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FINANCIAL IMPACTS OF ASSET TRANSFERS

FROM STATE / TERRITORY GOVERNMENTS TO COMMUNITY HOUSING ORGANISATIONS

Prepared for

National Shelter

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LIST OF ACRONYMS

AHURI	Australian Housing and Urban Research Institute
DSS	Department of Social Services
ICR	Interest Cover Ratio
LVR	Loan to Value Ratio
NAHA	National Affordable Housing Agreement
NRAS	National Rental Affordability Scheme
SHI	Social Housing Initiative
UNSW	University of New South Wales

LIST OF DEFINITIONS

Loan to Value Ratio (LVR)	The ratio debt as a percentage of the total appraised value of property.
Interest Cover Ratio (ICR)	An organisation's earnings before interest and taxes (EBIT) over one period by the organisation's interest expenses of the same period.
Impaired Asset	An asset that is worth less on the market than the value assigned on the company's balance sheet
Director's Interest	A system of limiting the free disposal of an asset following title transfer where a representative of the former owner retains an interest on the title and is able to stop inappropriate transactions (i.e. sale for profit).

1.0 INTRODUCTION

This study was undertaken by Sphere for National Shelter in August 2013 in order to provide a review of the financial impacts of the transfer of social housing assets from State/Territory governments to community housing providers. Funding for the study was provided by the Department of Social Services (DSS), [formerly the Department of Families, Housing, Community Services and Indigenous Affairs].

1.1 CONTEXT FOR THIS REPORT

National Shelter has recently been conducting a project to gather feedback from stakeholders around Australia about the operation of the National Affordable Housing Agreement (NAHA) since its commencement in 2009.[1] The project has involved extensive work to identify issues of concern to stakeholders and areas where National Shelter may be able to contribute strategic advice to government on housing policy reform that supports the reduction of homelessness and the increase of affordable housing supply through the NAHA and other policy platforms.

The current study has been commissioned to build on this work by focusing on one of the key issues which has emerged from National Shelter's NAHA consultations: the financial impacts on both governments and community housing providers of the transfer of social housing assets.

This study specifically focuses on this one area of investigation. It takes place against the background of much broader research in this area undertaken by Professor Hal Pawson and colleagues for the Australian Housing and Urban Research Institute (AHURI)[2]. The aims of the AHURI project, entitled *Public housing stock transfers in Australia: past, present and prospective* include the following:

> *What policy, operational and financial barriers would need to be overcome to support larger-scale tenanted transfers in future?*

What policy, operational and financial barriers would need to be overcome to support larger-scale tenanted transfers in future? The current study is intended to complement this larger project by providing modelling which can inform specific policy conversations about the financial impacts of transfers, including testing of sensitivities to different scales and types of transfer. It is also intended to be a response to the specific issues raised in the NAHA consultations.

1.2 RESEARCH SCOPE AND ACTIVITIES

Research for this study has focused on understanding the financial impacts of stock transfers, for both governments and community housing providers. Specifically, it addresses issues around:

- The impact of stock transfer, both management rights only and title, on the financial performance of community housing organisations
- The ability of community housing organisations to leverage further funds and development opportunities on transferred assets

[1] For more detail on the broader project, see National Shelter National Affordable Housing Agreement Consultations reports, June 2013.

[2] Pawson, H., Milligan, V., Wiesel, I. and Hulse, K. (2013), Public housing transfers: past, present and prospective, AHURI Final Report No.215. Melbourne: Australian Housing and Urban Research Institute.

- The impact on the credit rating and balance sheet of State and Territory governments of the title transfer of social housing assets to community housing organisations.

The study did not address other important issues such as the implications for tenants of transfers or the transfer process. Some aspects of this are considered in the AHURI research discussed below.

The study uses both qualitative research and quantitative analysis to explore the perspectives and experiences of governments, community housing providers, and other key stakeholders in Australian jurisdictions. The original study methodology involved:

- Review of literature and current policy on stock transfer to community housing organisations in Australia, and of key international evidence
- Interviews with:
    - Representatives from Treasuries and Housing Authorities in four Australian jurisdictions which have had significant activity in transfers to date: Queensland, New South Wales, Victoria and Tasmania
    - Representatives from community housing organisations in the same four jurisdictions
    - Officers from financial institutions which have been involved in providing finance to housing providers
    - Standard and Poors rating agency
    - Representatives from the NSW Federation of Community Housing Associations
- Modelling of financial impacts of stock transfers to explore the relationship between title transfer and the growth potential of community housing providers.

Research, analysis and reporting have been undertaken during a tightly restricted time period of four weeks. This has meant that it was not possible to conduct all the desired interviews. In particular, it proved impossible to secure interviews with representatives from Treasury Departments (apart from Tasmania) at such short notice.

2.0 CURRENT SITUATION

This section of the report contains an overview of current policy and practice regarding the transfer of social housing assets to community housing providers.

2.1 BACKGROUND: ECONOMIC IMPACTS OF THE UK EXPERIENCE OF ASSET TRANSFERS

Stock transfers can be seen as part of the new directions for many Australian jurisdictions following international trends towards:

- Separation of housing from central government
- Improving the financial viability of housing providers.

Research is currently being undertaken by Pawson, for the AHURI, on the lessons to be learned in Australia from the United Kingdom (UK) experiences of stock transfer, which focused around 'reinvigorating' social housing both financially and culturally by changing its management and ownership. Pawson notes that the benefits identified by the UK Government since it began actively promoting transfer activity in 1997 included:

- Channelling investment to remedy neglect
- Reforming organisational governance to 'empower tenants and disadvantaged communities'
- Stimulating beneficial culture change.[3]

The underlying assumptions for this policy direction were that British Housing Associations (HAs), (equivalent to Australian community housing providers) were better placed than local governments to access private finance to conduct repairs and modernisation, and would provide better governance and tenancy management services. It was also hoped that HAs would be better at implementing asset management programs and portfolio approaches to stock redevelopment, and that their business models and organisational practices would be more flexible and responsive.

In these areas – and many others – Pawson's 2009 review of transfers found that the transfer policy had been effective and HAs had exceeded expectations.[4] Transfers assisted to achieve better outcomes for tenants, providers, and governments. In terms of the economic impacts on HAs, Pawson described the debt profile associated with stock transfers as being substantial and incurring significant risk during the early years (as shown in Figure 1)[5].

However, it should be noted that in the United Kingdom that the stock was purchased by HAs (at a discounted rate). This resulted in the higher levels of debt up front. It is also worth noting that the income streams of HAs in the United Kingdom are more robust than in Australia because of the generous Housing Payment.

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[3] *Transforming Australia's Social Housing Sector: Pointers from the British Stock Transfer Experience*, Hal Pawson presentation to 6th National Housing Conference, Edinburgh 2009.

[4] For details see *The Impacts of Housing Stock Transfer in Urban Britain,* Pawson, H., Davidson, E., Smith, R. & Edwards, R. , Chartered Institute of Housing (for the Joseph Rowntree Foundation), 2009. Available at www.jrf.org.uk

[5] It is worth noting that UK housing associations had to buy the stock (at a discounted rate. Furthermore, their income streams are more robust due to government housing payments.

Finally, the goals of stock transfer in the United Kingdom were focused more on estate renewal and modernisation, as well as providing additional and better services to tenants. In Australia, the focus is predominantly on growth.

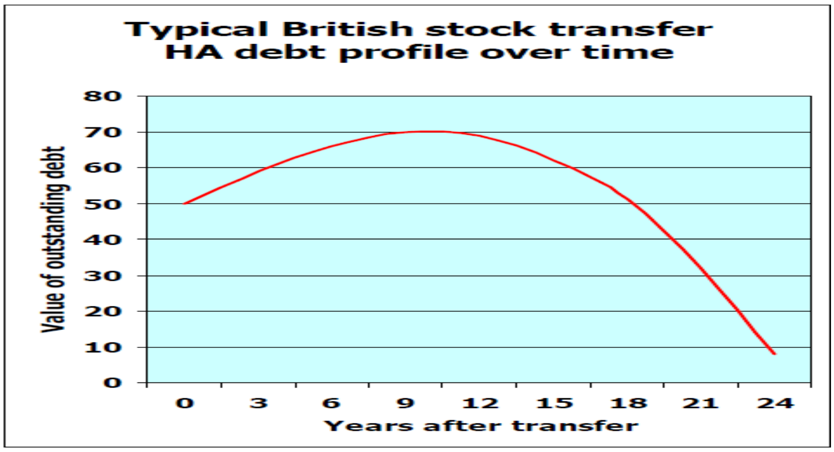

Figure 1: From slide 13 of Pawson's presentation: Transforming Australia's Social Housing Sector (see note 3)

While Pawson found that some HAs required 'rescue' by larger organisations during the period of greatest debt, none defaulted on their obligations. Mergers and diversification of business models among HAs have protected them from failure. However, he identifies two major dangers to the successful 1997-2009 model of stock transfers arising from changes in international economic circumstances:

- The threat of deflation – especially for organisations in the first 10-12 years of the transfer profile debt curve
- Increased difficulty in securing financing for new transfers.[6]

Pawson's comparative work suggests that similar dangers associated with exposure to market trends are relevant for community housing providers in Australia and that in order to avoid the necessity of selling stock in order to repay debt, policy should be developed and fine-tuned with consideration for changing market factors which may impact on providers' ability to secure and service debt.

2.2 AUSTRALIAN NATIONAL POLICY ON TRANSFERS

Significant reform of the Australian social housing sector was introduced in 2009 with a network of interrelated programs and initiatives associated with the NAHA.[7] One objective of the reforms is to strengthen the role of the community housing sector in terms of both its scale and its capacity to respond to housing need.

The key national policy statements relevant to the transfer of social housing assets from State / Territory governments to community housing providers are:

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[6] Ibid.

[7] For an overview, see National Shelter National Affordable Housing Agreement Consultations reports, June 2013.

- A stated target of growing the community housing sector so that it comprises up to 35% of social housing stock by July 2014[8]
- An expressed intention that up to 80% of new stock constructed under the Social Housing Initiative (SHI) (part of the Nation Building – Economic Stimulus Plan) would be transferred to community housing providers, and up to 50% would also have title transferred.[9]

While the NAHA has been designed at a national level, individual States / Territories have responsibility for its implementation, through local policy frameworks and initiatives. One factor which operates as an incentive for States / Territories to implement transfers is the current design of Commonwealth Rent Assistance (CRA): this payment from the Commonwealth Government is not available to tenants of government housing but is available to community housing tenants. It enables the rent paid to the housing provider to be set closer to market rent, while maintaining the same after-housing income as similar public housing tenants. This can increase rent paid to the housing provider, and can increase revenues very significantly (see section 4.4).

Alongside policies on transfers and rental assistance, there has been a continuing commitment to the development and implementation of a nationally consistent regulatory framework for community housing providers (National Regulatory System Community Housing). The regulatory framework is intended to support greater flexibility and consistency in inter-State/Territory operations and allow providers to operate more easily across jurisdictional boundaries. A major aim of the regulatory framework is the assurance of standards for the governance and viability of providers which protect government funding and equity in the sector and enhance investor and partner confidence. The implementation of this system has commenced in most jurisdictions and the first round of registrations is expected to be complete by mid-2015.

2.3 OVERVIEW OF TRANSFERS TO DATE

In Australia, the bulk of transfers have occurred as part of the Nation Building Economic Stimulus – Social Housing Initiative (SHI) program. Between 2010 and 2012, 10,800 properties developed under this program were transferred to community housing providers, approximately 5,000 of which were transferred with title and the remainder with management rights only[10]. This represents approximately 3% of the total public housing stock in Australia.

In addition to this, three states and the Australian Capital Territory had transferred stock prior to the SHI. Only New South Wales and Victoria had transferred titles, with all other transfers being management contracts only. In all across these three jurisdictions 10,500 dwellings were transferred prior to the SHI, with 1,000 of these involving transfer of title.

Figure 2 summarises the state of transfers to 2012.

[8] Implementing the National Housing Reforms: A progress report to the Council of Australian Governments from Commonwealth, State and Territory Housing Ministers, November 2009,page 26. Available at www.coag.gov.au.

[9] *Social Housing Initiative Review*, Housing Ministers' Advisory Committee (KPMG), September 2012, p33. Available at www.fahcsia.gov.au.

[10] Pawson et at, 2013, p21

Figure 2: Tenanted public housing management and asset transfers 1995–2012, completed transactions (dwellings)

	ACT	NT	NSW	Qld	Tas	Vic	WA	SA	National
Pre-SHI transfers									
Tenanted management outsourcing	240 (1)		7,861	153		1,431(2)			9,685
Tenanted title transfers			400			575			975
Total pre-SHI transfers	240 (1)		8,261	153		2,006			10,660
SHI Transfers									
Management outsourcing only	74		2,920 (3)	2,579	249				5,822
Asset transfers			3,099				1,291	616	5,006
Total SHI transfers completed2	74		6,019	2,579	249		1,291	616	10,828
Total									
Total management transfers 1995-2012	*314*		*10,781*	*2,732*	*249*	*1431*			*15,507*
Total asset transfers 1995-2012			*3,499*			*575*	*1,291*	*616*	*5,981*
Total Transfers	*314*		*14,280*	*2,732*	*249*	*2,006*	*1,291*	*616*	*21,488*

1. The ACT figure refers to the 'Community Housing Program', 1998–2001, which involved management outsourcing for 209 public housing dwelling. Seventy-seven of these dwellings were returned to management by Housing ACT in 2007. Titles of the remaining 132 dwellings were transferred to a CHP in 2007 when they were redesignated for future use as affordable housing.

2. Aboriginal Housing Victoria (AHV) transfer included 200 homes transferred with vacant possession as part of a transaction largely involving tenanted

3. Homes developed by Housing NSW with management outsourced to CHPs immediately upon completion and intended for future 'vesting' (or title transfer), but remaining in state government ownership at the time of the survey.

4. These figures do not include dwellings funded under the stimulus package but procured or developed directly by CHPs (e.g. in Victoria and Queensland).

Source: Adapted from Pawson, H., Milligan, V., Wiesel, I. and Hulse, K. (2013), *Public housing transfers: past, present and prospective*, AHURI Final Report No.215. Melbourne: Australian Housing and Urban Research Institute, pp20, 21

Overall, transfers of stock to date have been characterised by:

- Slow progress towards 2009 stated aim for up to 35% of social housing to be managed by CHPs by 2014 and lack of scale in transfers to date
- Considerably greater transfers of management contracts than of property titles
- A high proportion of existing transfers arising from developments under the SHI, rather than from longer-term public housing stock – especially the more recent transfers.

In addition, a number of community housing organisations have received contributions from State / Territory governments to support the development of social housing stock, either through cash, loans, or land. These contributions have provided equity for growth and development of portfolios for some providers. [11]

2.4 STATE / TERRITORY POLICIES AND PRACTICES

For each jurisdiction, this section of the report provides an overview of the stated government policy position, as well as historical and expected future approaches to transfer of public housing assets.

2.4.1 QUEENSLAND

Queensland is committed to large scale transfers of management contracts to support renewal of its social housing stock. Key features of its policy framework are outlined in the following table.

Policy framework	The Queensland Government has recently announced a new policy in this area, committing to an intention to transfer 90% of the management of all social housing dwellings to the non-government sector by 2020[12]. An implementation plan is currently in development, due for release in November. Policy also supports consolidation of providers.
Implementation	As at 31 December 2012, approximately 75% of social housing stock (54,394 dwellings) is managed by the state government and almost 25% (17,935 dwellings) is managed by non-state government organisations such as (not-for-profit community organisations, local governments, including Indigenous councils)[13] Implementation of transfer policy focuses on tenancy management transfers and provision of funding and/or land for developments, to be repaid in kind as social housing.
Progress to date	The first major transfer project is the Logan Renewal Initiative, involving 20-year management contracts for up to 5,000 dwellings. This is currently in the second stage of its tender process[14].
Future plans	Anticipate to achieve 90-100% transfer of management contracts by 2020.

In addition to this, some properties previously built by providers using government funding over past decades have had their titles transferred in specific cases; this is not part of general policy.

[11] For more detail, see National Shelter National Affordable Housing Agreement Consultations: National Report, June 2013.

[12] Department of Housing and Public Works, *Housing 2020: Delivering a flexible, efficient and responsive housing assistance system for Queensland's future,* Queensland Government, 2013. P8

[13] *Housing 2020*, pp3, 5

[14] See www.communities.qld.gov.au/housing/housing-services/social-housing/reforming-housing-assistance-in-queensland

The approach to the delivery of new policy in Queensland is not yet fully developed, and terms for transfers have been negotiated very much on the basis of individual cases. Government wishes to build the sustainability of the community housing sector and considers the Logan initiative to be an opportunity to learn and refine expectations and requirements for future transfers.

While responsive and cyclical maintenance is transferred, it is not yet clear who will have responsibility for structural and long-term maintenance of transferred properties.

2.4.2 NEW SOUTH WALES

New South Wales has transferred by far the greatest levels of stock. Properties transferred to housing providers in this state account for 67 per cent of all transfers across Australia (twice as much as NSW's population share).

There have been delays in the actual 'vesting' of titles agreed in 2010 associated with the change of government which are expected to be overcome during 2013-14. Other key features of the policy context are outlined below.

Policy framework	Community Housing Asset Ownership Policy (May 2011) allows not-for-profit companies registered as Class 1 or Class 2 community housing providers under the Housing Act 2001 to own government funded housing. If a registered provider ceases to operate, its assets remaining after payment of its liabilities must be transferred to another registered provider meeting the same criteria.[15] 2007: Growth target of 30,000 social housing properties by 2017[16]
Implementation	From 2009: 3,500 properties transferred (management only) to housing providers in 17 portfolio locations under Property Transfer Program. Title transfer under Social Housing Initiative (SHI) with individual leveraging targets negotiated with individual providers. Proceeds from any sales to be reinvested in supply with no net loss of units Strong regulatory code to support asset management and portfolio planning.
Progress to date	6,000 units transferred under SHI (title) with additional large scale transfers at Bonnyrigg and Dubbo 1,005 dwellings transferred in Blue Mountains and South West Sydney (management only) under Property Transfer Program.
Future plans	Delayed title transfer promises to be honoured, but new transfers likely to be of management contracts only for next few years. New government appears to have higher expectations about levels of leveraging.

[15] See p3 of *Community Housing Asset Ownership Policy* (May 2011). Available at www.housing.nsw.gov.au.

[16] See Planning for the Future: New directions for community housing in New South Wales (December 2007). Available at www.housing.nsw.gov.au.

Government retains a statutory interest in land vested in a provider, procured using government funding, or acquired using the proceeds of sale of government land. This is registered on the title. Consent is required to sell, mortgage, lease, redevelop or subdivide the land – except for the purposes of providing community housing.

The NSW Affordable Housing Guidelines (July 2013) expressly indicate that responsibility for all levels of maintenance, from responsive through to stock replacement, sits with the community housing provider if the stock is vested or leveraged with them.[17]

2.4.3 TASMANIA

Tasmania is committed to targets of transferring 35% of its social housing stock into management by community housing providers. It has no policy to transfer any titles. Key policy features are described below.

Policy framework	In October 2011, Cabinet endorsed the national target of transfer of 35% of stock. This target is for 10-20 year management contracts only; there is no intention to transfer title of existing public housing assets. Vacant land can also be transferred for the purpose of development for social housing. The aim is to reduce the decline in quality and quantity of social housing stock in the state.
Implementation	Better Housing Futures program aims to transfer up to 4,000 properties (management) of 13,500 total
Progress to date	500 units in the Rokeby Clarendon Vale area had been transferred by 2013 Over 85 per cent of Tasmania's 530 SHI dwellings have been transferred (with 230 dwellings developed by community housing providers) No vacant land has yet been transferred.
Future plans	Tenders for construction and transfer (management) of up to 3,500 new dwellings across North West, North, and South of the state are under consideration July 2013. 120 vacant plots are available.

No specific requirements are placed on providers to leverage against transferred assets. The approach is one of risk-sharing and partnership, with targets negotiated during each individual tender process to take account of factors such as:

- Condition of assets and extent of deferred maintenance burdens (12 months is usually allowed for condition assessment)
- Organisational capacity and appetite for risk
- Potential to reduce decline in overall levels of stock; if there is potential for growth in stock (often through NRAS incentives), revenue-sharing arrangements are also negotiated
- Length of time for development plans for vacant land, and usages of newly built stock e.g. build 10: sell off 4, use 2 as NRAS, keep 4 for long term housing.

Tasmania is currently exploring options to increase regulation of providers and improve protection of assets.

[17] See p10 of *NSW Affordable Housing Guidelines* (July 2013). Available at www.housing.nsw.gov.au.

2.4.4 VICTORIA

The Victorian Government released an new Housing Policy Framework in March 2014.[18] Key features of past policy and the future directions flagged in this framework are outlined below.

Policy framework	Discussion papers released in April 2012 articulate the unsustainability of the current social housing system and call for an entirely new approach.[19] The options paper outlines models for the development, transfer, and financing of social housing, all of which involve increased participation by non-government organisations. Analysis undertaken by KPMG favours public private partnerships, stock transfers, government guarantees to support leverage, and discussions with financiers. The final framework document commits the Director of Housing to consider a strategy for stock transfer to the community hosuing sector and to continue to test the viability of PPP arrangements.
Implementation	Some transfers (of title and management) occurred prior to 2008. From 2008, as part of the SHI, direct funding was also provided to housing associations by government at the rate of 75% of development costs of new housing (and there has also been some 100% funding) In 2012, eight Housing Associations (larger development organisations) owned or leased 9,000 properties while 33 housing providers (primarily tenancy managers) managed 5,000 properties (and a further 4,000 for transitional housing); this is about 20% of Victoria's total social housing stock
Progress to date	2008 Asset Conversion Strategy: 575 transfers of dwellings (title) to Housing Associations, with expectation of 15% portfolio growth through leveraging; also transfers of management contracts. While a report by the Victorian Auditor in 2010 suggested that 5 of the 8 Housing Associations who received transfers had not met the leverage target, the Community Housing Federation of Victoria has argued that there was specific agreement to defer this in order to meet SHI deadlines, and that all but one have now done so[20] There have been no transfers since 2008: awaiting outcome of policy review
Future plans	The New Directions for Social Housing document flags a target of up to 12,000 social housing dwellings transferred to the community housing sector, with further details to be developed. At this stage the strategy doesn't specify whether these are to be trasnfers of title or management transfers.

Victoria retains a Director's Interest on the titles of any properties transferred, to ensure that stock is used for social housing purposes and that overall numbers of properties do not decline.

[18] *New Directions for Social Housing: A Framework for a Strong and Sustainable Future,* Victorian Government, March 2014

[19] *Pathways to a fair and sustainable social housing system* and *Social Housing; A discussion paper on options to improve the supply of quality housing* (KPMG), April 2012. Both available from www.dhs.vic.gov.au.

[20] Victorian Auditor General Office *Access to Social Housing*, June 2010, reported in *Pathways* discussion paper (above). It must be noted that the conclusions of this review have been challenged: Work conducted by the Community Housing Federation of Victoria has shown that only one organisation did not achieve 15% leveraging, and this outcome was known to the government when they transferred the stock.

2.4.5 OTHER JURISDICTIONS

WESTERN AUSTRALIA

In 2010, Cabinet endorsed the national targets for transfers. The Western Australian (WA) Affordable Housing Strategy aims to provide 20,000 affordable housing options by 2020. At February 2013, 1,400 housing assets had been transferred to 8 providers, with a growth target of a further 500 units over the next ten years.

SOUTH AUSTRALIA

Under *Better places stronger communities,* South Australia has committed to up to 5,000 transfers of management contracts to community housing providers by 2018, beginning with 2 packages of 500 properties. The government is considering longer contract terms than it has used in the past, to support leverage for growth.

In June 2013, the SA government called for expressions of interest for the transfer of title to 2 packages of 500 properties over the next 18 months, with a growth expectation of a further 100.

AUSTRALIAN CAPITAL TERRITORY

In 2013 there were 590 tenancies managed by community housing providers, compared to 10,956 public housing tenancies[21]. Title transfers have been very limited and there is some resistance to this approach at policy level. Most providers have limited scale and capacity and have not received transfers. However, the one large community housing development provider, supported by an innovative revolving fund of $70m of low interest loans) and some title transfer has delivered a significant favourable outcome in terms of growth.

[21] Report of Government Services 2014, Table 17A.3

3.0 STOCK TRANSFER: ISSUES AND ANALYSIS

This section of the report contains an overview of the evidence collected through interviews of the key issues surrounding the transfers of assets, from the perspectives of governments and community housing providers in four key Australian jurisdictions. It identifies particular perspectives where relevant, and tests them against the available evidence.

3.1 ISSUES FOR GOVERNMENTS

Interviews were conducted with representatives from the relevant State Housing Authority and, where possible, Treasury departments. Research focused on:

- Government understanding of the financial implications of transfers in terms of potential for stimulating growth in social housing provision
- Government perspectives on any potential adverse impacts to them associated with title transfers.

The perspectives of each jurisdiction were shaped by local issues and preferred policy approaches; each is reported separately.

3.1.1 QUEENSLAND

POTENTIAL FOR TRANSFERS TO STIMULATE GROWTH

The focus in this state is on the renewal and reconfiguration of existing stock, rather than on growth. Some growth targets have been negotiated with the specific providers involved in the Logan Initiative tender process, but these are not intended to be general (and nor are they made public). The Government does expect that transfers will bring improved tenant outcomes.

POTENTIAL FOR TRANSFERS TO IMPACT ADVERSELY ON STATE

Caveats on titles are in place to ensure that where title transfer does occur, there is no reduction in the overall supply of social housing, but Queensland has decided not to pursue a general policy of title transfers.

Community housing providers reported that the reluctance to transfer titles originated in Treasury, but Queensland's Department of Housing identified the reasons for lack of large-scale plans for title transfer as being:

- Political sensitivity to the community's preference that assets of this type be owned by government
- Desire to test capacity, processes, and outcomes from the Logan Initiative and build on this experience in future transfers
- Need to manage significant change associated with massive transfer of management contracts and allow for adjustments by both government and providers before adding further innovations.

3.1.2 NEW SOUTH WALES

POTENTIAL FOR TRANSFERS TO STIMULATE GROWTH

The policy settings in NSW are largely driven by delivering stock growth. This state has delivered significantly more transfers than any other jurisdiction (see section 3.4.2). The recent delays experienced in title transfers appear to be related to the new state government wanting further evidence of the capacity of the sector in delivering growth and re-negotiating growth targets, rather than weakness of policy or implementation practice.

The current and planned transfers in NSW will put the proportion of social housing managed by housing providers slightly below the 35% target. At present, the government has not indicated that further stock transfers will be implemented.

POTENTIAL FOR TRANSFERS TO IMPACT ADVERSELY ON STATE

Departmental officers from New South Wales did not express any concerns relating to adverse impacts to the State Government. The government has developed a Tripartite Deed between the Land and Housing Corporation, housing providers and financiers to give financiers a degree of comfort when housing providers take mortgages on their properties. This Deed allows the Land and Housing Corporation to transfer properties to an alternative provider in case of loan defaults and insolvency. At the same time, the Deed provides a remedy in terms of the risks associated with housing providers borrowing and the potential residual liability to the government.

3.1.3 TASMANIA

POTENTIAL FOR TRANSFERS TO STIMULATE GROWTH

The Tasmanian government understands that there is very limited potential to leverage against existing stock, and that any growth could be achieved only through redevelopment and access to NRAS incentives with a focus on stock renewal. Without NRAS, 10-year growth would be limited to 2-2.5% (100-120 units on 4,000 base) but with NRAS it could be 12.5-15% (500 units).

The government also understands the value of CRA but recognises limits on its use in Tasmania. It is estimated that 85% of transferred properties are eligible. However, due to depressed property prices in Tasmania, sometimes CRA cannot optimised because market rents are lower than CRA thresholds. Overall, it is estimated that CRA provides $8m pa in additional landlord income.

POTENTIAL FOR TRANSFERS TO IMPACT ADVERSELY ON STATE

Individual business cases for the transfer of land or assets can be successful, but the decision not to embed a policy of significant transfers of title is based on three key factors:

- Political choice: The government prefers not to 'privatise' state assets on a large scale
- Lack of demonstrated capacity among providers: Providers need to demonstrate that their models can be successful for management prior to considering title transfers e.g. demonstrate realistic assumptions about income levels and maintenance costs
- Lack of strong protections for government: Need for better protection of government assets before transfers of title occur e.g. National Regulatory System, caveats on titles.

These are all factors that may change over time, and title transfers may increasingly occur in future.

The potential impact on state balance sheets is not considered an issue. Assets that are transferred to community housing provider management are recorded as impaired, but not fully written down. The Tasmanian Treasury does not consider social housing assets to be financial because they cannot be converted to cash, and accordingly does not consider there would be any significant impacts on the state balance sheet if titles were to be transferred.

Treasury's concerns are limited to ensuring that Housing remains within its operating budget and protects government assets. It is up to Housing how it achieves these goals.

3.1.4 VICTORIA

POTENTIAL FOR TRANSFERS TO STIMULATE GROWTH

From the perspective of the Victorian Government, the main objective of transfers is the improvement of the condition of existing properties, stock growth and the achievement of improvements in tenant services. Government reports that growth has been focused on building a more sustainable community housing sector. However, providers reported that the government's expectations with respect to the levels of growth that could be achieved were not always realistic.

In recent years, Victoria has achieved significant growth in the numbers of properties under management as well as improvements in their condition.

POTENTIAL FOR TRANSFERS TO IMPACT ADVERSELY ON STATE

The Victorian Government reports that it is strongly aware of the public policy issue of balancing the interests of the most vulnerable with sustainable partnerships for development. It seeks to move carefully in order to support both these objectives.

It was reported by community housing providers that management contracts for housing stock of greater than 5 years are not favoured by Treasury due to their impacts on state balance sheets. This was not able to be confirmed with Treasury as an issue. From a policy perspective, it was noted that issues associated with impacts on balance sheets can be overcome through careful timing, including the spacing of transfers over several years to reduce the impact of writing off assets in any single year. This was not described as a policy objection to transfers of title and/or long-term management contracts, but rather as a requirement that these be undertaken judiciously and in phases.

3.2 ISSUES FOR COMMUNITY HOUSING PROVIDERS

Interviews were conducted with community housing providers and peak bodies, as well as financial institutions that lend to community housing organisations. Perspectives on the benefits and risks or disadvantages associated with transfers of management contracts and property titles were explored.

Many issues were shared across jurisdictions; data and analysis is presented in combined tables, followed by individual points raised during interviews.

3.2.1 TRANSFER OF MANAGEMENT CONTRACTS

Transfer of management contract generally involves the community housing provider taking responsibility for managing the tenancy agreement and the ongoing repairs and maintenance of properties which continue to be owned by government.

The key perspective of community housing providers in all four jurisdictions was the need for these types of transfers to offer opportunities for change as well as simply shifting the responsibility for tenancy management. Many providers saw these contracts as first steps towards later acquisition of property titles. Without support for new practices, transfers of management contracts are simply changes to the name of the landlord which provide an opportunity to access additional income in the form of CRA.

Providers described key potential advantages and limitations associated with transfer of management contracts as in the table below.

Advantages	**Risks**
Increased scale of rental incomes	Increased burden of reporting to government
CRA entitlement increases potential landlord revenue by approximately 50% (over government landlord revenue)	Sovereign risk of changes to CRA arrangements
Government retains responsibility for structural maintenance – not clear in all jurisdictions (and NSW and new transfers in QLD expressly pass on responsibility for all levels of maintenance)	Substantial responsive and cyclical maintenance costs on poorly maintained and ageing stock; lack of clarity regarding structural and lifecycle maintenance, especially for short contracts where large cyclical costs can fall within a particular contract period
Greater potential to borrow against rental income – especially for longer contracts e.g. 10 years	Costs of insurance, rates and charges
Opportunities to demonstrate models, deliver improved outcomes, and build reputations	Costs of securing tenant agreement to transfer; Need for new staff and higher levels of training to support more complex tenancy needs

Specific observations from providers included:

- A key issue is the length of management contracts. Short leases (less than 3 years) do not provide opportunities for leverage because lenders require evidence of longer-term incomes (this is in addition to issues around major cyclical maintenance falling due during a short contract period described in the table above).
- Without capacity to engage in portfolio management, providers are dependent on government to ensure the long term maintenance of properties and the sustainability of their business models. They cannot actively engage in management of the condition of the properties to maximise values and plan for major works. Close communication and partnership is required to ensure that this type of arrangement does not result in the same demise of assets over time faced by government housing providers.
- Transfer of management contract without title can be seen as ‘using CRA to fund maintenance costs that states can’t afford’.
- It is possible for providers who manage contracts to partner with government in redevelopments involving temporary transfers of title. These models may make profits for providers, but if assets are ultimately transferred back to government, the incentives for participation are very limited.

3.2.2 TRANSFER OF PROPERTY TITLES

When governments transfer property titles to community housing providers in Australian jurisdictions they generally retain a caveat or director’s interest on the title. Amongst other requirements, the terms include:

- Properties cannot be sold or used for a purpose other than community housing without government consent
- Government is the priority creditor for any debt against the assets
- If a provider fails, government can step in to ensure transfer of assets to another provider.

In the case of title transfer, community housing providers saw the key issue as ensuring that they had sufficient freedom and flexibility to actively manage portfolios. The importance of a strong regulatory system to protect government investment and allow providers to make deals, trade and generate returns for expansion was noted as central to this.

In addition to the advantages and risks of contract management, providers' perspectives on transfer of property titles included the issues outlined below.

Advantages	Issues
Greater potential to borrow against security of properties	Credit risk associated with borrowing
More autonomy and control, creating opportunities for innovation and dynamism (if contracts and relationships sufficiently strong and flexible)	Delays and uncertainties in dealing with government – at the front end of projects; long timeframes and unrealistic expectations of developments
Improved financial strength of organisation, in terms of balance sheet position	Annual costs of insurance and valuation; Depreciation; Need to keep substantial cash reserves available for maintenance
Potential to manage to average numbers of properties over time and to make profits from disposals	Burden of reporting on assets to government e.g. Quarterly Vested Asset Title Reports in NSW
Ability to access NRAS incentives for redevelopment (with appropriate approvals if required)	Organisational risks associated with guaranteeing services to tenants while carrying out upgrades and maintenance
Better long term portfolio planning and management e.g. strategic aggregation and reconfiguration to support expansion	Need for staff with portfolio management and development experience

Specific observations from providers included:

- Governments tend to overvalue assets – and therefore overstate the value of security and title for borrowing. While governments value stock at market rates, banks consider them heavily impaired assets (see Section 4.2).
- Delays associated with working with governments, and with changes in governments, can have substantial impacts on development projects; conversely, unrealistic expectations from government about the timing of developments can endanger contracts.
- Title transfer to support asset growth is most effective when delivered at a scale which allows providers to adopt a genuine portfolio management approach; there is little potential for leverage against individual properties due to low values and obligations to tenants.
- While growth targets can be set by governments and negotiated with providers, it is unrealistic to impose specific levels of leverage; leverage levels are an output of the value of a portfolio and expected revenues, not an input.

- The model used in NSW ,for the transfer of Nation Building properties was cited as providing the best outcomes seen in the Australian jurisdictions, with realistic expectations and targets (though long delays). This view was held by a number of housing providers outside NSW; it is supported by the levels of transfers which have been successfully achieved in that state.

3.2.3 OTHER IMPLICATIONS AND IMPACTS OF TRANSFERS

Several community housing providers raised further issues indirectly related to the transfer of social housing assets which are relevant to future choices about policies and practices. These included:

- Risks and liabilities for governments associated with large changes to government housing staffing levels as a result of stock transfers; in some cases, these liabilities are extensive (e.g. potential staff redundancies) Political and ideological considerations regarding 'privatisation' of public assets
- Retention of government's ultimate accountability for tenancies and assets, and importance of strong regulation in mitigating this risk
- The importance of broader policy settings for the success of transfer policy; in particular, the crucial role of CRA and NRAS funding in supporting transfers.

3.3 CASE STUDIES

In practice, stock transfers can take a number of different forms, depending among other things on the policy orientation of the State or Territory government, the capacity of the community housing organisations involved and the locality and condition of the stock. This section provides some brief case studies to serve as examples of how stock transfer is being implemented.

Case study: Borrowing against title to meet growth targets (NSW)

A commitment was made to a CHP of over 1,000 transfers of title. So far the provider has received just over 570 (with the remainder expected to be transferred soon). Prior to the transfer the provider had not held debt (but had had no need for it). After the transfer, they raised $50m which was then invested in growth of the assets.

Securing finance was a slow process and required the lender to invest substantial time in understanding the business model of the community housing sector and its relationships with government. In particular, the role of government as primary creditor on property titles had to be clarified.

Once this was understood, the lender was happy to accept a second mortgage over the properties as security for a line of credit which could be used to develop new properties. The limit on the total that could be borrowed was set by cash flows, rather than title. Annual reviews of debt, incomes and assets are conducted, with additional security taken against newly developed properties if required to support the line of credit. There is no need for the lender to individually approve each proposed development project because the debt is secured against existing properties.

The provider has already undertaken substantial growth using this model, expects to continue to grow when further properties are received, and feels that targets for growth set by government are realistic. Limits on future growth will be those imposed by the bank lender: ongoing monitoring of ICR and LVR.

Refinancing of the debt will occur after three years. If refinancing cannot be secured, the provider will be forced to sell the newly developed properties in order to remain viable. These properties are currently mortgage free. The value of the transferred properties against which the debt was initially raised is not sufficient to repay the debt. The provider has an obligation to government to undertake leveraging and growth, and this situation could lead to breach of this agreement, and ultimately to deregistration.

Case study: Small scale growth through leveraging (VIC)

An urban Housing Association received titles for 200 properties around Melbourne that it had already managed for several years. This increased the asset base of the organisation, and the maintenance and replacement responsibilities, but did not impact on income streams.

While some debt had previously been taken against revenues from managing the properties, the title transfer allowed use of the properties as security for additional borrowing. Debt is taken in the form of commercial lending secured with a mortgage against the properties, and overall LVR is comfortable at 30% against the portfolio as a whole.

The Association undertakes full portfolio management, with the condition of properties regularly reviewed and sales and/or redevelopments undertaken, with government consent when required by director's interest on titles. Sales and recycling of capital allow access to NRAS incentives which have contributed significantly to growth in both assets and incomes.

The limit on borrowing is income, not assets – the provider has mortgage free properties that could be used if needed as security. Short management contracts (3-5 years) provide challenges with lenders, but the Association reports that the Victorian Government prefers not to transfer long-term contracts due to impacts on its balance sheet (due to effective disposition of the asset). It was noted that this was not an issue in another jurisdiction, where the Association also operates and 10-year contracts are standard.

Case study: High levels of leveraging (VIC)

In 2005-06, a regional Housing Association with strong commitment to growth received titles to 40 properties which they were already managing. The provider negotiated to leverage growth of 15% of the value of the assets, and delivered this without difficulty; government had initially required leverage at 25%.

The Victorian Government subsequently offered equity directly to the providers, with a 25% leverage expectation. This provider secured substantial funding of $30m and secured required levels of debt for development. The debt is held through a syndicated debt facility secured as a fixed and floating charge against the whole portfolio of assets. As developments are completed, they are added to the portfolio.

The provider now owns and manages over 1,000 properties (and manages a further 300). Debt levels are substantial and the organisation is highly leveraged with no further capacity to pursue growth opportunities. All surpluses go into servicing over $60m of debt, which is held at standard rates.

The upper limits on the amount that can be borrowed are determined by cash flow. Rental revenues from tenants are limited by the nature of the tenant group and surpluses must be directed to service existing debt. The provider does not have capacity to set aside funds for long term structural maintenance or replacement of stock, or flexibility to undertake good practice in portfolio management such as aggregation and reconfiguration.

4.0 THE IMPORTANCE OF TITLE TRANSFER

This section of the report addresses the three main research questions for the study:

- The impact of stock transfer, both management rights only and title, on the financial performance of community housing organisations
- The ability of community housing organisations to leverage further funds and development opportunities on transferred assets
- The impact on the credit rating and balance sheet of State and Territory governments of the title transfer of social housing assets to community housing organisations.

4.1 IMPACTS ON FINANCIAL PERFORMANCE OF COMMUNITY HOUSING PROVIDERS

For management contract transfers, the impacts on the financial performance of community housing providers are closely tied to the length of the contracts transferred, the scale of the transfers, the condition of the properties, and the arrangements for long-term and cyclical maintenance and renewal.

In the case of title transfers, there is much greater scope for variation in impacts, and for much more significant impacts on providers. There can be a fundamental tension between government perceptions of the value of assets transferred and their real value to providers (see below). The other principal factor impacting on the financial health of providers is the extent of government requirements regarding levels of leveraging and growth, development timeframes, and caveats on titles.

For both types of transfers:

- CRA is a crucial component of viability, and represents a sovereign risk.
- A risk-based regulatory system will support strong financial management by providers engaged in complex development activities and provide protection to all parties.

4.2 IMPACTS ON LEVERAGING AND DEVELOPMENT ABILITY

In the case of community housing providers, the two factors of relevance for leveraging are:

- Revenues, which are dependent on levels of rental income from properties with subsidised rents substantial operational costs
- Security against properties, both those transferred from public housing stock and those subsequently developed as part of growth strategies.

Through interviews with lenders the following conclusions can be drawn:

- Lenders demand evidence (and ongoing monitoring) of both revenues and assets in order to approve substantial borrowing.
- Value of assets – lenders consider them to be impaired and discount market values substantially because their use as social housing presents a reputational risk for financiers should they need to repossess properties in the event of default, so they tend to be considerably more conservative in setting loan-to-value ratios for social housing properties.

- Ownership of title – although caveats / director's interests do not in themselves have adverse impacts on the ability of community housing providers to secure funding.

The experience of providers to date is that while security is necessary, the limit on borrowings has historically been levels of ICR, not LVR (however in NSW, this is starting to shift). This is explored further in the modelling section which follows.

4.3 MODELLING: TITLE TRANSFER AND GROWTH POTENTIAL

Sphere has performed financial modelling to illustrate the relationship between housing providers having title to the properties they manage and growth potential through leveraging – in particular the minimum level of ownership required to maximise leverage. For the purpose of modelling the following assumptions have been made:

- The housing provider has 1,500 dwelling before leveraged stock growth
- Tenants of the 1,500 transferred dwellings are social housing tenants paying only 25% of household income in rent.
- On average, dwellings deliver a surplus of $2,500 per annum after maintenance and upgrade costs are taken into account (and the same level of surplus is applied to leveraged dwellings)[22].
- No equity is contributed.
- Average value of properties is $300,000 per dwelling for both existing and leveraged dwellings. This would mean that if the housing provider had title to all the dwellings under management then the value of the properties owned would be $450 million.
- Debt has an interest rate of 6.0% p.a. and is amortised over 20 years
- The loan to value ratio (LVR) is not to exceed 25% - this is consistent with the current requirements of lenders to the sector
- The interest cover ratio (ICR) is at least 1.5 times - this is consistent with the current requirements of lenders to the sector.

It should be noted that this is a conservative 'base case'. Most providers increase their leverage by including additional equity or supporting income streams through NRAS or mixed incomes. Similarly, other policy instruments could improve the ICR currently required. Finally, while the modelling shows the *minimum title transfer required* to maximise the leverage potential, there are other reasons related to portfolio management (and income stream risks) that would require higher levels of title.

Sphere has modelled how the growth potential of a housing provider with the above constraints changes as the level of assets ownership grows – up to $450 million which would mean 100% of the properties under management come with title transfer. The modelling estimates the minimum amount of title transfer required to maximise growth.

Figure 4 and Figure 5 show that growth potential increases with the value of assets owned by the provider up to around a third ($150 million) of the managed portfolio. After that, the ICR becomes

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[22] This is based on Sphere's previous work for NSW Shelter, see: http://www.shelternsw.org.au/publications/doc_download/157-leveraging-affordable-rental-housing-for-sustainability-and-growth. This surplus includes an assumption of $30 per week CRA income per tenant.

the limiting factor and, consequently, transferring more properties with title makes no difference to growth.

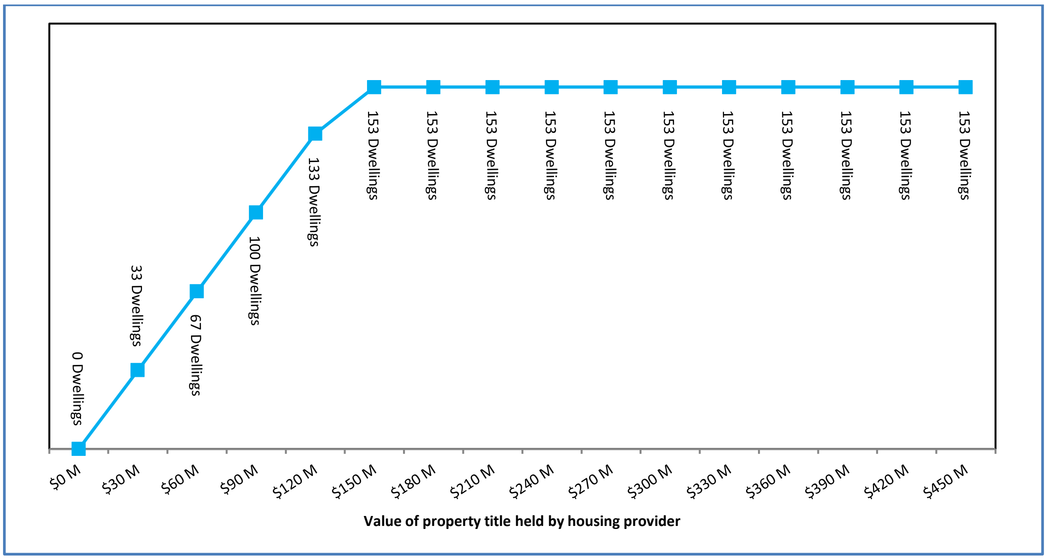

Figure 2: Growth potential as the value of title transferred changes

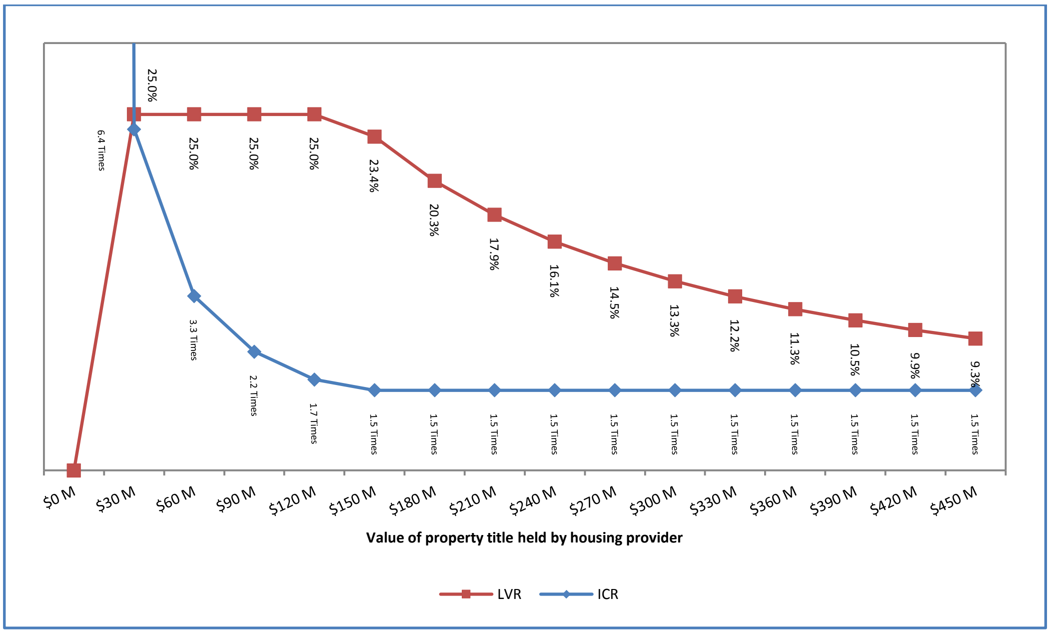

Figure 3: LVR and ICR as the value of title transferred changes

This means that for a provider with the above characteristic there is:

- A level of transfer of title to maximise growth potential – in this case around $150 million or one third of the properties under management.

- A maximum level of growth[23] which in the last instance is limited by the surpluses the housing portfolio can generate – in this case 153 dwellings (around 10% growth on the original 1,500 dwellings).

These metrics are clearly sensitive on debt terms – in particular interest rates and the minimum ICRs. To illustrate this point Figure 5 shows how these two metrics change with interest rates of 6% and 9%; and minimum ICRs of 2.00 times, 1.75 times and 1.50 times. The graph shows that the higher the ICR and the interest rate, the lower the benefit of title transfer in terms of growth potential.

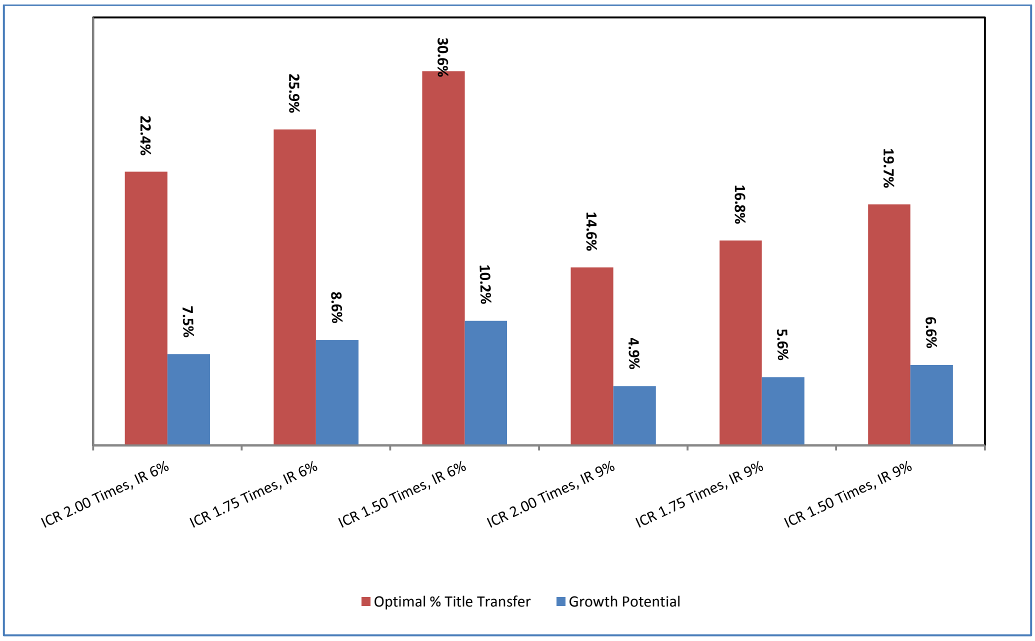

Figure 4: Optimal level of title transfer and growth potential

In summary, whilst transfer of title is essential to ignite growth, obtaining title for around **one third** of the properties managed by a housing provider would suffice to maximise growth potential which might be as high as **10%** on top of the original properties under management.

This minimum level of title transfer will clearly vary with:

- The maximum LVR. Housing providers and financiers who are comfortable with LVRs higher than 25% will increase their growth potential with higher levels of title transfer.
- The level of surpluses generated by the portfolio – the example modelled assumes dwellings with public housing rent rules. In settings where tenants pay higher rents (i.e. affordable housing where rents are charged up to 74.9% of market rent), the growth potential will be higher. Similarly, larger providers might be able to deliver higher surpluses through economies of scale.
- Financial investment incentives such as NRAS that can make the growth potential higher.

[23] Growth potential % is defined as the numbers of dwellings leveraged over the size of the original portfolio x 100.

4.4 MODELLING: THE IMPORTANCE OF CRA

In this section, analysis has also been performed with the same assumption as Section 4.3 but this time assuming that CRA is not available – (at an average loss of $30 per week/per dwelling resulting on an average lower surplus per dwelling of $940 pa after maintenance and upgrade costs are taken into account).

Figure 6 shows that growth potential grows with the value of assets owned by the provider up to around a fifth ($90 million) of the managed portfolio. After that, the ICR becomes the limiting factor and, consequently, transferring more properties with title makes no difference to growth.

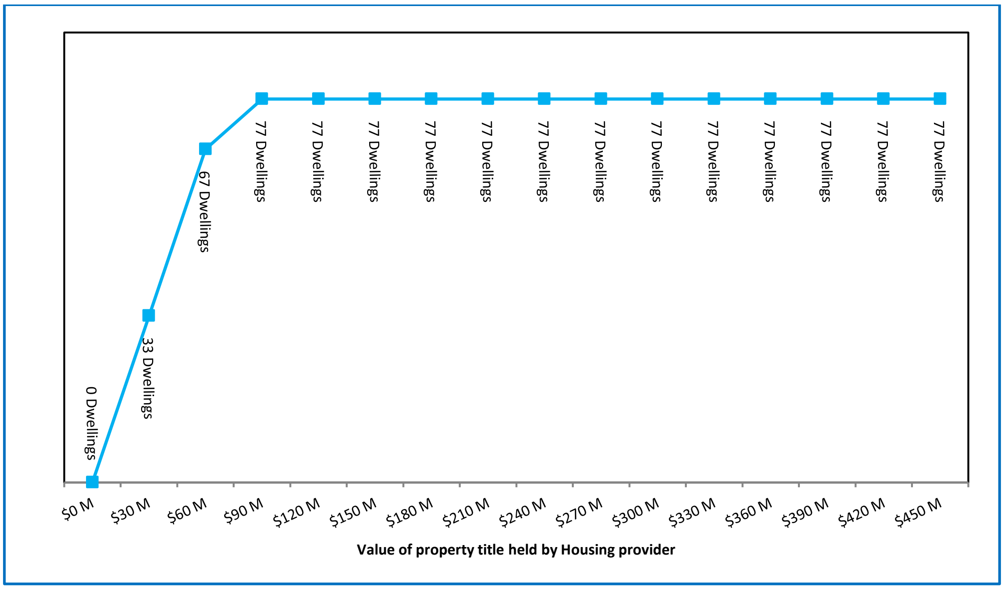

Figure 5: Growth potential as the value of title transferred changes – without CRA

This means that for a provider with the characteristics described in Section 4.3 but with tenants who do not receive CRA:

- The level of transfer of title to maximise growth has been reduced to $90 million or one fifth of the properties under management. The non-availability of CRA has consequently limited the effectiveness of title transfer as a mechanism for growth from one third of the properties under management to one fifth of the properties under management.
- The maximum level of growth has been reduced to 77 dwellings (around 5% growth on the original 1,500 dwellings). The non-availability of CRA has consequently halved the growth potential.

The modelling clearly demonstrated that:

- CRA is an essential component to maximise the growth potential of housing providers.
- A change in Commonwealth policy on the eligibility of community housing tenants for CRA is a significant risk for both housing providers and financiers. In the case where a provider has borrowed against cash flows which include CRA, a change in policy would mean that the housing provider no longer can afford loan repayments and that most likely up to one half of the leveraged dwellings would have to be sold to keep the organisation solvent.

4.5 IMPACTS ON THE CREDIT RATINGS AND BALANCE SHEETS OF STATE AND TERRITORY GOVERNMENTS

4.5.1 IMPACTS ON GOVERNMENT BALANCE SHEETS

The National Shelter NAHA consultations identified concerns about impacts on government balance sheets as one reason given to providers for 'reluctance' to transfer property titles.[24] National Shelter note that "there is some question about whether this is a real or perceived problem, particularly when there was no research to support the claim."

This project has found that while there is clearly a 'budget loss' to State / Territory balance sheets associated with the transfer of either titles or long-term contracts, the level of impact of this depends on the particular practices of the jurisdiction. Factors which influence how the impacts are described include:

- Accounting practices: inclusion of social housing stock as 'financial assets'
- Valuation practices: Governments which value social housing assets at market value perceive greater losses
- Phasing: Spreading 'losses' across several years to reduce single-year impacts
- Staffing liabilities: inclusion of costs of redundancies associated with transfers.

These factors influence how transfers are reported on balance sheets and therefore the scale of the 'loss' that is reported in the budget. While it was not possible to secure interviews with Treasury representatives in all jurisdictions, government and community housing representatives reported that attitudes towards these 'losses' vary between Australian jurisdictions, with some Treasuries finding the issue not at all significant and others considering it a major barrier to transfers.

4.5.2 IMPACTS ON CREDIT RATINGS

Both throughout National Shelter's NAHA consultations and during research for this study, the issue of potential negative impacts on State / Territory credit ratings as a result of transfers of stock was frequently raised. It was suggested that the removal of substantial assets from the balance sheet could adversely impact on assessment by third party agencies.

An interview with a ratings agency confirmed, however, that this fear was unfounded.[25] The agency emphasised that their ratings were provided on the basis of a State /Territory's ability to repay its debt, not on the basis of the amount of assets that it holds. Only financial assets are considered as part of the balance sheet, and the agency considered that "the impact on credit ratings [of transfers] would be minimal" because there is "minimal contingent liability, given the structures that are in place".

The agency does not consider transfers to have a high risk of impacting adversely on State/Territory budgets, because governments are protected from adverse impacts by the extensive regulation of the community housing sector and by the retaining of interest on the titles which allows them to reallocate properties in the event of serious problems with a provider.

[24] See National Shelter NAHA Consultations report, p34.

[25] There is no reason to believe that other ratings agencies would take significantly different positions on these issues.

Specific factors contributing to the ratings agency's assessment included:

- The fact that there were no debt obligations on the transferred assets at the time of transfer
- The caveats / director's interests / tripartite agreements which give governments the ability to control the long-term use of the assets, even after transfer of title
- The existence of a comprehensive regulatory framework, including oversight of the financial health of community housing providers
- The limited nature of the government's role in the event of the failure of a provider to oversight of the transfer of assets to another provider
- The small scale of assets under consideration, in comparison to the total of State / Territory balance sheets.

5.0 CONCLUSIONS

This section of the report draws out the conclusions from the research and analysis undertaken for this study. It contains an overview of the findings from the work undertaken to address the key research questions of the study, and a section containing recommendations for consideration for policy making and areas requiring further research.

5.1 FINDINGS FROM THE CURRENT STUDY

In terms of the financial impacts of stock transfers, the current study has found both variations and consistencies between the experiences of the Australian jurisdictions considered. Key findings overall are:

- The sustainability of stock transfers for renewal or growth of community housing provision is heavily dependent on CRA.
- Title transfers do support leverage but increasing access to title does not necessarily increase growth – however, modelling a conservative 'base case' suggests that community housing providers need title to at least about one third of their portfolio in order to maximise growth potential leverage. After this point, Interest Cover Ratios become the limiting factor on borrowing rather than Loan to Value Ratios.
- However, ownership of title has other financial implications, both in terms of risk management and portfolio management
- NRAS incentives provide additional capacity to support growth (but long-term effects after the end of the incentive period need to be considered).
- While governments are apprehensive about the impacts of transfers on their balance sheets, the ratings agency did not consider this to be a relevant issue due to the special nature of housing assets and the substantial levels of protection in place to protect governments from risks.
- Political priorities, ideologies, and past experiences impact greatly on the approaches of different governments to transfer policy and practice. Perceived political or reputational risk can impact policy settings, even when real risks are minimal.
- It has taken time to develop trust and understanding between governments, providers, and lenders. There is increasing experience and understanding of the models which is facilitating better relationships and faster policy implementation, although changes of government can result in additional delays.
- The development of a rigorous national regulatory framework supports improved confidence among government and lenders and is expected to increase potential for growth through leverage.
- For transfers of management contracts only, the length of the contract is crucial. Short contracts do not support borrowing for growth or long-term maintenance of stock. There is danger that short contracts simply defer stock demise as they do not provide community housing providers with a mechanism to renew the portfolio or raise extra funding.
- For transfers of either title or management to be effective in supporting portfolio management and long-term sustainability, community housing providers must have real control of stock; this can be achieved through flexible partnership with government or direct ownership.
- Current government valuation and accounting practices can create artificial barriers to transfers.
- Governments can be unrealistic in their initial expectations regarding the scale and timing of growth, but over time more realistic expectations are identified.

5.2 POLICY RECOMMENDATIONS AND AREAS FOR FURTHER RESEARCH

Substantial further findings and recommendations relevant to transfer policy have been made in the recent AHURI report *Public housing stock transfers in Australia: past, present and prospective*. However, the current study has identified some areas where additional policy direction and / or further research are required:

- **Title transfer** – the study has found that there exist no impediments that stand up to scrutiny to transfer of title from State and Territory Governments to community housing providers. In fact, ensuring that housing providers possess title of around one third of their portfolios will maximise growth potential. Given the high level of need for social housing in Australia - as reflected by long waiting lists in all jurisdictions – it would be important for the Commonwealth to play an active role in providing incentives to State and Territory Government to undertake limited title transfer programs (perhaps modelled on the NSW approach for the transfer of nation building properties).

  Setting a target of 10%-15% of social housing stock for title transfers would improve growth returns for the CRA investment in the community housing sector. The Commonwealth has been generous in allowing eligibility for CRA for community housing tenants. This target could either be a condition for the continuation of this policy or, alternatively, the target could be introduced as an element in future national affordable housing agreements.

- **Management contract transfers** – there needs to be recognition from governments that transfer of contract management alone does not necessarily provide sufficient opportunity to support renewal or growth. Factors that influence the extent to which providers benefit from these transfers include:

  - Contract length: short contracts do not provide the certainty of revenues which lenders require in order to provide substantial finance
  - Maintenance arrangements: for short-term contracts, major cyclical maintenance and structural maintenance / renewal needs to remain the responsibility of government; only long-term contracts, together with a partnership approach to portfolio management and redevelopment opportunities, support providers in taking responsibility for major ongoing maintenance

- **Valuation of assets** – governments need to bring their valuation of housing assets into line with that of lenders (and community housing providers). Government practice of recording values of properties at market prices creates unrealistic expectations about their leveraging potential - and increases the potential for adverse impacts of transfers on the balance sheets of States and Territories (see below).

  <u>FURTHER RESEARCH</u>: Pawson has indicated that the UK model where public housing is valued as a business, with maintenance costs factored in against asset values and transfer price reflecting total value and projected income stream, requires further investigation for Australia. The current study supports this.[26]

[26] Hal Pawson 2013, Ibid.

- **Accounting practices** – despite the lack of concern of the ratings agency, State / Territory government accounting practices currently create 'book losses' associated with the transfer of housing stock which impact the balance sheet and reportedly cause concern in some jurisdictions. There is a need to mitigate these perceived losses through changes to accounting practices, where they are providing a barrier to stock transfers.

  FURTHER RESEARCH: Pawson has also identified options including State / Territory government adoption of accounting conventions where profit/loss is published net of public housing, or the Commonwealth Government co-operates to mitigate book losses by drawing on revaluation reserves. The current study supports further exploration of options such as these.[27]

- **CRA** – there needs to be explicit understanding of the importance of CRA in supporting current arrangements and awareness of the risks associated with any change in policy in this area. In many cases, community housing providers rely on CRA to increase their rental revenues by 1.5 times the levels of rental incomes available to public housing for the same tenants.

  FURTHER RESEARCH: The question of whether CRA is the most effective way to provide Commonwealth support for the community housing sector needs investigation, alongside exploration of alternative models and the impacts of any changes to the current system.

- **NRAS** – consideration needs to be given to the long-term effects of using NRAS incentives to support growth in the community housing sector. At the end of the 10-year incentive period, providers will lose guaranteed income streams and potentially be compelled to sell properties or change their usage away from community housing.

  FURTHER RESEARCH: The longer-term effects of NRAS on the community housing sector need further exploration.

- **Impact on tenants** – the impact of title transfer on tenants is outside of the scope of this study. However, this is clearly an issue of great importance.

  FURTHER RESEARCH: The effect of title transfer on tenants.

[27] Hal Pawson 2013, Ibid.