The Sydney Morning Herald

4 September 2018

OPINION

Tax breaks can solve the housing crisis

If governments won't provide enough public housing, they should subsidise more community housing.

Australia stands on the precipice of a social crisis. Industry Super Australia estimates a national affordable-housing shortage (mostly sub-market rentals and emergency housing) of about 350,000. Two-thirds or more of that shortage is in NSW and Victoria.

The main objective of housing policy was once to get families into decent homes. Not any more, apparently.

The affordable-housing shortage is testimony to 30 years of inadequate planning and short-term thinking. ERIN JONASSON

A rising tide of housing distress has causal effects like homelessness, mental illness, family stress, domestic violence, wage stagnation and welfare dependency.

The additional economic costs of housing distress are borne by all levels of government. They will continue to rise from now on. This is a lose-lose scenario for this and future generations.

Housing stress is a mainstream economic problem that wastes human resources and destroys productivity. Yet none of these social and productivity imposts are being measured; a worthy challenge for the next *Intergenerational Report*, due by 2020.

The social dividend from fixing this problem far exceeds any other mainstream economic or fiscal reform because it deals with the fabric or "infrastructure" of social cohesion.

Listening to radio ads, one could be forgiven for thinking the goal of Australian government housing subsidies is to give mum-and-dad investors the ability to buy multiple existing properties using debt via a self-managed super fund. As a result, some own multiple properties and pass wealth to the next generation in their family. Meanwhile, others face periods of homelessness and impoverishment, which is also passed to subsequent generations who can't access education or jobs due to unstable housing, let alone home ownership.

The affordable-housing shortage is testimony to 30 years or more of inadequate regional and national planning, coupled with short-term thinking. Successive governments have directed too many resources at spurring demand for existing property rather than building new homes for the most needy.

Australian governments must work together urgently to address this before the trickle becomes a flood and our nation experiences a homelessness epidemic.

What is affordable housing? The common definition of housing stress is spending more than 30 per cent gross of one's pre-tax income on housing on an ongoing basis. Australian families face a daily dilemma: choosing between paying rent, or paying for childcare, car repairs, food or medical bills. Depending on the city, 40 to 60 per cent of urban households are locked out of rental markets.

Fixing the social-housing shortfall

First, we must identify where the need is greatest by local government area, remembering that some regions are cheaper because they are remote, rundown or sub-standard for some other reason. This is a job for an office of national housing, operating within a Productivity Commission more inclined to evidence-based analysis. It would be charged with generating and releasing these analytics each year.

Second, all levels of government must pool existing housing subsidies and reprioritise them for the sole purpose of building and/or operating housing for the disadvantaged (the federal government will need to use carrots and sticks here).

Third, all levels of government must identify underused public and private landholdings. The federal government must provide effective incentives for recycling assets, and for charities, churches and community groups to give up excess landholdings on long-term leases.

Governments must use housing subsidies for the sole purpose of providing housing for the disadvantaged.

Finally, governments must lever the balance sheets of long-term investors, such as overseas pension funds, Australian superannuation funds, insurance companies and family offices, to invest in affordable housing.

Right now, most long-term portfolio investors have little interest in residential property in Sydney and Melbourne due to current yields of about 3 per cent (and falling prices). These returns are too low for funds that benchmark inflation plus 4 to 6 per cent. Sub-market rental units return even less and tenants are generally even more risky.

However, more innovative industry superannuation funds are developing direct-investment proposals in affordable housing, especially by targeting key workers and identifying the most reliable renters in the sub-market distribution. But these projects are likely to be a drop in the bucket compared to the scale of the overall problem. Regrettably, so are government policy experiments in inclusionary zoning, town-planning processes, bond aggregators and so on. These do not address the heart of the affordable-housing crisis.

Brick-by-brick, building-by-building, the affordable-housing sector is being denied access to the scale of equity capital needed to address housing shortages. Sure, banks will lend them debt finance for a price, however that must be repaid on commercial terms. Sustainable projects employ 70 per cent or more equity finance. Who will provide that capital?

Tax credits for affordable housing

The missing link in this policy chain is the provision of an efficient and effective mechanism to deliver equity capital to affordable-housing providers. This would allow institutional investors to effectively write down or write off every dollar they ever invest in a sector, with no adverse impact on their rate-of-return benchmarks.

The missing link is a policy such as affordable-housing tax credits.

Assuming that the Productivity Commission identified the location of a material housing shortage, the federal government could authorise a statutory corporation to tender for the construction of these places.

The successful developer/operator would structure the project financing based on receipt of tradeable tax credits (the funding source for the equity capital), which they would sell to long-term portfolio investors. The investors who buy tax credits could then write off their tax liabilities immediately. Federal or state revenue/housing authorities would require investors to ensure projects are delivered as promised in terms of affordability, quality and quantity. Investors entrust the management and maintenance of the housing developments to qualified community-housing entities.

Over time, tax credits should trade at close to face value. The credit-efficiency goal would be to ensure that 90 per cent of tax credits go to direct-housing investment.

By embedding an affordable-housing tax credit into the tax code (just like negative gearing is), the program will become a self-perpetuating funding stream into affordable housing that is regulated via a statutory body to eliminate fraud and waste. It should not be subject to the vagaries of political change through the annual budget process. This program is likely to attract significant private-sector equity capital and build permanently affordable, privately owned and managed affordable-housing developments as community resources.

If an Australian scheme generated $1 billion in tax credits and those credits were invested at 90 per cent efficiency at $400,000 per two-bedroom unit or townhouse (to target 40 to 60 per cent of area median income households), it would produce 2300 units a year; nearly 23,00 units in a decade. Yet $1 billion is a small fraction of the $20 billion spent subsidising superannuation, with little affordable-housing benefit generated.

Has a viable tax-credit scheme operated anywhere else in the world? The United States' low-income housing tax credit program generated three million units from 1987 to 2015 in 45,900 projects. It now creates about 110,000 units a year with a total worth of about $US8 billion a year. Operators achieved a 97.8 per cent occupancy rate in 2016 and a 0.7 per cent cumulative foreclosure rate. The scheme has a long, successful pedigree.

The now defunct national rental-assistance scheme provided a good foundation for the proposed tax-credit scheme. But a new scheme must incentivise and guide state-based effort and call for expressions of interest for very large tranches of support to attract institutions. The rental-assistance scheme developed a good head of steam and should be built on.

Is this proposal an example of the rent-seeking by the super sector? Not at all. Maybe Australian super funds will access these tax credits (perhaps to replace some taxpayers' loss of imputation credits after the next election). However, certain portfolio investors and non-financial corporations that face higher effective tax rates will find housing tax credits attractive.

Can we avert a looming housing crisis? Put simply, we need to build more assisted houses in the right places. We need to remove existing market distortions that muddy incentives for new building. We need government, via long-term institutional investors, to allocate big pools of capital to assisted housing.

In the final analysis, governments must realise that if they are unprepared to deliver affordable housing directly via public balance sheets (i.e. public housing), they must provide equivalent subsidy to private balance sheets, probably via not-for-profit community-housing providers.

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