

2. CITY HOUSING – RENT REVIEW

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The purpose of this report is seek approval to increase rents for City Housing units from the first rental period unit in July 2003 and to set in place a policy mechanism for ongoing annual reviews.

EXECUTIVE SUMMARY

As a result of the Asset Planning Process it became evident that there is a need for a rent increase in order to ensure the Housing Development Fund is self sufficient in perpetuity, (i.e. no recourse to rates funding). The proposed rentals that equate to the cost of providing the service in perpetuity are contained in table 1.7 of this report. There are two ways of achieving these levels of rent, by an immediate increase to these levels in July 2003 or by way of a stepped increase. It is acknowledged that the proposed rent increase for bedsit units is at a level that results in a net effective change in weekly rent for superannuitants of \$14.00. Option two of Appendix 1 (attached) provides for a stepped rental increase for bedsit and studio units over three years that reduces the annual change in weekly net effective rent to \$5.50 or less, with little effect on long term financial sustainability of the portfolio. However, it should be noted that this may cause some difficulties in immediately implementing some levels of service, owing to funding limitations.

An exercise which assessed the true cost of consumption (the gradual wearing out of the infrastructure) for studio/bedsit, one, two, three and four bedroom units showed that current rental levels did not support the continued provision of housing for tenants in the future, at the existing levels of service without recourse on rates.

Rental levels have been regularly reviewed but not increased since 1997. The current rentals for studio/bedsit units and one bedroom units are such that the tenants (mainly Elderly Persons Housing (EPH) tenants) are unable to qualify for the accommodation supplement provided by central government via Work and Income New Zealand. Central government influences housing affordability by way of the accommodation supplement. Historically low interest rate loans and grants were offered by central government to local authorities to support their housing portfolios. Given that these have not been available for some time it is now reasonable to access central government funding from the accommodation supplement via an increase in rentals.

As it is a legal requirement (Residential Tenancies Act 1986) that tenants receive 60 days notice of any proposed rental increase and as Council rental agreements specify any increase will be applied from the first rental period in July, it is imperative that any proposed rental increase in 2003 be considered by the Council no later than the 24 April Council meeting.

A future annual rent review mechanism which uses revised cost of consumption rents, market rents and inflation indexed rents to balance reviews is also proposed.

The removal of heavily discounted EPH rentals and the introduction of consistency between EPH, public rental housing and Trust Housing rentals is also proposed, as is the removal of dual occupancy charges.

The reasoning behind all initiatives are embodied within this report but in essence the motive is to better align current rental levels with future funding requirements and to introduce a consistent rental charging regime. The draft 2003/04 City Housing budget incorporates the rental increase and will result in an additional net revenue of \$1.1m over the 2002/03 budgeted revenue.

RELEVANT CURRENT POLICY

The asset management policy requires the Council to ensure that the housing fund is financially self supporting, (allowing for all costs including depreciation, loan servicing, administration and maintenance).

The Housing Tenancy Services Policy states:

1. That the Council, in fulfilling its role as housing provider, seek to offer security of tenure to tenants, as appropriate.
2. That, from July 1991, equivalent properties attract the same level of rent for the same level of occupancy.

3. That differential rents between single and double occupancy remain.
4. That the annual rent review date for all tenancies be the first rental period in July.

CONTEXT OF REPORT

This report expands upon discussions held to date with the Housing Subcommittee over the last 18 months, with regard to the proposed Asset Management Plan and the need for a rent increase.

The report is also in line with the two "issues" and "options" seminars held for all Councillors late in 2002.

Within this report is a full assessment of impacts on different types of tenants, market rent levels, accommodation supplement and electricity line charge issues.

ISSUES FOR CONSIDERATION

Current Rent Levels

Current rental levels for elderly persons housing are as follows:

Table 1.0

Bedsit units	\$48.00 per week
Studio units	\$52.00 per week
1 Bedroom units	\$70.00 - \$110.00 per week, average \$73.00
2 Bedroom units	\$100.00 - \$120.00 per week, average \$110.00
3 Bedroom units	\$130 per week (only 1 unit)

Current rent levels for public rental housing are as follows:

Table 1.1

Bedsit unit	\$75.00 per week (1 only)
1 Bedroom units	\$74.00 - \$95.00 per week, average \$88.00
2 Bedroom units	\$100.00 - \$145.00 per week, average \$113.00
3 Bedroom units	\$117.50 - \$170 per week, average \$140.00
4 Bedroom units	\$175.00 - \$180.00 per week, average \$176.00

An arbitrary figure of 80% of market rent (average across the total portfolio) for Council housing units has been often referred to within the Council but there is no formal policy ratifying this. Past history suggests that when the 1989 amalgamation of territorial authorities occurred the level of rents were on average 80% of market at that time.

The analysis undertaken by the Property Asset Management Team to date indicates that current rental levels range from 46% to 85% of market rents, depending on whether you are a tenant of an EPH unit or public rental unit.

The average market rates for 1, 2, 3 and 4 bedroom flats across the whole of Christchurch are as follows:

Table 1.2

1 Bedroom	\$130.00 per week
2 Bedroom	\$165.00 per week
3 Bedroom	\$220.00 per week
4 Bedroom	\$195.00 per week

Note: Tenancy Services bond data 1 July 2001 – March 2002.

It should also be noted that rental demand has driven rents up further since March 2002.

Four bedroom flats are relatively uncommon and this influences the average. By comparison a four-bedroom house has an average market rate of \$259.00 per week.

No market rent information was available from Tenancy Services for studio/bedsit units. However Simes Valuation advise that the level of discount between a one bedroom unit and a studio/bedsit unit would be \$10.00-\$15.00 per week. Therefore it is not unreasonable to assume a difference of \$13.00 per week. However, given that the market rent information is skewed by inner city apartment rents we have deducted these from the assessment and thus reduced the average market rents further to the following levels in Table 1.3:

Table 1.3

Studio/bedsit	\$104.00 per week
1 Bedroom	\$117.00 per week
2 Bedroom	\$159.00 per week
3 Bedroom	\$210.00 per week
4 Bedroom	\$190 - \$250 per week

Affordability

Housing New Zealand (HNZC) charges qualifying tenants 25% of their income for rent. Central government then pays HNZC the difference between the rent paid and the "market" rent in order to ensure continued maintenance, sustainability and expansion of their housing stock. Evidence from the United States, Canada and Britain indicates that a rent to net income ratio of 25-30% is an appropriate benchmark to pursue when considering rent affordability.

Tenants' incomes vary depending on their circumstances. The range of benefit payments are as follows:

Table 1.4

Unemployment Benefit	\$157.37 per week
Sickness/Medical Benefit	\$157.37 per week
Invalids Benefit	\$196.70 per week
Superannuitants (single)	\$238.80 per week
Domestic Purposes Benefit	\$225.40 per week

Central government through Work and Income New Zealand provides the accommodation supplement to low income qualifying tenants. The rent level at which the accommodation supplement starts depends on the type of benefit paid. For superannuitants the accommodation supplement is available when the weekly rent is more than \$60.00 per week, whereas for someone on an unemployment or sickness benefit the accommodation supplement starts at \$39.00 per week and at \$49.00 per week for invalids. The income benefits are lower for those individuals who may be able to change their circumstances through employment, i.e., the unemployed and those on sickness/medical benefits.

Conversely superannuitants and invalid beneficiaries are better off in terms of their ability to pay rent. Having said this it is important not to adjust our rentals to suit individual circumstances. That is the domain of central government through their income benefit and accommodation supplement structures. For this reason it is important that there is no bias or discounted rental structure distinguishing EPH and public rental rates.

Beyond the threshold rental levels mentioned above, Work and Income New Zealand subsidise rents by 75% for those who qualify through low income/asset ownership.

Location Based Rents

Currently the Council does not determine rental levels for different housing complexes based on their location. This assists tenants to live in their desired location and to not be prohibited from doing so owing to the rents being unaffordable. Tenants are therefore often able to live in the neighbourhood they have an affinity with, close to family and friends, support and local amenities.

The disadvantage with this concept is that it makes it difficult to develop Council housing in suburbs with high land values without compensating rent levels.

The benefits of charging rents that do not account for a location premium are considered to outweigh the disadvantages. It does make development in premium locations look like a poor option in terms of its financial viability. However, such developments must be considered in the context of benefit to the overall portfolio and service to our tenants.

We recommend that the existing rent location policy remain in the short to medium term.

Rent Categories

Currently there are nine rent categories across the portfolio. Some of the variations between rental rates within one, two, three and four bedrooms are very minor. The degree of variation needs to be consolidated to ease administration and discrepancies in existing rental rates. By examining the current rental rates and consulting with the Housing Team these existing categories have been consolidated into three categories within one, two, three and four bedroom units with one rate for studio units and one rate for bedsits.

Cost of Consumption, Market Rates and Proposed Rent Levels

The cost of consumption exercise as a result of the Asset Management Plan process determines the full lifecycle costs of maintaining a typical unit (considering interest on funds plus inflation costs), and seeks to determine the current rental rate required to ensure that the management and ownership of that unit is sustainable. The same analysis is carried out on studio/bedsit units, 1, 2, 3 and 4 bedroom units. The results show that for bedsit/studio and one bedroom units that the level of rent required to support the cost of consumption is significantly higher than current rental rates.

Therefore, the proposed rental increase will affect tenants of studio/bedsit and one bedroom units. There will also need to be upward movement in rents for EPH units in the 2, 3 and 4 bedroom category to bring them into line with public rental rates. The resultant cost of consumption rates for studio/bedsit and one bedroom units are summarised as follows:

Table 1.5

Unit Type	Cost of Consumption	Market Rent	Current Rent
Studio/bedsit	\$74.00 per week	\$104.00	\$48.00 - \$52.00
1 Bedroom unit	\$78.00 per week	\$117.00	\$73.00 average

The \$4.00 difference in cost of consumption rates does not adequately reflect the market's perception of the difference between the appeal of a studio/bedsit unit and a one bedroom unit. As stated previously, Simes believe the difference to be in the order of \$10.00 - \$15.00 per week.

Impact of Increase

Any proposed increase will be a significant discount from market rates. No increase in rents has occurred since 1997, yet benefit incomes have increased 10%.

Nevertheless, the increase will impact on some tenants' affordability more than others. The worst affected tenants will be elderly persons who are renting either bedsit or studio units. This is largely because the existing rents of these units is so low, but is also because such tenants are only eligible for the accommodation supplement when their rent is above \$60 per week. In terms of their proposed rent to income ratio however, the affordability is still acceptable.

Considering the market rents and difference between bedsit and one bedroom level of service, we believe the appropriate post July 2003 rental rates for studio/bedsit units should be \$68.00 per week and \$81.00 per week for one bedroom units. These are above the thresholds for eligibility for the accommodation supplement assuming low incomes/assets. Therefore, tenants who previously have not accessed this supplement will need to do so to minimise the effect of the increase. This will require some educational and support work by housing officers to help some tenants manage the transition to the new rental levels. This will impact housing officers' normal work loads and as a consequence some additional resourcing may be required.

The proposed **average** rental levels are as follows:

Table 1.6

Unit Type	Average Weekly Rent
Studio/bedsit	\$70.00
1 Bedroom	\$81.00
2 Bedroom	\$113.00
3 Bedroom	\$140.00
4 Bedroom	\$176.00

Within each category there will be different rate structures. Categories A, B and C represent very good, good, and average quality units respectively. The categories have been developed by the Housing Team in conjunction with the Asset Planning Team.

Table 1.7

Bedsit	\$68.00
Studio	\$72.00
1 Bedroom	A Category \$95
	B Category \$79
	C Category \$65
2 Bedroom	A Category \$120
	B Category \$108
	C Category \$95
3 Bedroom	A Category \$160
	B Category \$132
	C Category \$112
4 Bedroom	A Category \$176

Effects on Tenants

The worst affected tenants are the superannuitants that are currently renting a studio or bedsit unit. The effect is shown below:

Table 1.8

Unit Type	Current Rental Rate	New Rental Rate	Difference	Accommodation Supplement	Net Difference	Net Effective rent	Net effective rent/income
Bedsit	\$48.00	\$68.00	\$20.00	\$6.00	\$14.00	\$62.00	25.96%
Studio	\$52.00	\$72.00	\$20.00	\$9.00	\$11.00	\$63.00	26.38%

For 2, 3 and 4 bedroom EPH units rents will need to be adjusted to public rental units rates.

The net impact on EPH tenants will, on average equate to an additional cost of \$11.00 - \$14.00 per week.

Maximising the Accommodation Supplement to Benefit Council/Minimising Impact on Tenants

The eligibility mechanism for the accommodation supplement does not distinguish between net and gross rents or variations in between. One way we can maximise the accommodation supplement for our tenants is to pay their electricity line charge and charge an equivalent increase in rent. For example a tenant who pays say \$70.00 per week in rent currently pays an additional electricity line charge of \$4.00 per week. If the Council took on the obligation of paying the tenants' line charge and increasing the rent by \$4.00 the tenant would benefit by \$3.00 per week being 75% of \$4.00. The net gain to the Council is nil but the saving to the tenant is significant.

We have had a legal opinion which indicates that this is a legitimate initiative. However, the mechanism will be time consuming and difficult to explain to our tenants.

In addition we recently received Trustpower's proposed charges from 1 April 2003 which show that their line charge may be reduced to as little as \$2 per week. In light of these issues we are not proposing to include this initiative as part of this rent review. However this initiative could be reviewed in future years.

The affordability ratios (rent to net income) of the proposed rent increases are summarised as follows:

Table 1.9

With new Income Benefit rates effective 1 April 2003

Unit Type	Tenant profile	Benefit	Effective rent	Change in rent post review	Affordability ratios	Assumptions
Bed sit	Superannuitants	\$245.30	\$62.00	\$14.00	25.28%	Assumes single person
Bed sit	Unemployed/Sickness	\$161.65	\$46.25	\$5.00	28.61%	Assumes single person
Bed sit	Invalid	\$202.50	\$53.75	\$5.75	26.54%	Assumes single person
Studio	Superannuitants	\$245.30	\$63.00	\$11.00	25.68%	Assumes single person

Studio	Unemployed/Sickness	\$161.65	\$47.25	\$5.00	29.23%	Assumes single person
Studio	Invalid	\$202.50	\$54.75	\$5.00	27.04%	Assumes single person
1 Bedroom	Superannuitants	\$245.30	\$65.25	\$2.00	26.60%	Assumes single person
1 Bedroom	Unemployed/Sickness	\$161.65	\$49.50	\$2.00	30.62%	Assumes single person
1 Bedroom	Invalid	\$202.50	\$57.00	\$2.00	28.15%	Assumes single person
2 Bedroom	Superannuitants	\$377.38	\$98.75	\$0.75	26.17%	Assumes married couple rate
2 Bedroom	Unemployed/Sickness	\$269.40	\$78.50	-	29.14%	Assumes married couple rate
3 Bedroom	Unemployed/Sickness	\$333.28	\$97.25	-	29.18%	Assumes couple with 1 child
4 Bedroom	Unemployed/Sickness	\$646.60	\$73.25	-	11.33%	Assumes 4 individuals

Affordability is a function of income, rent level and the accommodation supplement mechanism. Historically EPH housing rents have been low and therefore the biggest impact in terms of change in affordability affects superannuitants. However, from a straight rent to income equation they are still better off than the unemployed and medical beneficiaries and invalids.

Managing the Change in Rents

The new rents will require people to access the accommodation supplement to minimise the impact of the increases. This is likely to involve tenancy officers helping some tenants with the transition. A full information pack will be sent to tenants advising of the proposed rent increase, how to apply for the accommodation supplement, and this will also contain a telephone help line. It is anticipated that additional resources may need to be employed initially to ensure the transition occurs smoothly. However, the economic benefits that the rent review will bring the fund in the short and long term will outweigh the temporary additional cost.

As mentioned the largest increase in rent affects superannuitants in bedsit and studio units. The number of superannuitants in this category is estimated to be 397. The net effective increase is \$11.00 - \$14.00 per week.

Mechanisms for Future Rent Reviews

Without periodic rent reviews the fund's annual surplus reduces each year as inflation impacts upon operating expenses. In addition infrequent reviews can impose significant rental change which in turn impacts on tenants' ability to budget for rent and other necessary living expenses. In order to maintain an adequate fund return to ensure its sustainability, rents should be adjusted annually by the amount of inflation increase. Furthermore, this needs to be balanced with market rentals, however given that City Housing rents are significantly discounted from market rents it is unlikely that this would impact rent reviews in the short to medium term. The proposal therefore is to adopt the following formula to review rents annually.

$$N = R \times \frac{CPI(t)}{CPI(t-1)}$$

N = new annual rent
R = Previous annual rent
CPI (t) = Consumers' Price Index (All Groups) for the nearest date, either preceding or following the date of review.
CPI (t-1) = Consumers' Price Index (All Groups) for the nearest date, either preceding or following the Commencement date (in this case 1 July 2003).

In addition to relationship to market rents, further balance of the Annual Reviews will be achieved by revising the cost of consumption analysis as this is subject to fluctuation as forecast assumptions change.

Dual Occupancy Charges

Current Housing Policy states that differential rents between single and double occupancy remain. The consensus of the Asset Management and Housing Teams is that there are minimal additional maintenance costs associated with double occupancy tenancies and that the existing policy does not help to encourage sharing of accommodation costs. Therefore, our recommendation is to apply rentals based on the number of bedrooms, not number of occupants and to discontinue the dual occupancy rent policy. This new arrangement reflects "market" practice.

Recommendation:

1. That the proposed new rentals, as detailed in Table 1.7, be adopted effective from the first rental payment date in July 2003, with the exception of the studio and bedsit proposed rentals that are instead to be increased by way of a stepped rental over three years as detailed in option 2, Appendix 1 (attached).
2. That all housing rentals be annually reviewed, increased and reported to the Council prior to implementation in accordance with the 'Future Rent Review Mechanism' as follows:

$$N = R \times \frac{CPI(t)}{CPI(t-1)}$$

N = new annual rent

R = previous annual rent

CPI (t) = Consumers' Price Index (All Groups) for the nearest date, either preceding or following the date of review.

CPI (t - 1) = Consumers' Price Index (All Groups) for the nearest date, either preceding or following the Commencement Date (in this case 1 July 2003).

3. That the current dual occupancy rent policy (Housing Tenancy Services Policy Clause 3) be discontinued.
4. That the Property Manager address the need for extra funds if required to assist tenants to access the accommodation supplement.