatever model is chosen by the Commonwealth to enhance investment in affordable housing and in normalising such investment in a new asset class for the institutional finance market.

The proposed financing intermediary is not a holding vehicle or sovereign fund model where funds are invested in financial markets and proceeds used to support housing. Rather, the Intermediary is a debt aggregation model to address current short borrowing terms, inefficient negotiation burden and cyclical availability issues of commercial bank debt.

The Housing Finance Intermediary is a means of pooling housing projects to approach the capital markets. It will provide scale and even liquidity through aggregation into regular bond issues or funds and thereby facilitate private sector to finance unmet market demand.

While this intermediary project is model-agnostic, the Federation is confident that its preferred option and many others can 'plug in' to the aggregation structure. Various formulations of government support (equity in the form of grant or land, debt in the form of interest rate subsidy or yield gap funding, or credit support in the form of a guarantee) could all be contestably be allocated to housing development projects that are then aggregated, structured and rated to meet institutional investment appetites.

The Federation prefers that the Commonwealth government pursue funding models that rely on long-term cash flow-based private financing, commensurate with fixed-income investment, rather than more speculative models that rely on the sale of the dwelling units after a term in order to crystalise underlying asset appreciation. The community housing industry seeks to provide stability of tenure for residents as part of the expansion of affordable housing service provision in Australia. Therefore models that are predicated upon substantial portfolio recycling - to recognise yield through property values- are unattractive.

Federation Financial Intermediary Project Plan

- Specialist reference Group established.
- Summary of principles document -end of March 2016
- Investigation of governance, legal and regulatory arrangements for both Intermediary and for the community housing industry – May 2016
- Model costings – establishment and ongoing – May 2016
- Draft business case – mid June 2016
- Final for building profile and pursuing funding – July 2016

We envisage that the Intermediary will have the following characteristics:

- Be independent of government
- Be structured as a not for profit

- Be governed by a professional board with directors drawn from the financial, legal, housing regulatory and government sectors and individuals with specialist knowledge of the community housing industry

- Will facilitate credit ratings for aggregated financings

- Enable the development of a stable, new asset class in aggregated rental residential property

- Sidestep the need for community housing providers to individually build scale (though it will be for individual providers to decide whether to participate).

The Intermediary has attractions to the institutional investors. It will allow passive investment and not require investors to specialise in assessing the risk of what is a complicated rent and subsidy structure.

Challenges in the Australian Context

The project will also consider the challenges in the Australian context, specifically the limited long-dated bond market and the implications of negative gearing taxation settings which skew rental housing investment away from aggregated institutional solutions. It will also consider the Intermediary as a market-maker, which is creating a new asset class in securitised rental housing and establishing a longer-dated debt tenor, which may rely on some form of credit enhancement to overcome these Australian challenges and establish this mechanism. Again, because this aggregator will require some flow of funding to aggregate, the Intermediary's establishment will await government direction on the various layers of financial support necessary to underpin private affordable housing activity.

Once the business case has been established we intend to market test and consult with government. Likely issues which will require input include:

- Balancing the need for some government credit support in making the market, such as the guarantee, with the need for institutional investors to nevertheless take appropriate risk. The government will not bear inordinate risk; only reasonable exposure given that regulatory systems exist. In NSW all community housing industry members are registered in the National Regulatory System (NRS).

The importance of strong regulation

Comfort to lenders and investors by ensuring minimum standards of governance and promoting financial viability, thus lessening the probability of financial default.

Access to private finance for regulated providers at rates that reflect the perception that the sector constitutes a low-risk long term investment.

Safeguards for government as a major investor, and in terms of its key objectives for the affordable housing sector.

Protection for tenants.

In the UK the presence of regulation is one of the major reasons that there has been no incident of default by a regulated provider that resulted in loss to the lenders or investors

- The Intermediary does not ‘work’ in isolation: other layers of routinely-accessible housing development funding are essential. The Intermediary provides longer-dated stable debt based on rental surplus repayments, which may finance perhaps 50-60% of development costs depending on their affordability level.

National regulation

A single strong national regulatory system is essential, one in which both government and investors can have confidence. While this submission is made by the NSW Federation we recognise the applicability to other jurisdictions. The continued existence of three separate regulatory frameworks needs to be urgently addressed by the Commonwealth and State Governments. In addition, the national system’s operation needs to be sufficiently flexible to evolve as the community housing industry and in particular the financial instruments become more sophisticated. In these circumstances the regulators’ financial review and engagement needs to be similarly sophisticated. There also needs to be an agreed definition of community housing asset and whether this should include all below market rented housing.

The Federation has raised a number of issues already concerning the regulatory framework and its operation. We have a noted some overarching concerns below and further detail is available. We should however note the concerns are about the system and not the individuals involved.

The Federation believes the governance of the NRSCH also needs to be strengthened. It is unclear where responsibilities lie between the individual registrars who report to their respective Ministers, the Registrars’ Forum and the state / territory funding agencies. We are also unclear as to how the proposed advisory committee fits into this system. While the process for a provider to register an appeal about a decision is straightforward it is less than clear how the overall performance of the system is assessed and evaluated. Further engagement with the industry and key stakeholders, such as investors, should be improved both at a state level (at least in NSW) and the Commonwealth. We have suggested the National Consultative Forum that operated during the NRSCH development is a model for future engagement with the community housing industry.

Equally, the visibility of the regulatory system needs to be enhanced through both publication of aggregated industry information and engagement with key stakeholders. The publication of more analytical reports akin to those issued by the English regulator, the Homes and Communities Agency, is recommended.
In short, to attract private institutional finance to the affordable housing sector, the Commonwealth Government needs to immediately reengage with National Regulation and provide the leadership and direction the system currently lacks.

Implementation

Once the Financial Intermediary business case has been completed and the proposal achieves support from stakeholders, funding to establish the infrastructure and legal framework for the Intermediary will be required. This will include to:

- Establish the governance structure
- Document the legal framework
- Provide the initial capitalisation of industry-funded, first-call reserve fund (which is likely to be supported by fees thereafter)
- Document tripartite agreements delineating government limited guarantee
- Design the contestability process for participation in Intermediary finance and underwriting the feasibility of project and creditworthiness of borrowers.

Sources of industry-capitalised first-call reserve fund will need to be negotiated and could conceivably come from a range of sources including (in NSW) from the second phase of the Social and Affordable Housing Fund (SAHF), the Clean Energy Finance Corporation and superannuation funds.

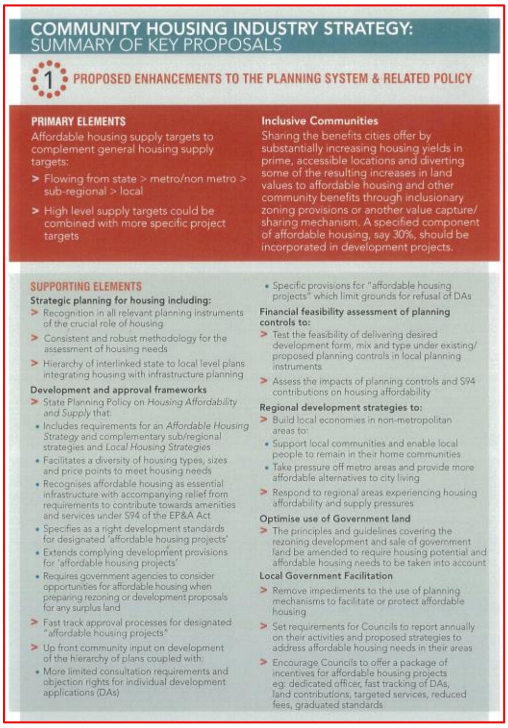
This would ideally culminate in either a 'proof of concept' or an initial seed fund issue possibly to aggregate the re-finance of short-term, commercial bank debt of the participating providers (which currently amounts to over $200 million in NSW alone).

Not a silver bullet – the role of government

The Financial Intermediary will be successful only if it is predicated upon stable, on-going government support for affordable housing in a form that underpins institutional investor confidence. Critical for the Financial Intermediary to facilitate a new market in aggregated rental investment will be a partial government bond guarantee in the short to medium term, which would reduce perceptions of new market and sovereign risk and therefore reduce the costs of finance. This would result in more value for money for other government financial support as lower risk margins mean cash flows will stretch further.

The guarantee is unlikely to be required to be cash-backed according to current accounting standards due to several defensive layers of regulatory and reserve fund protection (potentially in NSW from the SAHF). Other government action and initiatives would maximise the Financial Intermediary's overall impact. Bond (debt) finance will part-fund new social and affordable housing, but there will also need to be seed equity in the form of assets or land. Some limited grant funding targeted specifically at community housing providers to enable this equity transfer could be sourced from the NSW SAHF and act as a further catalyst for leveraging. Alternatively, government could provide land at discounted prices or via a trust type model, whereby government retains ownership but leases at nominal rents to providers. Both are potential options.

Below we have highlighted the key issues in which the Commonwealth and State governments could act together to tackle housing unaffordability.



COMMUNITY HOUSING INDUSTRY STRATEGY:
SUMMARY OF KEY PROPOSALS

1 PROPOSED ENHANCEMENTS TO THE PLANNING SYSTEM & RELATED POLICY

PRIMARY ELEMENTS

Affordable housing supply targets to complement general housing supply targets:

> Flowing from state > metro/non metro > sub-regional > local

> High level supply targets could be combined with more specific project targets

Inclusive Communities

Sharing the benefits cities offer by substantially increasing housing yields in prime, accessible locations and diverting some of the resulting increases in land values to affordable housing and other community benefits through inclusionary zoning provisions or another value capture/sharing mechanism. A specified component of affordable housing, say 30%, should be incorporated in development projects.

SUPPORTING ELEMENTS

Strategic planning for housing including:

> Recognition in all relevant planning instruments of the crucial role of housing

> Consistent and robust methodology for the assessment of housing needs

> Hierarchy of interlinked state to local level plans integrating housing with infrastructure planning

Development and approval frameworks

> State Planning Policy on *Housing Affordability and Supply* that:

- Includes requirements for an *Affordable Housing Strategy* and complementary sub/regional strategies and *Local Housing Strategies*
- Facilitates a diversity of housing types, sizes and price points to meet housing needs
- Recognises affordable housing as essential infrastructure with accompanying relief from requirements to contribute towards amenities and services under S94 of the EP&A Act
- Specifies as a right development standards for designated 'affordable housing projects'
- Extends complying development provisions for 'affordable housing projects'
- Requires government agencies to consider opportunities for affordable housing when preparing rezoning or development proposals for any surplus land

> Fast track approval processes for designated "affordable housing projects"

> Up front community input on development of the hierarchy of plans coupled with:

- More limited consultation requirements and objection rights for individual development applications (DAs)
- Specific provisions for "affordable housing projects" which limit grounds for refusal of DAs

Financial feasibility assessment of planning controls to:

> Test the feasibility of delivering desired development form, mix and type under existing/proposed planning controls in local planning instruments

> Assess the impacts of planning controls and S94 contributions on housing affordability

Regional development strategies to:

> Build local economies in non-metropolitan areas to:

- Support local communities and enable local people to remain in their home communities
- Take pressure off metro areas and provide more affordable alternatives to city living

> Respond to regional areas experiencing housing affordability and supply pressures

Optimise use of Government land

> The principles and guidelines covering the rezoning development and sale of government land be amended to require housing potential and affordable housing needs to be taken into account

Local Government Facilitation

> Remove impediments to the use of planning mechanisms to facilitate or protect affordable housing

> Set requirements for Councils to report annually on their activities and proposed strategies to address affordable housing needs in their areas

> Encourage Councils to offer a package of incentives for affordable housing projects eg: dedicated officer, fast tracking of DAs, land contributions, targeted services, reduced fees, graduated standards

Planning Mechanisms

The Federation's planning strategy sets out our proposals for enhancements to the planning system and related policy, many of which have national relevance. In the strategy we argue that the benefits from substantially increasing housing yields should at least in part be diverted into affordable housing. If the opportunity to realise affordable housing, and related community benefits, from rezoning and redevelopment is not to be missed, then in NSW it is urgent that the government acts, given the many urban and regional development and regeneration zones already announced.

In the 2015 Future Cities collaborative publication, *Can you afford to live where you choose? – Local Approaches to making it affordable for people to live in their communities*. http://www.futurecities.org.au/sites/fcc/media/467.pdf, the economics of inclusionary zoning are well summarised. It will be considerably more difficult to argue for an affordable housing contribution where a requirement is not made explicit at the earliest possible opportunity. In all circumstances, negotiations to secure affordable housing will be challenging, and the Federation recommends that State governments develop robust and reliable site feasibility models to assess what affordable housing contributions can be supported.

Property Transfer to the Community Housing Sector

The Federation's property transfer position paper outlines our proposals to optimise the outcomes from transferring property from public housing to the community housing industry.

Our position on a Property Transfer Program

The ability of the community housing industry to optimise the outcomes of the NSW Government's Social Housing Policy will depend on policy decisions, including whether the Government offers title or management transfers, the term of a management lease and expectations around property condition.

The NSW Federation of Housing Associations has conducted a series of workshops with our members to determine a common position on what they think a PTP should achieve and how we can partner with Government in its design and implementation.

Strategic objectives

We believe that an effective PPT should have the following strategic objectives:

1. To achieve a viable and interconnected social housing system.
2. To be highly responsive to the needs of tenants and communities.
3. To further develop business models and structures that deliver the benefits of efficiencies of scale, while retaining local services, areas of specialization and the flexibility to respond to tenants' needs.
4. To maximize public value through community housing providers combining their rental income with other government subsidies, tax benefits and private finance to provide additional, low cost, housing.
5. To undertake major renewal of public housing neighbourhoods, maximise community renewal outcomes through long term investment and improve tenant and community engagement and asset redevelopment.

We believe there is scope for the Commonwealth and State governments to work towards establishing 'good practice guidelines' for effective Australian property transfer to the community housing industry. While individual State governments will retain the decision around whether and, if so, how to transfer properties to community housing providers, there are issues around accounting treatments, valuation standards and methodologies, contractual agreements and resident involvement. It will be appropriate for the community housing industry to be involved in these discussions.

Construction Finance

It is important to note that bond finance is generally unavailable to fund construction costs. Rather, it is based on stable operating phase cash flows. In NSW, the SAHF (for example) could be set aside to fund a revolving construction debt facility that gets repaid at completion, when taken out by operating phase bond finance or with market-rate sales within mixed tenure development. This would be revolving and recycled to new projects. Similar mechanisms will be required in other jurisdictions.

Broader Economic and Social Benefits

The Federation notes that the Affordable Housing Working Group Issues Paper notes that submissions should take into account the overall fiscal environment across the Commonwealth, states and territories. While acknowledging these, the Federation believes there is scope both to put existing transfers between the Commonwealth and states to best use by ensuring that these are tied to projects, programs and providers that increase supply and also improve tenant and community outcomes. As was noted at the Sydney roundtable by one Treasury official, governments are being asked to account for subsidy allocation and the outcomes achieved. This should apply to all sectors. One aspect of achieving these broader outcomes is the way that community housing providers can work with specialist homelessness services to address the needs of this population. Establishing funding certainty well before the 2017/18 financial year starts must be a government priority.

In addition it is increasingly recognised that adequate well located housing has wider economic and social benefits. Indeed, it is anticipated providers in NSW will have additional contractual obligations tying payments to broader social outcomes. The Federation encourages both Commonwealth and State governments to consider reallocating government expenditure towards housing in recognition that secure long term affordable housing will have positive long term fiscal impacts.

The NSW community housing industry recognises the obligation and is already involved in self-initiated projects to demonstrate performance. From the multiple initiatives, we highlight three taking place:

- Enhancing the Federation's HouseKeys – a comparative database to include cost efficiency measures using the methodology trialed in the AHURI project 71025, Cost effectiveness and tenant outcomes in social housing. Note this project includes non-NSW providers www.ahuri.edu.au/publications/projects/p71025#sthash.MTFdaGn9.dpuf
- Participating in a joint project with the Centre for Social Impact and Homelessness NSW to develop shared housing and homelessness indicators
- An initiative led by three providers to develop an Australian Social Return on Investment model.

Strategic Commissioning

At the Sydney roundtable, officials raised towards the session close whether a similar body to the English Homes and Community Agency (HCA) might be applicable in the Australian context. The HCA has multiple roles including that of regulator. It is also responsible for increasing the number of new homes that are built in England, including affordable homes and homes for market sale or rent; improving existing affordable homes; improving existing affordable homes and bringing empty homes back into use as affordable housing; increasing the supply of public land and speeding up development and helping to stimulate local economic growth by using its own land and investment; and attracting private sector investment in local areas. Such an approach at the Commonwealth and / or State levels is worthy of further consideration and research, providing it does not prevent short term action to address housing unaffordability.

The Federation can see the benefits in a tightly timetabled review of current practices and an examination of other models – not just in the UK- with a view to developing a strategic commissioning framework for social and affordable housing that:

- Is underpinned by a robust needs analysis articulated in housing plans
- Minimises procurement and management costs to government and community housing providers and their partners
- Facilitates the process through, for example, land assembly and stimulation of investment,
- Estimates the supply and other policy objectives that could realistically be achieved.

Community housing and Government can work in partnership to deliver excellent outcomes. Together, we make a significant difference to housing supply and economic prosperity.

For more information contact **Wendy Hayhurst**, CEO, WendyH@communityhousing.org.au, 0421 046 832
NSW Federation of Housing Associations. 301/64 Kippax Street, Surry Hills NSW 2010.