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Parliamentary Budget Officer

Senator Christine Milne Leader of the Australian Greens Parliament House CANBERRA ACT 2600

Dear Senator Milne

Please find attached a response to your costing request, *Safe as Houses* (letter of 14 August 2013).

The response to this request will be released on the PBO website (www.aph.gov.au/pbo).

If you have any queries about this costing, please do not hesitate to contact Colin Brown on (02) 6277 9530.

Yours sincerely

Phil Bowen

22 August 2013



# **COSTING – ELECTION CARETAKER PERIOD**

Name of proposal to be costed:	Safe as Houses			
Summary of proposal:	The proposal would raise finance for non-profit housing organisations to construct a maximum of 7,200 new homes a year. The required funds will be raised through three kinds of bonds:			
	• 10 per cent from 'zero interest social housing growth bonds' issued to and held by the Government			
	• 20 per cent from 'tax smart housing supply bonds', which are long-term fixed interest bonds offering tax-free interest issued to retail investors, and			
	• 70 per cent from 'AAA housing supply bonds' guaranteed by the Government and issued to wholesale investors.			
	An independent financial intermediary, the Australian Affordable Housing Finance Corporation (AAHFC), would have responsibility for issuing the bonds and loans as part of the scheme.			
	The proposal will have effect from 1 July 2014.			
Person/party requesting costing:	Senator Christine Milne, Australian Greens			
Date costing request received:	14 August 2013			
Date costing completed:	22 August 2013			
Date of public release of policy:	27 July 2013			
Additional information requested (including date):	On 16 August 2013, additional information was sought from the applicant on whether the funding for the AAHFC is capped. On 22 August 2013, additional information was sought on the intended recipient of the finance provided by the zero interest social housing growth bonds.			
Additional information received (including date):	On 17 August 2013, Director of Policy, Office of Senator Christine Milne advised that the funding for the AAHFC is capped. On 22 August 2013, Director of Policy, Office of Senator Christine Milne advised that it was intended that the zero interest finance would be provided to non-profit housing organisations.			
Agencies from which information was obtained:	Not applicable			

## **Costing overview**

This proposal is expected to decrease the underlying cash balance by \$59 million and decrease the fiscal balance by \$330 million over the 2013-14 Budget forward estimates period. The impact on the underlying cash balance reflects an increase in payments of \$30 million and a decrease in receipts of \$29 million over this period. The impact on the fiscal balance reflects an increase in expenses of \$300 million and a decrease in revenue of \$30 million over this period.

This proposal will have an ongoing impact that extends beyond the forward estimates period. The decrease to revenue in the forward estimates period continues to grow beyond the forward estimates by an additional \$10 million a year on the previous year's impact due to the tax concessions that continue to apply to the tax smart housing supply bonds issued in previous years.

The proposal would reduce the headline cash balance by \$1.3 billion in total over the 2013-14 Budget forward estimates period. The reduction in the headline cash balance reflects the \$204 million worth of zero interest social housing growth bonds acquired by the Government each year.

The underlying cash balance impact of this proposal differs from the fiscal balance impact because of the loan discount component of the concessional (zero interest) social housing growth bonds, which is an accrual expense but does not impact on the underlying cash balance.

The departmental expenses of the AAHFC of \$10 million a year are capped as specified by the requestor.

A detailed breakdown of the components of the costing's financial impact is included at Attachment A.

The costing is considered to be of medium reliability because the housing supply bonds are costed using data mainly from sources other than actual tax or expenditure data.

The impact on the underlying cash balance is \$115 million lower over the forward estimates period than those presented in the costing request. The impact on a fiscal balance basis is \$155 million higher over the forward estimates period than those presented in the costing request. These differences arise because of a revision in the costing methodology used by the PBO.

Table 1: Financial implications (outturn prices)<sup>(a)</sup>

Impact on	2013-14	2014-15	2015-16	2016-17
Underlying cash balance (\$m)	-	-10	-20	-30
Fiscal balance (\$m)	-	-100	-110	-120
Headline cash balance (\$m)	-	-214	-428	-642

<sup>(</sup>a) A negative number for the fiscal balance indicates a decrease to the budget bottom line in accrual terms. A negative number for the underlying cash balance indicates a decrease to the budget bottom line in cash terms. Amounts may not sum due to rounding.

## **Key assumptions**

The PBO has made the following assumptions regarding the raising of funds through three kinds of bonds:

- A total of \$2.04 billion of housing supply bonds would be required to finance the construction of 7,200 homes per annum. This is based on a third of the homes being built from prefabricated material, at \$150,000 each and two thirds being standard housing, at \$350,000 each.
- The AAHFC is assumed to be part of the general government sector.
- The discount rate used to calculate the loan discount for the zero interest social housing growth bonds is 6 per cent. This is an estimate of the market rate for loans to housing associations and is 100 basis points above the rates charged to large businesses as reported in Lawson et al. (2012).
  - The loan discount of the zero interest bonds is based on a maturity of 10 years.
- For the tax smart housing supply bonds, investors in these bonds are assumed to have an average marginal tax rate of 40 per cent. These bonds are assumed to earn 6 per cent per annum on a pre-tax basis, based on the assumptions in Lawson et al. (2012).
- The interest rate on the AAA housing supply bonds is assumed to be equal to the government long term bond rate of 3.75 per cent (RBA, 2013).
- It is assumed that the AAHFC does not charge a margin on the finance provided to community housing organisations.
- The costing assumes that funds are raised by the AAHFC are on-lent during the same periods that the funds are raised.

## Methodology

The costing sums the revenue and expenditure impacts associated with each of the initiatives under the proposal.

For the zero interest social housing growth bonds, the expense cost is calculated as the fair value of the interest forgone in providing the bond at a zero interest rate (or the 'loan discount'). This loan discount is calculated as the present value of the forgone interest and is recognised in the fiscal balance at the time of the loan.

In relation to the relation to the AAA housing supply bonds, expenses and revenue are calculated on the basis of the AAHFC issuing bonds and on-lending to non-profit housing organisations. The provision of a government guarantee is a contingent liability that does not impact on the underlying cash or fiscal balances.

For the tax smart housing supply bonds, the cost is the revenue forgone due to the tax exemption in the hands of the investor. The timing of each year's tax revenue implications will occur when income tax returns are lodged, that is, in the next financial year.

The departmental expenses of the AAHFC are capped.

#### **Data sources**

• Estimates are mostly based on the information and assumptions provided in Australian Greens, 'Safe as houses' introducing housing supply bonds, released on 27 July 2013.

- Assumptions for the housing supply bonds were based on those contained in Lawson, J. et al. (2012) *Housing Supply Bonds—a suitable instrument to channel investment towards affordable housing in Australia?* AHURI Final Report No. 188. Melbourne: Australian Housing and Urban Research Institute.
- Long term bond rate based on 10 year Australian Government bond rate in Reserve Bank of Australia (2013) 'Statistical Tables: Capital Market Yields Government Bonds Monthly', August 2013.

## ATTACHMENT A: COMPONENTS OF COSTING

Table A1: Breakdown of underlying cash balance impacts (\$m)<sup>(a)</sup>

Component	Cost type	2013-14	2014-15	2015-16	2016-17
Zero interest social housing bonds	Payments	1	1	1	-
	Receipts	1	1	1	-
Tax smart housing supply bonds	Payments	•	-12	-37	-61
	Receipts	1	12	27	41
AAA housing supply bond	Payments	1	-27	-80	-134
	Receipts	•	27	80	134
Departmental	Payments	1	-10	-10	-10
	Receipts	1	-	-	-
Total		-	-10	-20	-30

Table A2: Breakdown of fiscal balance impacts (\$m)<sup>(a)</sup>

Component	Cost type	2013-14	2014-15	2015-16	2016-17
Zero interest social housing bonds	Expense	1	-90	-90	-90
	Revenue	1	1	1	-
Tax smart housing supply bonds	Expense	•	-12	-37	-61
	Revenue	-	12	27	41
AAA housing supply bond	Expense	-	-27	-80	-134
	Revenue	-	27	80	134
Departmental	Expense	-	-10	-10	-10
	Revenue	-	-	-	-
Total		-	-100	-110	-120

<sup>(</sup>a) A positive number for the fiscal balance indicates a net increase in revenue in cash terms. A negative number for the underlying cash balance indicates a net increase in expenses or net capital investment in cash terms.

Note: Amounts may not sum due to rounding. Rounding is to the nearest million.

Table A3: Breakdown of headline cash balance impact  $(\$m)^{(b)}$ 

Component	Cost type	2013-14	2014-15	2015-16	2016-17
Zero interest social housing bonds	Payments	-	-204	-408	-612
	Receipts	-	-	-	-
Tax smart housing supply bonds	Payments	-	-12	-37	-61
	Receipts	-	12	27	41
AAA housing supply bond	Payments	-	-27	-80	-134
	Receipts	•	27	80	134
Departmental	Payments	-	-10	-10	-10
	Receipts	-	-	-	-
Total		-	-214	-428	-642

<sup>(</sup>b) A positive number for the headline cash balance indicates a net increase in receipts. A negative number for the headline cash balance indicates a net increase in payments including investment in financial assets for policy purposes.

Note: Amounts may not sum due to rounding. Rounding is to the nearest million.