

Risk Management in Community Housing

Managing the risks posed by growth in the provision of affordable housing

National Community Housing Forum

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Executive Summary

Recent research has identified a transition currently taking place in the social housing sector in Australia. Traditional models of social housing supply, encompassing large public housing agencies and small niche market community housing organisations, are making way for a more diversified system of affordable housing provision including larger scale non-government housing development vehicles engaging in partnerships with the public and private sectors. This report examines the risk management implications of the transition for these “Growth Housing Providers” as their business grows in scale, diversity and complexity.

The report begins with a survey of the evolution of the community housing sector in Australia (Chapter 2). Five phases in the development of the sector have been identified culminating in one which commenced around 2003 and which is characterised by the emergence of new affordable housing models involving private finance which require non-government ownership and management vehicles with the capacity to raise private debt and undertake project development, long term asset management and facilities management.

The report notes that the community housing sector has continuously adapted to changes in public policy throughout previous phases of development and, since the early 1990s, has developed long term strategic directions to grow the sector and make a more substantial contribution to the alleviation of housing need. This has resulted in gradual consolidation of the sector and the emergence of a small number of larger scale organisations alongside a few state government initiated affordable housing agencies. These organisations have accumulated significant intellectual property and market experience which places them in a good position to take up the challenge of the emerging affordable housing models.

Chapter 3 turns its attention to changes in the role of non-government housing providers in the Netherlands and the United Kingdom – two countries with large and highly developed social housing systems. In both cases governments are increasingly looking to the non-government sector as the major instrument of new affordable housing supply. The decision to channel significant growth funds through the non-government sector however, requires a corresponding investment in a risk management framework designed to provide high levels of confidence to both the public and private sector in their financial investment in the sector. In the Netherlands the emphasis is on a tiered system of guarantees whereas in the UK emphasis is placed on the role of the regulatory authority and its powers of intervention. In both cases however, the critical factor is the recognition that risk management is a systems issue, requiring investment in infrastructure and capacity building.

A review of contemporary affordable housing case studies (Chapter 4) leads to the identification of the essential characteristics of Growth Housing Providers if they are to take up “market opportunities” for affordable housing.

- Current initiatives by community housing organisations in arranging debt finance from banks indicates that Growth Housing Providers can be expected to take up a broader range of activities such as property development and asset management. They also highlight the important role to be played by state government agencies in supporting their initiatives – such as land procurement and the provision of capital subsidies secured through arrangements that do not preclude bank finance.
- Recent initiatives to facilitate the growth of affordable housing by state governments also highlight the requirement for Growth Housing Providers to demonstrate the capacity for more diverse and complex professional skills in management and commercial experience at Board level. They also indicate the importance of greater continuity of business and effective regulatory oversight – providing assurance to government and private investors alike.
- Neighbourhood renewal programs in large public housing estates provide another opportunity for Growth Housing Providers. The driving factor in these initiatives however, is in the capacity of non-government organisations to bring a sophisticated community development approach to the housing management task – one which is based on a place management approach and is committed to the implementation of local economic development initiatives.
- There are numerous opportunities for Growth Housing Providers to participate in the development of affordable housing within large scale development projects around the country. However, they require the provider to have the capacity to deal with much larger projects (50 plus units), developed over a much longer time frame (5-10 years), involving multiple financial contributors and corresponding complex legal arrangements, and accepting significant development and ownership risks. These projects also require involvement in a broader range of functions and the provision of a more diverse range of products.
- The opportunities beginning to emerge as a result of the private investment industry seeking to diversify their portfolio to include the residential property market highlight three important factors – the risk management capabilities of Growth Housing Providers will be a paramount consideration when assessing any loan application. The establishment of a formal system of accreditation of Growth Housing Providers, and the subsequent monitoring of their performance, and the implementation of government regulatory powers, which include the right to intervene in the case of failure to perform, are important contributions to the development of a comprehensive risk management framework.

Chapter 4 concludes that risk management is a systems issue involving all the interconnecting components or players which are participating in the development of an affordable housing strategy. The system will encompass those responsible for policy, finance, development, ownership, management and regulation of affordable housing. A systematic approach to risk management will be the most strategic and cost effective way to implement an affordable housing growth strategy. However, the quantum of growth

and the rate of implementation will be key issues determining the direction of the strategy. If the scale of growth is small and the capacity of the community sector limited the most cost effective approach for government may be the establishment of a special purpose non-government vehicle to develop and own affordable housing. On the other hand, if government is committed to significant growth over a longer time scale and the community housing sector is further advanced then it could be more cost effective to invest in a regulatory framework and identify existing community housing providers with the capacity to develop their business into development and ownership of affordable housing.

Chapter 5 moves from the present to the future. It assumes governments in Australia have made a commitment to significantly grow affordable housing and presents a vision for an affordable housing system which will nurture that growth. The vision is built on the foundations laid by the community housing sector and state government initiatives and informed by both the overseas experience and local market opportunities reviewed in earlier Chapters. The vision assumes a small number of Growth Housing Providers, differentiated from the traditional community housing provider in Australia by role, scale and complexity of business, will emerge to provide the new affordable housing model. Six key characteristics of the future affordable housing system are identified.

- A nationally consistent affordable housing policy framework and a collaborative approach to the development of affordable housing infrastructure.
- The development of an integrated affordable housing system within various state jurisdictions encompassing land supply, subsidies and regulation.
- A uniform understanding of the culture and capabilities of Growth Housing Providers.
- The recognition of community development as a way of doing business and the allocation of resources to community building.
- An acceptance of diverse functions and structures for Growth Housing Providers reflecting the nature and scale of the state.
- The provision of diverse housing assistance products for lower income households and the flexibility to develop products suitable to local markets.

Having established that risk management is a systems issue the report then turns its attention to a framework for internal risk management by Growth Housing Providers (Chapter 6). By drawing attention to the Australian/New Zealand Standard for Risk Management the report firstly recognises the fact that a Growth Housing Provider is essentially a social enterprise requiring a commercial framework and comprehensive approach to risk management.

The report then analyses the functions a Growth Housing Provider may be responsible for and, based on this analysis presents a generic risk management framework. The framework focuses on the core functions of property procurement, housing development, asset management, property management, tenancy management and community building.

The framework identifies that one of the most important risk management strategies for a Growth Housing Provider is the employment of people with the requisite skills, competence and experience to manage each function. Starting with this assumption a calculation is undertaken to identify the minimum scale of a Growth Housing Provider to cost effectively manage risk. We propose that 12.5 EFT staff are required, at a cost of approximately \$1.25M per annum, as the minimum level for a Growth Housing Provider undertaking all six core functions. Employing industry benchmarks for the unit cost of these functions we come to the conclusion that the minimum size of a Growth Housing Provider that is capable of comprehensive risk management and operate cost effectively is one with a portfolio under management of 500 dwellings and which is developing 25 additional dwellings each year.

The report concludes (Chapter 7) with a summary of the implications of the findings for both the community housing sector and both state and commonwealth governments.

If existing community housing organisations are to make the successful transition to Growth Housing Provider they will have to develop and sustain a culture of risk management – the scale and complexity of their business will demand a comprehensive and continuous process of identifying and assessing the risks they are exposed to and designing and implementing strategies to mitigate those risks. Failure to do so will place their organisations in jeopardy, threaten the homes of their tenants and place scarce public resources at risk. The capacity to achieve such a culture however is dependent on scale and there are limits to growth. This implies a degree of “stratification” of the community housing sector. As in all other countries where there is a strong commitment to growth in affordable housing through the non-government sector, there will be a small number of very large Growth Housing Providers and a large number of small community housing managers.

The major implication for state governments is the need to develop an Affordable Housing Strategy and transparent industry infrastructure. Together, these will provide greater certainty and improved capacity for Growth Housing Providers thus directly reducing their risk exposure. They also provide a framework by which the private sector can understand the nature of their involvement in affordable housing, increasing their confidence and reducing the risk premium on the cost of their services.

At the commonwealth level the implications are twofold. First, clarity and consistency with respect to tax and subsidy arrangements for affordable housing is an essential ingredient for greater involvement of the private sector and will make a substantial contribution to risk management. Second, the commonwealth can improve both the effectiveness and efficiency of state based affordable housing systems if it provides

leadership in the development of a nationally consistent approach to key elements such as land procurement, capital subsidy arrangements and regulatory frameworks.