



'Reshaping public housing' and work disincentives

Tenants' Union of NSW

Research paper

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Executive summary

The 'reshaping public housing' reforms (RPH), announced by the NSW Government in April 2005, include the following changes:

- changes to the rent rebate system to charge higher rents for tenants in receipt of Family Tax Benefit Parts A and B
- changes to the rent rebate system to charge higher rents for tenants whose households are in receipt of 'moderate incomes'
- imposition of a 'water charge', assessed as a rate of each tenant's rent
- termination of tenancies at the end of their fixed terms where the tenant's income is above the second moderate income threshold.

The changes will interact with the tax system and the social security system – the latter also being changed by the Commonwealth Government's Welfare to Work reforms – to effect public housing tenants' incomes and costs as they move into employment or increase their wages. This interaction has implications for work disincentives.

The paper considers the cases of two hypothetical public housing tenants who are subject to both RPH and the Welfare to Work reforms: 'Louis', a single person with a disability, and 'Melanie', a single parent with two children. The paper's findings include:

- A single person faces an effective average tax rate (EATR) of 69 to 77 per cent at most wage amounts – that is, between 69 and 77 per cent of his wage is lost to the social security, tax and housing systems.
- A single parent faces an effective marginal tax rate (EMTR) of 93 per cent at most wages in the 'moderate income' range introduced by RPH – that is, she keeps just 7 cents in each additional dollar she earns in this range.
- The incomes at which single persons and single parents become ineligible for public housing is not enough to afford 'middle of the road' or 'low end' private rental housing in inner or middle Sydney.

The paper concludes:

- The interactions between the social security system (per the Welfare to Work changes), the tax system and the housing system (per RPH) are numerous and complex, especially for single parents. This may be something of a disincentive itself.
- Contrary to the Commonwealth-State Housing Agreement, RPH contributes to increasing work disincentives.
- There are significant work disincentives at almost all wages up to the point where the top 'moderate income' rebate rate applies and where public housing eligibility is lost.

- Work disincentives persist in the range of wages above the eligibility threshold, because the incomes at which tenants become ineligible is too low for them to rent in the suburbs of the inner and middle rings of Sydney LGAs without cutting their disposable income.
- Though the work disincentives faced by a single person are discouraging, those experienced by a single parent are generally even more discouraging.
- Work disincentives in the lower half of the range wages are largely the result of the withdrawal of Centrelink benefits, in interaction with the tax and housing systems.
- The persistence of work disincentives in the upper half of the range is largely the result of the interaction of the housing and tax systems (and, where Family Tax Benefits are paid, the reduction of FTBA). In particular, the RPH reforms are the largest contributor to these disincentives.
- At any wage between \$125 pw and the top moderate income threshold (\$688 pw), a single person is subject to an EATR between 69 per cent 77 per cent.
- At any wage between \$125 pw and that at the top moderate income threshold (\$766.19 pw), a single parent with two children is subject to an EATR between 69 per cent and 76 per cent.
- Single persons on a 'moderate income' are subject to an EMTR of 81 or 84 per cent.
- Single parents with two children on a 'moderate income' are subject to an EMTR of 72, 93 or 100 per cent.
- Single persons who move out of public housing to a 'middle of the road' one-bedroom flat the inner ring suburbs face a cut in their disposable income of up to \$92.92 pw. They face lower EATRs in private rental (inner and middle Sydney) only at wages in excess of \$800 pw.
- Single parents who move out of public housing to a 'middle of the road' three-bedroom house in the inner ring suburbs face a cut in their disposable income of up to \$165.28. They face lower EATRs in private rental (inner Sydney) only at wages in excess of \$1 200 pw.

The effect of RPH will be to limit public housing tenants to a range of jobs that offer little financial reward. Getting a job paying more will mean moving out of public housing and – unless the person earns a lot more – facing costs that consume almost all of their additional income, or significant constraints as to where they can afford to live.

Introduction

In April 2005, the NSW Government announced, under the banner 'reshaping public housing' (RPH), a platform of reforms to public housing. The reforms were to include, amongst other things, the following changes:

- changes to the rent rebate system to charge higher rents for tenants in receipt of Family Tax Benefit Parts A and B (FTBA and FTBB)
- changes to the rent rebate system to charge higher rents for tenants whose households are in receipt of 'moderate incomes'
- imposition of a 'water charge', assessed as a rate of each tenant's rent
- termination of tenancies at the end of their fixed terms where the tenant is no longer eligible for public housing, including on grounds on income.

Some of RPH (for example, those relating to the water charge, the 'moderate income' rent rebates and aspects of the Family Tax Benefit changes) commenced in December 2005. Other aspects – in particular, the termination of tenancies on grounds of ineligibility – have yet to commence.

At the time of the announcement of RPH, there was already debate as to the work disincentives implicit in different areas of public policy. The debate has concentrated on work disincentives in the social security system, but work disincentives in housing assistance have also received attention, both from researchers (for example, Hulse & Randolph, 2004; Dalton & Ong, 2005; Shelter WA, 2005) and from government. In particular, the current Commonwealth-State Housing Agreement includes, at Objective 1.7, a commitment to 'reducing workforce disincentives to social housing tenants to facilitate greater social and economic participation.'

This paper considers how RPH interacts with the operations of the social security and tax systems (the former itself affected by the Commonwealth Government's 'Welfare to Work' reform agenda), and the implications of this interaction for work disincentives. It does so by setting out the effect of these systems on the disposable incomes of two hypothetical public housing tenants:

- 'Louis', a single person with a disability who is capable of working 15-29 hours pw
- 'Melanie', a single parent with two children (a boy and a girl) aged 12 and 10 years.

Both Louis and Melanie are subject to the Welfare to Work reforms – specifically the proposed 'Enhanced Newstart Allowance' (ENA) – and RPH, including the changes relating to continuing eligibility. (That is, they applied for their respective Centrelink payments after 1 July 2006, and commenced their public housing tenancies after 1 July 2005.)

The paper is in two parts. The first part considers the disposable incomes of Louis and Melanie respectively, over a range of wage amounts, after taking into account

the operations of the social security, tax, rent rebate and water charge systems. The second part considers the effect on the disposable incomes of Louis and of Melanie of having to move in private rental housing upon the termination of their tenancies on grounds of no longer meeting the income eligibility criteria. Because private rents vary geographically, this part also considers the locational dimension of these effects of RPH.

Measures of work disincentives

In its examination work disincentives, this paper uses a number of related concepts to measure two basic work disincentive problems: first, the *'why work?'* problem; and secondly, the *'how much work?'* problem. It considers these problems primarily from a financial perspective – that is, it looks at people's incomes and costs. We recognise, however, that the decisions that people make about work are not purely financial ones. As Hulse & Randolph (2004) suggest, there are many other 'behavioural factors' at work in these decisions, and their research indicates that motivations such as the maintenance of skills, confidence and self-esteem are strong, even in the face of significant financial disincentives. It should be kept in mind, then, that the financial disincentives discussed in this paper not only discourage the earning of additional income, but the realisation of those more personal hopes as well.

The 'why work?' problem.

This problem refers to financial disincentives that discourage an unwaged person from getting a job. Entering work usually means a relatively large increase in gross income, and the implications for a person's net income are measured in terms of the *replacement ratio* (RR) and the *effective average tax rate* (EATR).

The RR compares the disposable income a person receives if unemployed against the disposable income they would receive if employed at a given wage. For example, where a wage amount has an RR of 90 per cent, an unemployed person receives 90 per cent of the disposable income they would receive if they took a job paying that wage. The closer the RR is to unity, the greater the financial disincentive to work. As Hulse & Randolph state, 'for most unemployed people, this is a very real calculation' (2004: 7)

The EATR measures how much of a given wage is lost to tax, Centrelink benefit withdrawal and increased housing costs (that is, rent rebate reduction and increased water charge). Unlike RR, which compares net results at two given incomes, the EATR compares the increase in a person's disposable income to the increase in their total income that comes from earning a given wage. In other words, it introduces a consideration of fairness – 'how much of what I earn do I keep?' – that is relevant to decisions about entering work.

The result of these sorts of considerations is often referred to as an 'unemployment trap', because they discourage people from entering work in the first place.

The 'how much work?' problem.

This problem refers to financial disincentives that discourage a person in a job from increasing their wage: for example, by doing some overtime, or getting a better paid position. These sorts of increases are usually relatively small – at least compared to

those that come from moving from unemployment into employment – and the implications for a person's net income are measured in terms of the *effective marginal tax rate* (EMTR).

The EMTR measures how much of an additional dollar of income is lost to tax, Centrelink benefit withdrawal and increased housing costs (that is, rent rebate reduction and increased water charge). EMTRs of 60 per cent and above are regarded as 'high' (Polette, 1995; Wood & Ong, 2005).

The result of this sort of consideration is often referred to as a 'poverty trap' because it discourages or prevents people from increasing their income.

In considering these problems in terms of unemployment traps and poverty traps, one can consider whether the trap is 'deep' or 'wide.' A deep unemployment trap, for example, might be expressed in terms of a short range of wages that have very high RRs, such that there is little point getting a job that pays such a wage. A deep poverty trap would be indicated by a high EMTR such that earning a few extra dollars would amount to no net gain, or even a net loss of income. On the other hand, a deep trap may be easier to 'jump over' than a wide trap. In a wide unemployment trap, a relatively large range of wages – and hence jobs – are unattractive; in a wide poverty trap, even a relatively large wage increase may not be worthwhile. And to make the jump to a rewarding wage may be unrealistic.

1. Wages, social security, tax, rent rebates and water charges

This Part of the paper considers the effects of the tax, social security and housing systems on the disposable incomes of Louis and Melanie as they increase their respective incomes through wages – either by moving out of unemployment into a job, or by earning more.

The interaction of these systems is presented in four graphs for each of Louis and Melanie. Each point at which the graph turns represents an event in either the tax, social security or housing systems – for example, a change in rate – each of which is discussed in more detail in the Notes at the end of the paper.

In this paper of the paper, we consider ‘disposable income’ as the sum of income from the following sources:

- wages
- ENA (reduced as wages increase) and
- FTBA and FTBB (Melanie only).

less the following costs:

- tax
- Medicare levy
- rent (rebated according to income) and
- water charge.

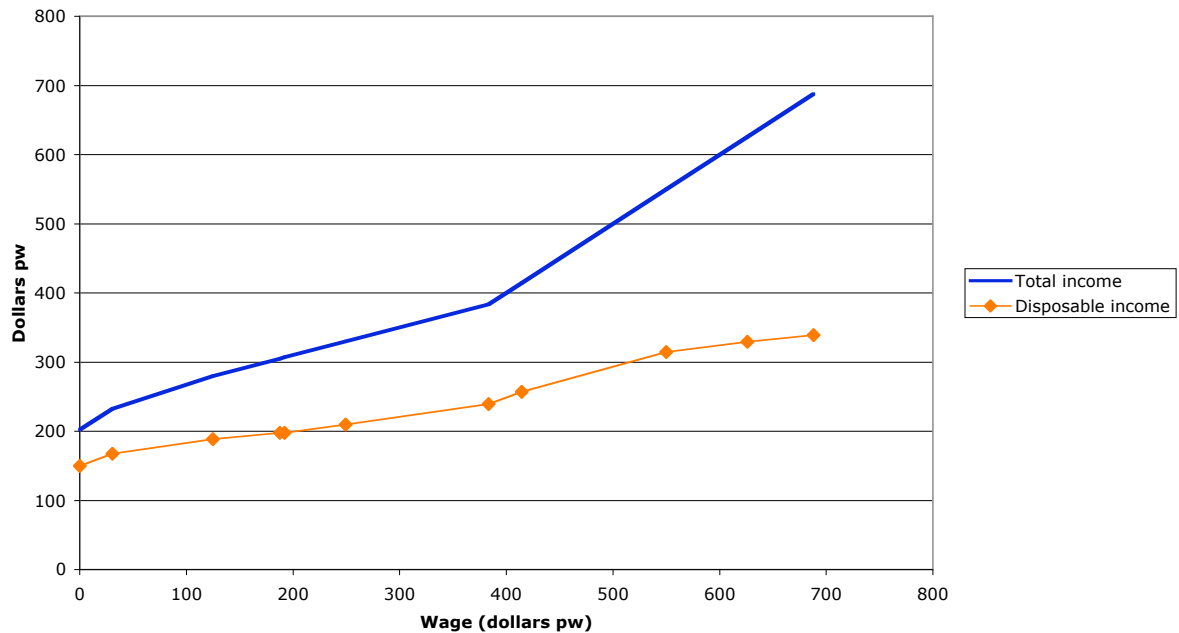
Note that this analysis does not consider the loss of concessions such as travel and health concessions. Louis and Melanie would each be eligible for these concessions, and the loss of them as Louis and Melanie move into work would affect their disposable incomes. Also, the analysis in relation to Melanie does not include any income from Child Care Benefit, nor the cost of child care: in effect it assumes that Melanie does not receive the benefit, and has no child care costs.

Note also that in each of the cases of Louis and Melanie, the rent continues to be rebated to the top of the moderate income sliding scale introduced by RPH. This means that we are assuming that the market rent for their respective premises is not lower than the rebated rent (and therefore does cut in before the highest rate of rebated rent is reached).

1.1. Louis.

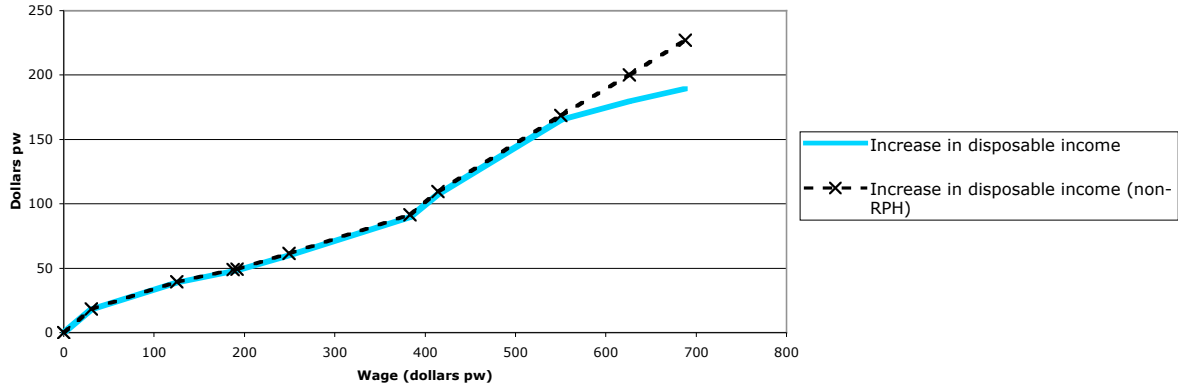
At the starting point of our analysis, Louis is unwaged and receives ENA. If Louis gets a job, he will begin to pay tax and his rent and water charge will increase, and if he earns more than a small amount his ENA will be reduced. Figure 1.1.1 illustrates the relationship between his wage, total income and disposable income.

Figure 1.1.1. Louis – income and disposable income



There are two notable features of Figure 1.1.1. First is the slow rate at which Louis's total income increases in the lower half of the wage range. This reflects the reduction in ENA at these wages, until it is withdrawn altogether at \$383.33 pw. Thereafter, Louis's wage represents his sole source of income. The second feature is how slowly Louis's disposable income rises compared to his total income and wage through the upper half of the range of wages. Figure 1.1.2 shows the slow rise of Louis's disposable income in relation to his wage. It also shows how much the RPH reforms reduce his disposable income.

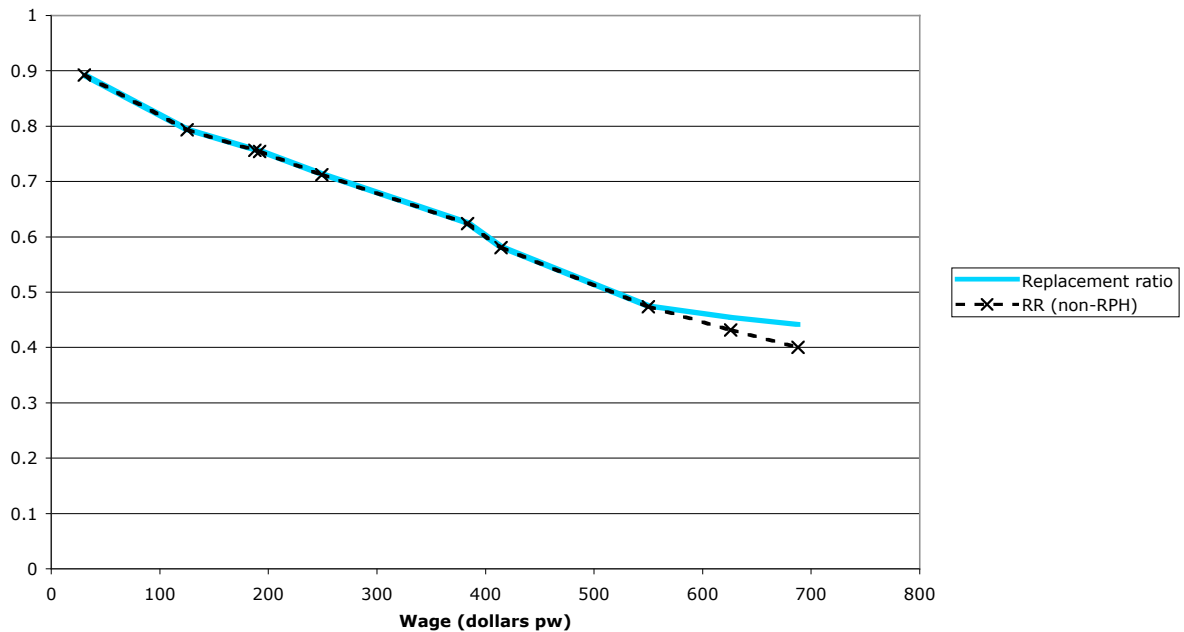
Figure 1.1.2. Louis - increase in disposable income



The RPH reforms reduce Louis’s disposable income, at the top wage in the range, by \$39.67 pw, or almost 12 per cent.

The work disincentive effects of this slow improvement in disposable income are shown in Figure 1.1.3 in terms of RRs: that is, how much of Louis’s disposable income while employed he would have had anyway if he was unemployed. The figure also shows the effect of the RPH reforms on Louis’s RRs.

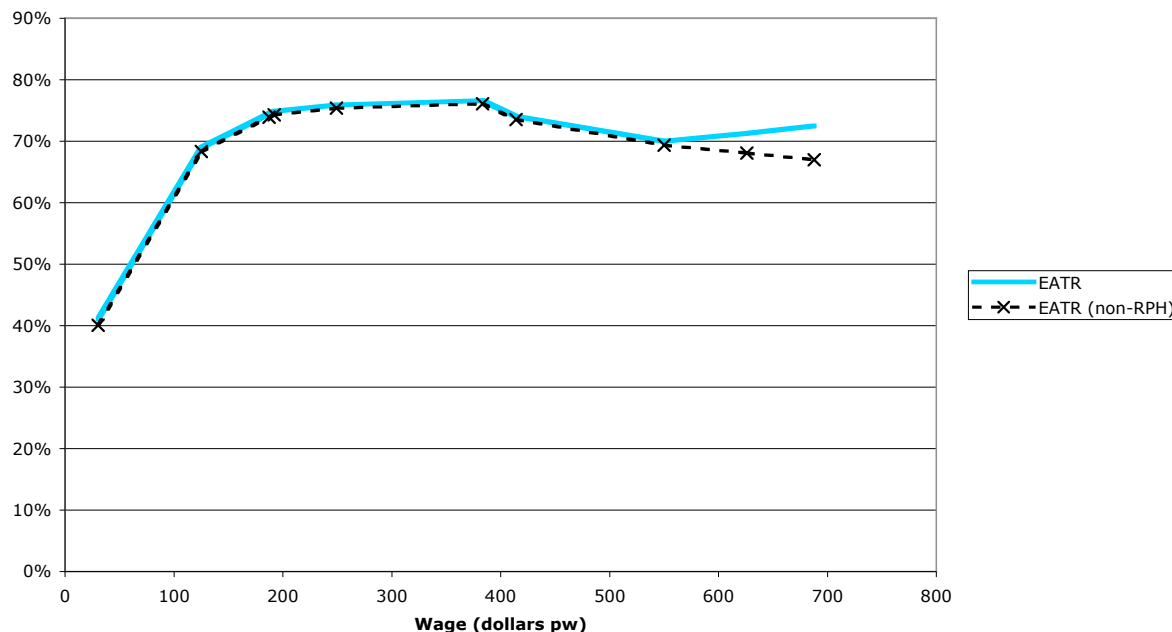
Figure 1.1.3. Louis – RR



The RR line shows that for most of the range of wages considered here, the RR remains above 0.5. Considering the top wage in the range, Louis would still receive about 44 per cent of the disposable income it provides if he was unemployed.

Figure 1.1.4 shows the EATRs faced by Louis, including the effect on EATRs of the RPH reforms.

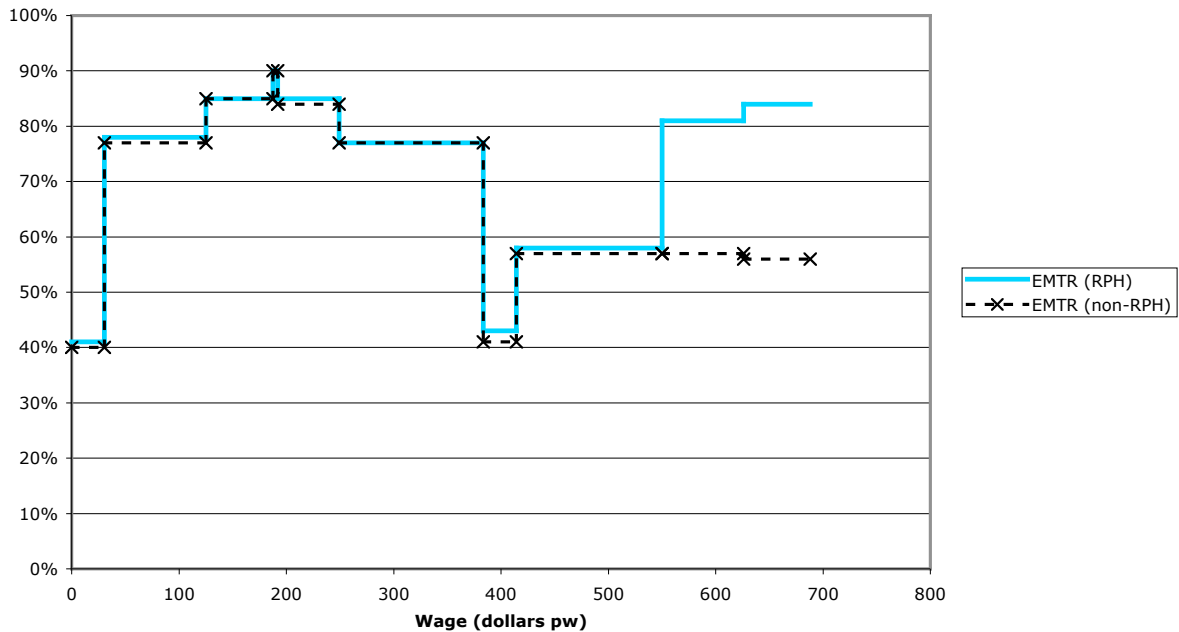
Figure 1.1.4. Louis – EATR



This figure tells an even more discouraging story: for jobs paying more than \$125 pw, the EATR is almost always above 70 per cent. In other words, if Louis gets a job in this wage range, he will lose between 69 to 77 per cent of his additional income to the social security, tax and housing systems.

If Louis is already in employment and looking to increase his wage by doing some overtime or going for a better paid position, he might consider how much of this potential additional income he gets to keep. This is indicated by the EMTR for his wage, as illustrated by Figure 1.1.5. The figure also shows how the RPH reforms contribute to EMTRs.

Figure 1.1.5. Louis – EMTR



It is worth keeping in mind that in the Commonwealth income tax system, the top marginal tax rate is 47 cents in the dollar on incomes over \$90 000 pa (\$1 726.12 pw). For Louis, the tax, social security and housing systems generate an EMTR in excess of the top marginal income tax rate – often much in excess – at almost all wage amounts. For most wage amounts, Louis’s EMTRs are also well above the 60 per cent benchmark for ‘high’ EMTRs (Polette, 1995; Wood & Ong, 2005).

The high EMTRs encountered at low wages are mostly products of the social security system through the tapered withdrawal of ENA (the peak at 90 per cent represents the phasing in of the Medicare levy). In the higher end of the wage range, the high EMTRs encountered are the product of the tax system in interaction with the housing system, and in particular the moderate income rent rebate rates introduced as part of the RPH reforms. Louis’s rent represents that single largest contributor to the very high EMTRs encountered at these wage amounts: for Louis, the sliding scale of the moderate income rent rebate rate represents a marginal rate of 49.92 per cent. As the figure shows, the very high EMTRs (81 and 84 per cent) in this wage range would be significantly lower but for the RPH reforms.

Summary: the structure of work disincentives for Louis

The range of wage amounts Louis may earn before he becomes ineligible for public housing can be considered in two almost equal halves. In the lower half of the range, the withdrawal of ENA is a significant disincentive to work. In the higher half of the range, disincentives persist due mostly to the moderate income rent rebate rate introduced by RPH reforms. These disincentives increase through the higher half of the range until they are of a similar magnitude to those produced by the withdrawal of ENA at lower wages.

But for the RPH reforms, Louis would experience something of a break from high EMTRs in the higher end of the range. Instead, if he struggles through or ‘jumps

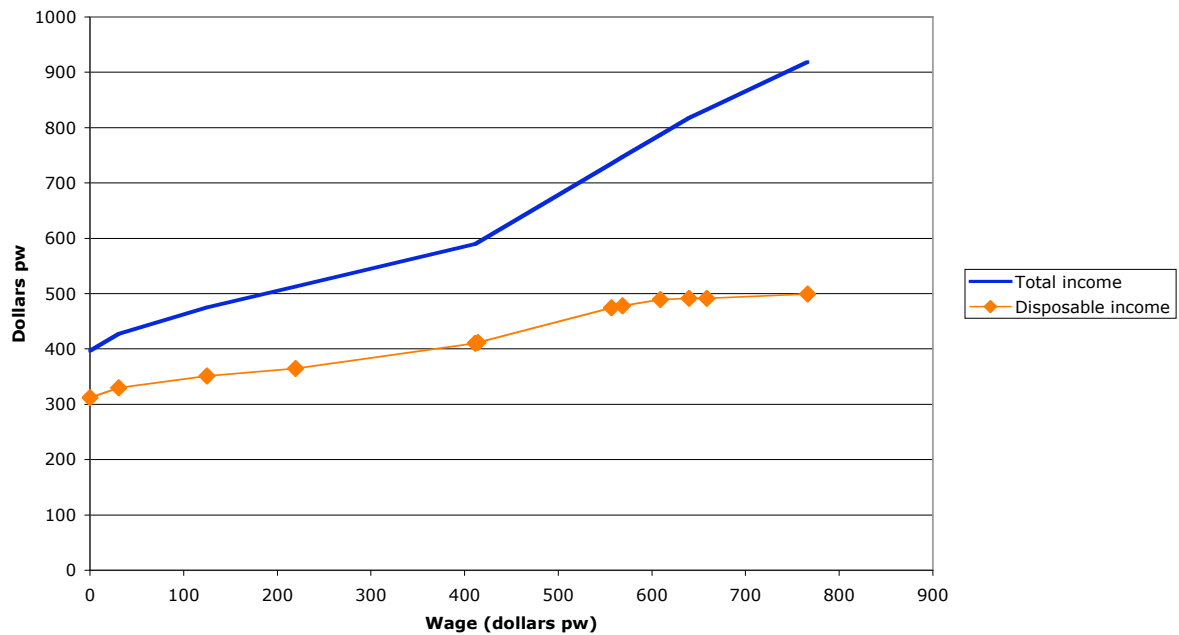
over' the work disincentives associated with the withdrawal of ENA, he will encounter similar work disincentives in the moderate income range.

So far the analysis has not considered whether the loss of eligibility for public housing past the top wage in the range creates an additional work disincentive (or, on the contrary, whether upon leaving public housing Louis also leaves behind the work disincentives associated with it). These questions are considered in Part 2 of this paper.

1.2. Melanie.

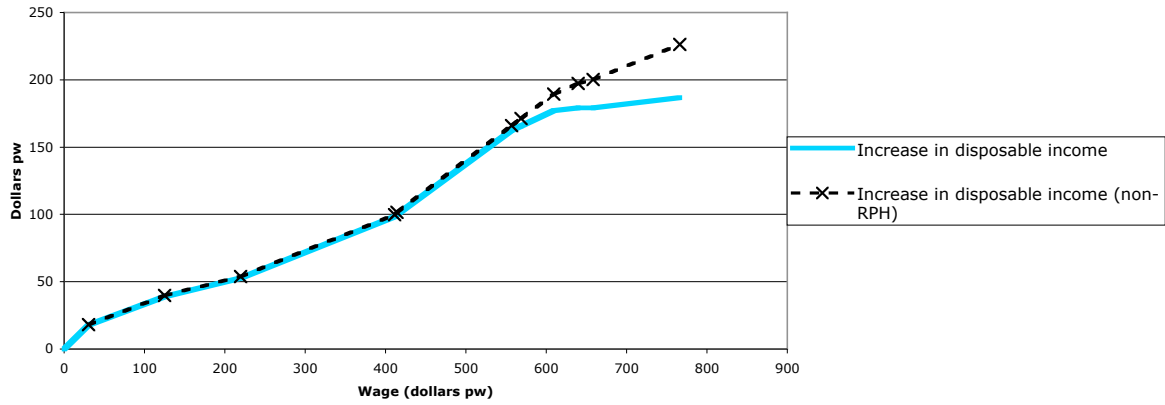
At the starting point of our analysis, Melanie is unwaged and receives Enhanced Newstart Allowance and FTBA and FTBB. If Melanie gets a job, she will begin to pay tax, her rent and water charge will increase and, if she earns more than a small amount, her ENA will be reduced. Also, at higher wages her FTBA will be reduced. Figure 1.2.1 illustrates the relationship between her wage, her total income, and her disposable income.

Figure 1.2.1. Melanie – income and disposable income



The contours of Figure 1.2.1 are similar to Louis's Figure 1.1.1, depicting the withdrawal of ENA to wage \$411.33 pw and the persistently slow rise of disposable income. As figure 1.2.2 shows, the line representing Melanie's disposable income is even flatter than Louis's, especially at the higher end of the wage range. The figure also shows how the RPH reforms contribute to this effect.

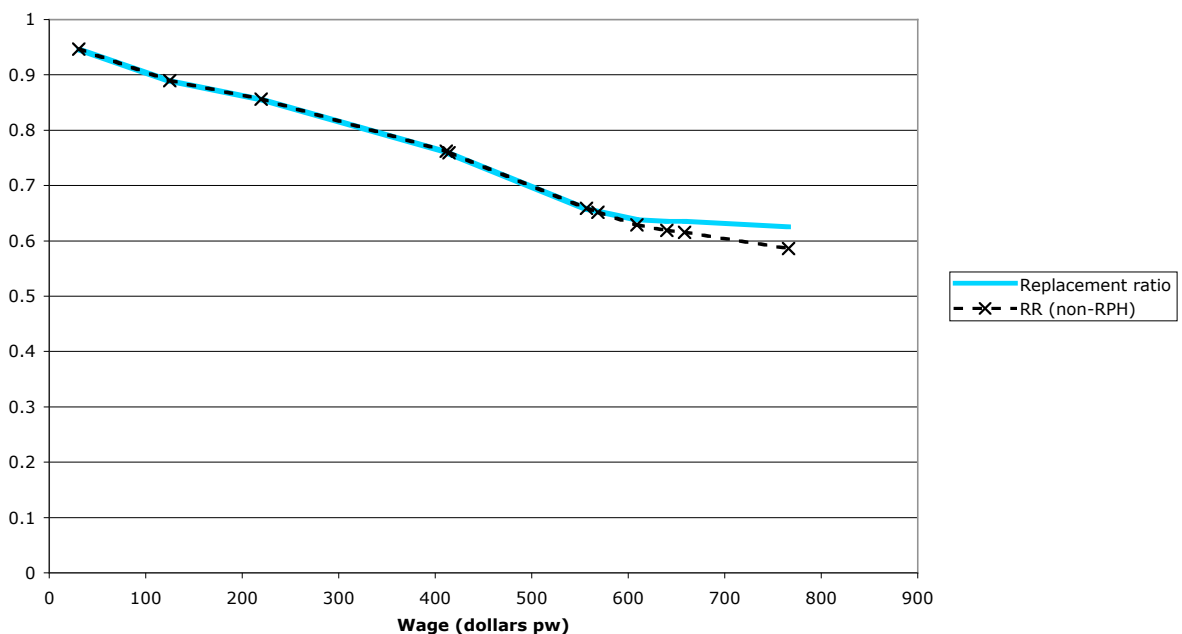
Figure 1.2.2. Melanie – increase in disposable income



Compared with Louis’s disposable income, Melanie’s disposable income starts higher and improves more slowly: after earning \$766.19 pw, Melanie’s additional disposable income is slightly less than Louis’s additional disposable income after earning \$688 pw. This is because Family Tax Benefit provides Melanie with a higher disposable income in the lower half of the range, before it begins to be withdrawn in the higher half.

The work disincentive effects of this slow improvement in disposable income are shown in Figure 1.2.3 in terms of RRs. The figure also shows the effect of the RPH reforms on RRs.

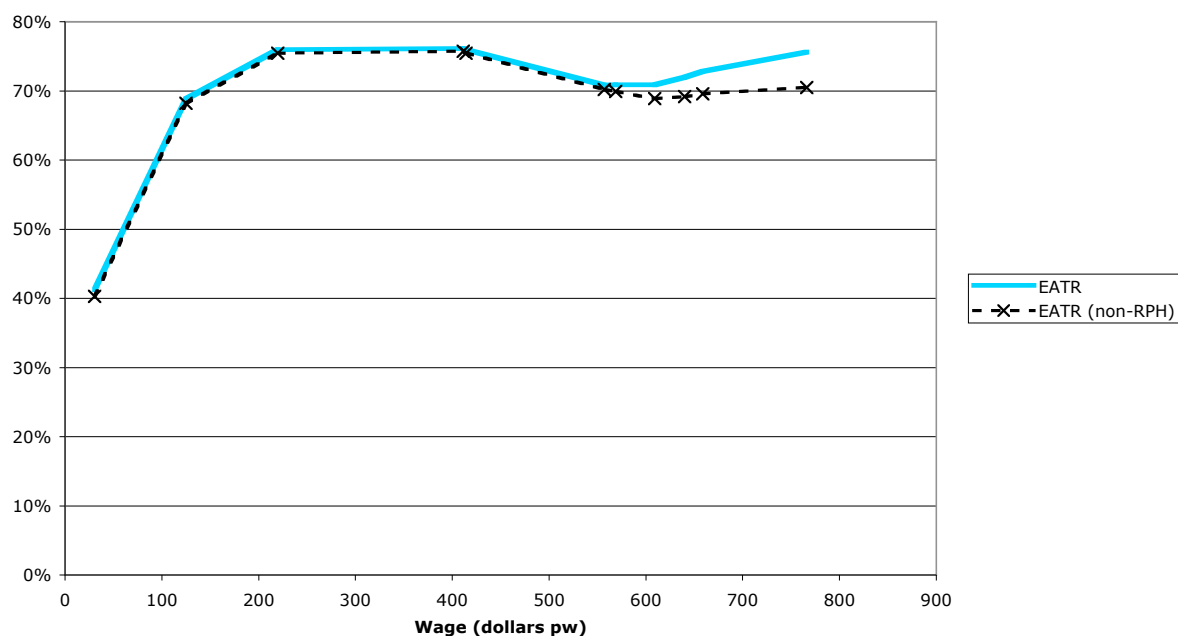
Figure 1.2.3. Melanie – RR



For Melanie there is no job paying a wage in this range with an RR less than 0.62 – generally higher than the RRs that apply to Louis. (But for the RPH reforms, the RR would drop below 0.6 near the top of the wage range). This is significant: it indicates that the only wage amounts promising an attractive increase in disposable income are wage amounts in excess of the top moderate income threshold and the threshold for eligibility for public housing. To allow Melanie to remain eligible while taking up a job that promises an increase in disposable income in the same proportion that Louis gets from a job paying at the top eligible wage in his range, the Department of Housing would need to adjust upwards the eligibility threshold considerably.

Figure 1.2.4 shows the EATRs faced by Melanie, as well as the effect of the RPH reforms on EATRs.

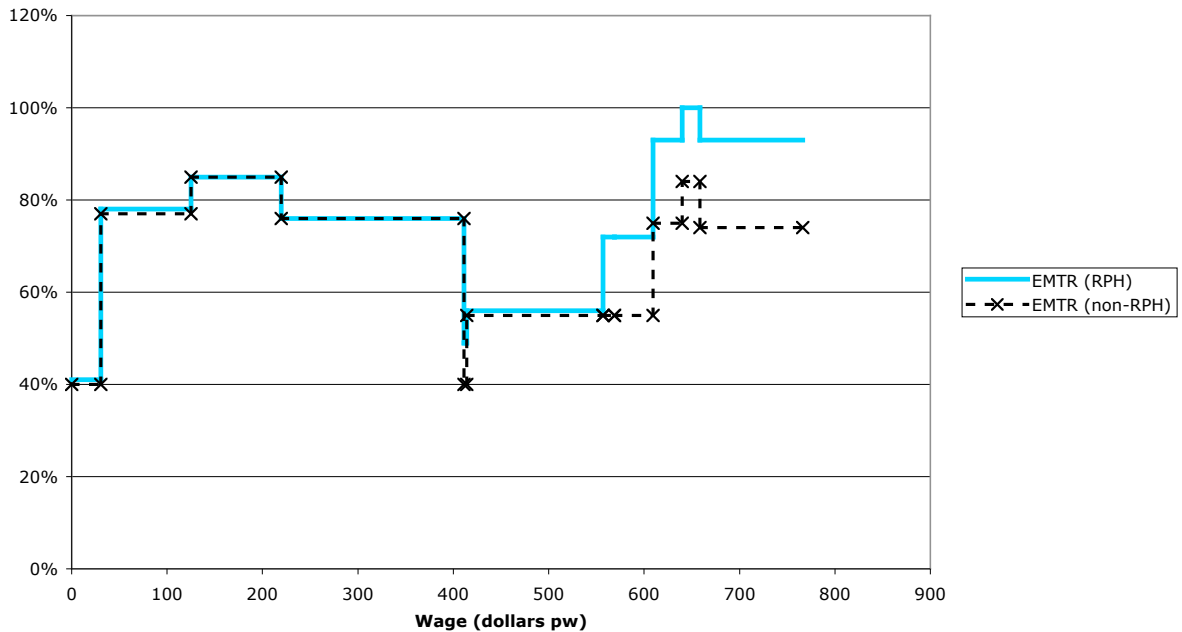
Figure 1.2.4. Melanie – EATR



Like Louis, Melanie faces high EATRs – not less than 69 per cent – for all jobs paying more than \$125 pw.

If, in spite of these disincentives, Melanie does work, and looks to increase her wage, she will encounter EMTRs as shown in Figure 1.2.5. The figure also shows the contribution of the RPH reforms to EMTRs.

Figure 1.2.5. Melanie – EMTR



Like Louis, Melanie will encounter EMTRs considerably greater than the top marginal income tax rate for most of the range of wages considered – never less than 40 per cent, and mostly in excess of 70 per cent and, at one stage, reaching 100 per cent. Also like Louis, Melanie’s rent is the single largest contributor to the very high EMTRs encountered at the higher end of range of wage amounts, and this is a result of the RPH reforms, particularly the moderate income rent rebate rates. For Melanie, the sliding scale of the moderate income rent rebate rate can be expressed as a marginal rate of 43.31 per cent. This contributes to EMTRs of 72, 93 and even 100 per cent between the moderate income thresholds. But for the RPH reforms, EMTRs at these wage amounts would be considerably lower.

In contrast to Louis, there is more of a stacking effect in Melanie’s EMTRs, because in addition to the higher rates of rent paid at wages in the moderate income range, two other marginal costs are also encountered in that range. First, at wage \$609.18 pw, Melanie begins paying the Medicare levy, which is phased in at a marginal rate of 20 per cent. Next, at wage \$639.84 pw, Melanie begins to lose her FTBA at a rate of 20 cents in the dollar. The stacking of these marginal costs on top of the moderate income rent rebate rate results in the top EMTR of 100 per cent. At most wages between the RPH moderate income thresholds, Melanie keeps not more than 7 cents from every additional dollar she earns.

Summary: the structure of work disincentives for Melanie.

As with Louis, Melanie’s range of wage amounts that still make her eligible for public housing can be considered in two almost equal halves. In the lower half of the range, the withdrawal of ENA generates a significant disincentive to work. In the higher half of the range, disincentives persist due mostly to the moderate income rent rebate rate introduced by RPH reforms. Through most of these wage amounts the RPH reforms also stack with the Medicare levy and the withdrawal of FTBA.

This results in EMTRs that are even higher than those produced by the withdrawal of ENA.

Melanie faces even greater work disincentives than Louis, in terms of getting into work (for example, higher RRs) and of earning additional income while in work (that is, very high EMTRs at wages in the RPH moderate income range). If she struggles through or jumps over the work disincentives associated with the withdrawal of ENA in the lower half of the wage range, she encounters an even stronger combination of work disincentives in the RPH moderate income range.

In Part 2 of the paper we consider the effect of the loss of eligibility for public housing as a further work disincentive for Melanie.

2. Loss of public housing eligibility and the cost of private rental

This Part of the paper examines the effects of becoming ineligible for public housing and having to find accommodation in the private rental market.

At the time of writing, the Department of Housing has yet to publish all its criteria for the assessment of the continuing eligibility of public housing tenants. However, it has indicated that it proposes that tenants will be ineligible for continued public housing where their household income is in excess of the second 'moderate income' threshold for a household of that type (Department of Housing, 2006).

The effects considered are:

- effects on disposable income resulting from renting privately in particular areas
- locational constraints resulting from renting at an affordable rate (30 per cent of income).

The following analysis uses data from the NSW Department of Housing's *Rent and Sales Report* (2005) relating to median rents for localities throughout the State. For Sydney, the localities are local government areas (LGAs); outside of Sydney, the localities are statistical divisions.

There are two related interpretations of the significance of median rents that are relevant here. First, it is a measure as to the relative quantity of housing: that is, where the median rent is higher than the amount a person is looking to pay, more than half the properties available to rent are beyond their budget. Second, the median rent is a measure as to the relative quality of housing: it represents the rent for a 'middle of the road' property for that area.

The *Rent and Sales Report* also includes data as to rents at the first and third quartiles of properties rented in each Sydney LGA, which can be interpreted in a similar way: in particular, where the first quartile is more than the rent a person is looking to pay, more than three-quarters of the properties available to rent are beyond their means, and the rent they are looking to pay will buy them a 'low-end' property only.

There are two important factors bearing on Louis's and Melanie's prospects for renting privately that are not considered in this analysis, but which should be noted. First, the analysis does not consider how much of the affordable housing stock is appropriate to either Louis or Melanie (for example, in terms of being suited to Louis's disability). Second, the analysis does not consider the extent to which affordable housing stock is sought and occupied by households who could afford to pay more. As the research of Yates, Wulff & Reynolds suggests, 'higher income households, particularly if they are employed young couples, may seek to pay lower rents and may be given some preference by agents and landlords in accessing low rent dwellings' (2004: 26).

Note also that in this Part, water costs (including the Department of Housing's water charge) have not been included in costs in determining disposable incomes. Water costs are determined differently between the tenures: in public housing, the water charge varies according to income; in private rental housing water costs vary

according to use or are built into the rent. We do not have data as to water costs in private rental housing, so have removed this cost for the purpose of fair comparisons between the tenures.

Finally, another note on comparisons: we noted that in Part 1 it is assumed that both Louis and Melanie are renting premises where the market rent is not lower than the 30 per cent rebated rent (if it were otherwise, they would pay the market rent, rather than the 30 per cent rebated rent). In Part 2, we continue with that assumption. This means that the most relevant 'like for like' comparisons will be where the private market rent is at least as high as the 30 per cent rebated rent paid at the high end of wages in public housing. As we will see, this means the following part will focus on comparing the effect of moving out of public housing into the Sydney private rental market – especially in the inner and middle rings of Sydney LGAs.

2.1. Louis.

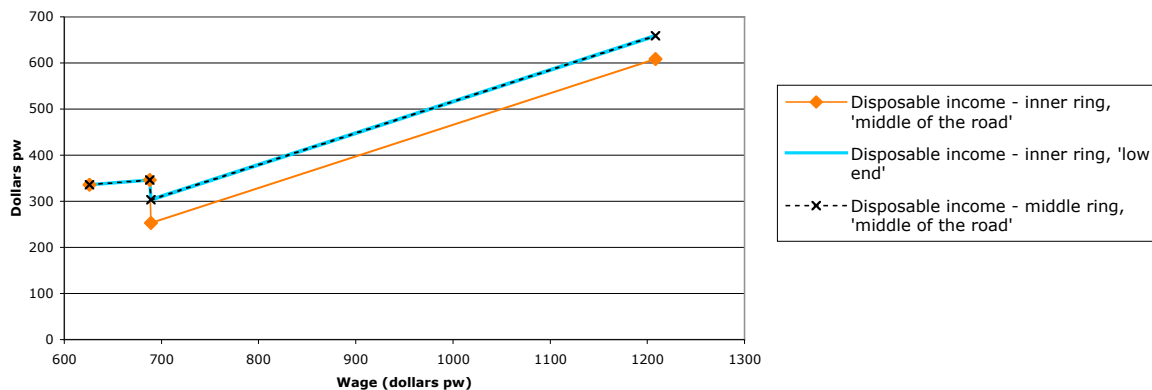
If he earns a wage in excess of \$688 pw, Louis is no longer eligible for public housing, and at the end of the fixed term his tenancy is terminated. Thereafter Louis will look to the private rental market for his housing. As a public housing tenant, Louis's dwelling was a one-bedroom flat – we will assume that he will look for the same in the private rental market.

Note that because he does not receive a qualifying Centrelink payment, Louis is not eligible for Rent Assistance.

First we will consider the effect on Louis's disposable income if he is concerned to live in a particular location (because, for example, he wants to be close to his work or his doctor). In most of the outer ring of Sydney LGAs and outside of Sydney, the median rent is affordable for all wages above \$688 pw. This analysis considers what happens if Louis is concerned to stay in the suburbs of the inner or middle ring of Sydney LGAs. These areas are, of course, a major part of the New South Wales rental market. They also include a number of public housing estates, where the Department of Housing and other agencies are attempting to encourage tenant employment.

Figure 2.2.1 shows how much Louis's disposable income drops if he loses eligibility for public housing at a wage of \$688 pw and rents in these areas, and how much more than the eligibility threshold he needs to earn before he comes out ahead.

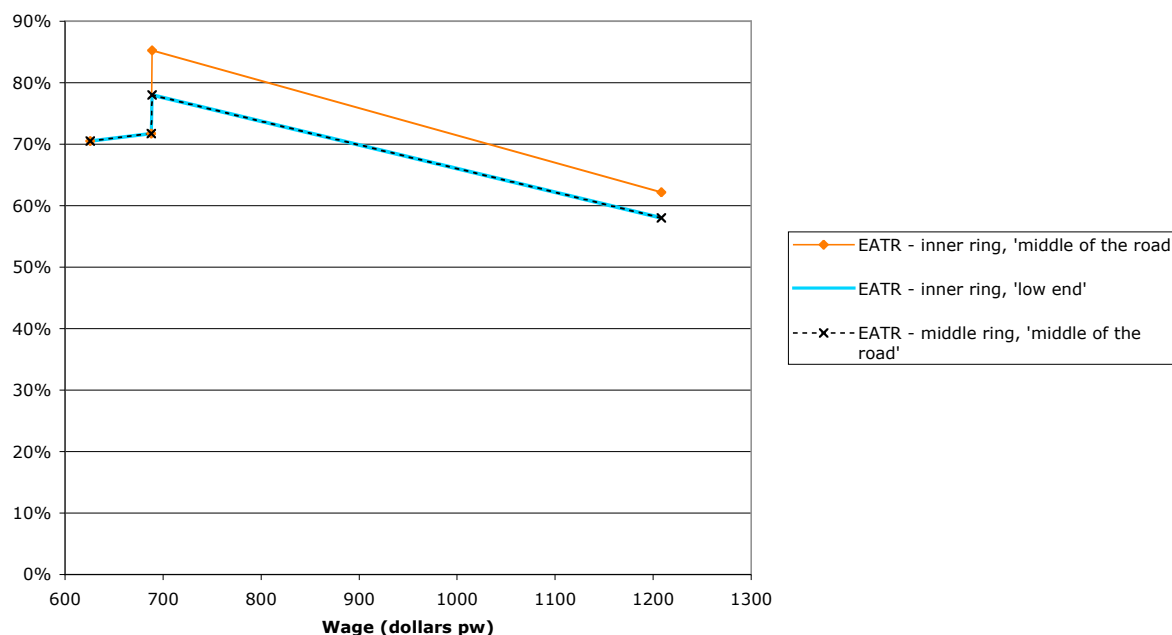
Figure 2.1.1. Louis - disposable income as a private tenant



If Louis is only just ineligible for public housing, and he rents either a 'low end' property in the inner ring, or a median rent property in the middle ring (coincidentally, the amount is the same), his disposable income drops \$42.92 pw. If he rents a median rent property in the inner ring suburbs, his disposable income drops \$92.92 pw, and will have to earn well over \$800 pw before he is in front again.

Figure 2.1.2 shows, in terms of EATRs, how much of Louis’s wage is lost as he moves into private rental housing.

Figure 2.1.2. Louis - EATRs as a private tenant



Up to 85 per cent of Louis’s wage is lost to tax and housing costs if Louis rents a ‘middle of the road’ flat in the inner ring, and up to 78 per cent in the middle ring. These rates fall below the EATR that applied to Louis’s highest wage while still eligible for public housing only if Louis earns more than \$1 000 pw and \$800 pw respectively.

In other words, the wage at which Louis becomes ineligible for public housing under the RPH reforms is too low for him to rent most properties in the inner and middle rings of Sydney without significantly cutting his disposal income.

Secondly, we consider the alternative: how Louis’s locational choices will be constrained if he seeks premises for which the rent is not more than 30 per cent of his income. As the foregoing indicates, Louis would have to move out of most areas in the inner and middle rings of Sydney unless his wage is rather higher than the eligibility threshold. Table 2.1.1 shows which LGAs have median rents that are affordable only at wages higher than \$688 pw, and how much higher than that amount Louis would have to earn in order to access affordable rental housing.

Table 2.1.1. Louis – locations constrained by affordable median rents

Location ¹	Income required for an affordable 'middle of the road' flat	Gap between threshold and required income
Ashfield	699.30	11.30
Auburn	699.30	11.30
Burwood	699.30	11.30
Strathfield	715.95	27.95
Tweed Heads ²	715.95	27.95
Rockdale	732.60	44.60
Kogarah	765.90	77.90
Pittwater	774.23	86.23
Ku-ring-gai	782.55	94.55
Hunters Hill	799.20	111.20
Leichhardt	815.85	127.85
Lane Cove	865.80	177.80
Hornsby	865.80	177.80
Warringah	865.80	177.80
Randwick	932.40	244.40
Mosman	940.73	252.73
Botany Bay	999	311
North Sydney	999	311
South Sydney	999	311
Waverley	999	311
Woollahra	999	311
Canada Bay	999	311

¹ The *Rent and Sales Report* no 73 does not present data for one-bedroom dwellings in Campbelltown, Wollondilly, Kiama and Shellharbour, because too few bonds were lodged for such premises in these areas.

² The data for Tweed Heads relates to two-bedroom units. The *Rent and Sales Report* does not provide data for one-bedroom units outside the Sydney Greater Metropolitan Region.

Manly	1032.30	344.30
Willoughby	1148.85	460.85
Sydney	1165.50	477.50

The high rents in Sydney mean that Louis cannot afford even the first quartile or 'low end' rent in many areas unless he earns considerably more than the eligibility threshold, as Table 2.1.2 shows.

Table 2.1.2. Louis – locations constrained by affordable 'low end' rents

Location	Income required for an affordable 'low end' flat	Gap between threshold and required income
Ku-ring-gai	699.30	11.30
Canada Bay	749.25	61.25
Warringah	765.90	77.90
Lane Cove	795.87	107.87
Mosman	815.85	127.85
Randwick	832.50	144.50
Woollahra	832.50	144.50
Waverley	865.80	177.80
North Sydney	899.10	211.10
South Sydney	899.10	211.10
Manly	899.10	211.10
Sydney	999	311
Willoughby	1007.33	319.33

Summary: the structure of work disincentives for Louis

In Part 1 we noted that significant work disincentives were generated over the range of wages at which Louis remains eligible for public housing. In this part we have seen that if Louis rents in the inner and middle rings of Sydney, significant work disincentives persist at wages beyond the eligibility threshold. For example, if Louis is concerned to stay in inner Sydney, he is better off earning \$688 pw and staying in public housing than earning more than \$800 pw and moving into a 'middle of the

road' private rental flat. The loss of disposable income to unaffordable private market rents in the inner and middle rings of Sydney contributes to EATRs that are higher than those encountered in public housing until Louis's wage is more than \$900 pw, after which point they decline.

The alternative for Louis is to move out of the inner or middle ring to the outer ring of suburbs, or out of Sydney altogether. Both the costs of staying in inner or middle Sydney, and the constraints on choice of location if moving out, are significant work disincentives.

2.2. Melanie.

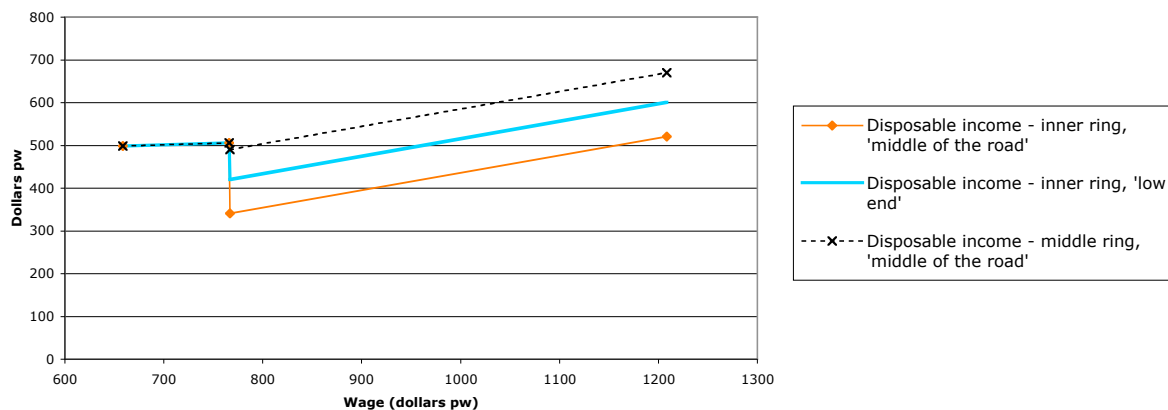
If she earns a wage of more than \$766.19 pw, Melanie is no longer eligible for public housing, and at the end of the fixed term her tenancy is terminated. Thereafter Melanie will look to the private rental market for her housing. As a public housing tenant, Melanie's dwelling was a three-bedroom house – we will assume that she will look for the same in the private rental market.

Melanie, unlike Louis, is eligible for Rent Assistance (because she receives more than the base rate of FTBA). The maximum rate of Rent Assistance is \$58.31 pw, which is added to her FTBA (hence Melanie's income at the lowest wage amount that makes her ineligible for public housing will be \$978.12 pw).

First we will consider the effect on Melanie's disposable income if she is concerned to live in a particular place (because, for example, she wants to live close to her work or her children's schools). In most areas outside Sydney, and in most of the outer ring of Sydney LGAs, the median rent is affordable at \$978.12 pw. The following analysis considers what happens to Melanie's income if she is concerned to stay in the inner and middle rings of Sydney LGAs.

Figure 2.2.1 shows how much Melanie's disposable income may drop when she leaves public housing to rent privately, and how much more than the eligibility threshold she needs to receive before she comes out ahead, if she rents in these areas.

Figure 2.2.1. Melanie - disposable income as a private tenant

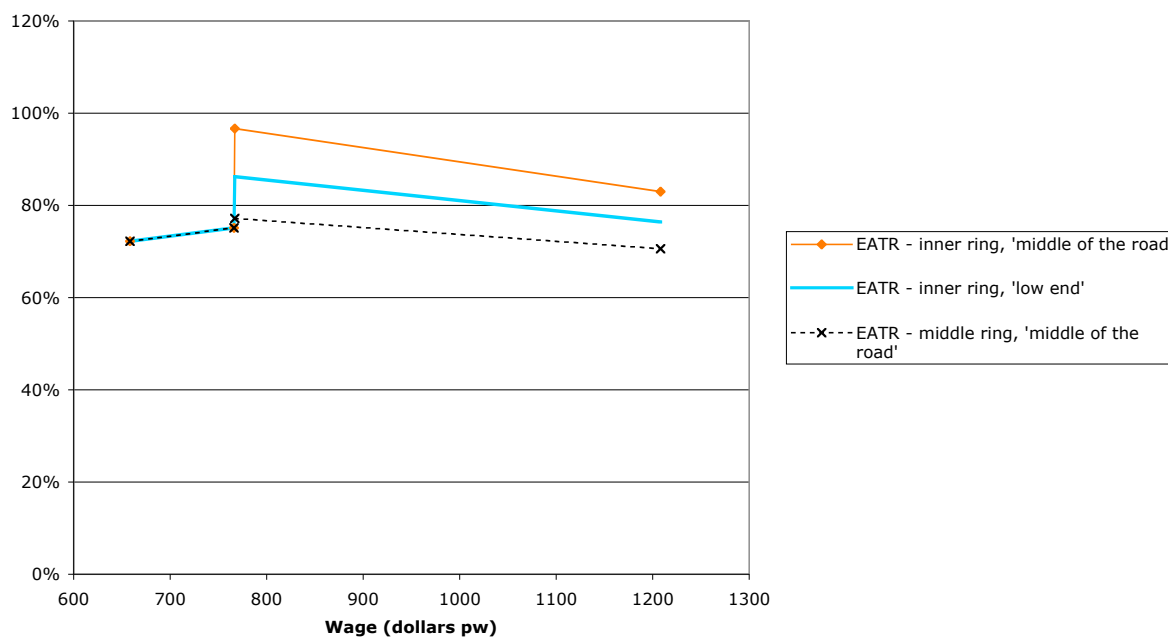


If Melanie is only just ineligible for public housing, and she rents a median rent property in the inner ring suburbs, her disposable income drops \$165.28 pw – even after taking into account her Rent Assistance. At this her disposable income is only \$25.16 more than if she was unemployed. She will have to get job paying almost \$1 200 pw before she is in front of the disposable income she would have had if she remained in public housing at the top eligible wage. If Melanie takes a job paying

\$1 200 pw and pays the median rent in the inner suburbs of Sydney, her disposable income will be a mere \$14.49 higher than if she was employed at \$766.19 pw and remained in public housing, and only \$205.01 higher than if she was not employed at all. If she rents a 'low end' property in the inner ring, Melanie loses \$85.28 pw; in the middle ring, at the median rent, she loses \$15.28 pw.

Figure 2.2.2 shows, in terms of EATRs, how much of Melanie's wage is lost as she moves into private rental housing.

Figure 2.2.2. Melanie - EATRs as a private tenant



The rates for the inner ring would be high if they were marginal rates; as the effective tax rate applied to *every* dollar Melanie earns, they are extraordinarily high. At the top wage considered, the EATRs for the inner ring (76 per cent and 83 per cent) are higher than that which applied at the top wage at which Melanie was still eligible for public housing (72 per cent); the EATR for the middle ring (71 per cent) is only slightly lower.

Comparing figures 2.2.1 and 2.2.2 with the relevant figures for Louis, it will be noted that not only does Melanie's inner ring disposable income drop further, but also her disposable income and EATRs generally improve more slowly than Louis's. This is because throughout this range of wages Melanie's FTBA, even though supplemented by Rent Assistance, continues to be withdrawn at 20 cents in the dollar.

In other words, there is a two-fold problem with the eligibility threshold for Melanie: first, the wage at which Melanie becomes ineligible for public housing under the RPH reforms is too low for her to rent most properties in the inner ring of Sydney without significantly cutting her disposal income; second, Melanie loses eligibility for public housing and faces higher private rents at the same time as a significant source of her income is being withdrawn.

Alternatively, Melanie might look for premises for which the rent is not more than 30 per cent of her income. The following considers the locational constraints on her

search for affordable housing. Table 2.2.1 shows which areas have median rents that are affordable only at incomes higher than \$978.12 pw, and how much higher than that amount Melanie would have to receive in order to access affordable rental housing.

Table 2.2.1. Melanie – locations constrained by affordable median rents

Location	Income required for an affordable 'middle of the road' house	Gap between threshold income and required income
Canterbury	999	20.88
Tweed Heads	999	20.88
Baulkham Hills	1032.30	54.18
Hurstville	1065.60	87.48
Strathfield	1065.60	87.48
Rockdale	1098.90	120.78
Kogarah	1132.20	154.08
Hornsby	1165.50	187.38
Sutherland	1165.50	187.38
Ashfield	1198.80	220.68
Marrickville	1198.80	220.68
Ryde	1215.45	237.33
Botany Bay	1265.40	287.28
Burwood	1265.40	287.28
Canada Bay	1332	353.88
South Sydney	1431.90	453.78
Leichhardt	1531.80	553.68
Warringah	1590.10	611.96
Ku-ring-gai	1598.40	620.28
Lane Cove	1648.35	670.23
Randwick	1665	686.88
Willoughby	1665	686.88
Pittwater	1731.60	753.48

Waverley	1906.43	928.31
Manly	2022.96	1044.86
Sydney	2114.55	1136.43
Woollahra	2164.50	1186.38
Mosman	2297.70	1319.58
North Sydney	2297.70	1319.58

As Table 2.2.2 shows, Melanie cannot afford even the first quartile or 'low end' rent in many areas – more areas than Louis – unless she receives considerably more than the amount she receives when she is just ineligible.

Table 2.2.2. Melanie – locations constrained by affordable 'low end' rents

Location	Income required for an affordable 'low end' house	Gap between threshold income and required income
Kogarah	986.68	8.56
Hurstville	999	20.88
Rockdale	999	20.88
Sutherland	1061.61	83.48
Botany Bay	1065.60	87.48
Hornsby	1065.60	87.48
Marrickville	1086.58	108.46
Ryde	1098.90	120.78
Ashfield	1119.88	141.76
Burwood	1157.18	179.06
Canada Bay	1165.50	187.38
South Sydney	1273.73	295.61
Ku-ring-gai	1332	353.88
Randwick	1365.30	387.18
Leichhardt	1373.63	395.51
Warringah	1444.55	466.43
Willoughby	1465.20	487.08

Pittwater	1465.20	487.08
Lane Cove	1473.53	495.41
Waverley	1739.93	761.81
North Sydney	1823.18	845.06
Woollahra	1831.50	853.38
Manly	1831.50	853.38
Mosman	1964.70	986.58

Melanie's Rent Assistance adds a twist to this analysis. At the beginning of this part it was pointed out that moving from public housing premises to like premises in the private market may result in a cost to the tenant where the market rent is high, but may not result in a benefit where the market rent is low, because they were probably paying market rent in public housing. Melanie's case demonstrates an exception to this. If Melanie moves to 'like premises' – specifically, a 'middle of the road' property – in the outer ring suburbs or elsewhere in New South Wales, she might come out ahead because of Rent Assistance. Melanie will also come out ahead if she finds a middle ring 'low end' property. Essentially, for tenants in these areas who are in receipt of a wage that renders them ineligible to continue in public housing, but who are eligible for a qualifying Centrelink payment, Rent Assistance may deliver a greater financial benefit than their (much reduced) rent rebate. Note, though, that Rent Assistance is only paid where the recipient's rent is above certain thresholds. If this is to be regarded as an incentive to leave public housing, it should be regarded as a qualified one.

Summary: the structure of work disincentives for Melanie

Melanie experiences work disincentives over the range of wages at which she remains eligible for public housing and, particularly if she rents in the inner ring of suburbs, significant work disincentives persist at wages beyond the eligibility threshold. If Melanie is concerned to live in inner Sydney, she is better off on an income of \$919 and staying in public housing than receiving an income of more than \$1 200 pw and renting a 'middle of the road' or even a 'low end' house. Melanie's loss of disposable income to unaffordable private market rents in inner Sydney contributes to EATRs that are higher than those she encountered in public housing until her wage is more than \$1 200 pw.

The alternative is for Melanie to move out to the outer ring of suburbs or out of Sydney – where she may actually improve her disposable income because of Rent Assistance. Her locational choices, however, are even more constrained than Louis's, and both options should be regarded as significant work disincentives.

Conclusions

Having worked through the respective cases of Louis and Melanie, we can make a number of conclusions.

General conclusions

- The interactions between the social security system (per the Welfare to Work changes), the tax system and the housing system (per RPH) are numerous and complex, especially for single parents. This may be something of a disincentive itself.
- Contrary to the Commonwealth-State Housing Agreement, RPH contributes to increasing work disincentives.
- There are significant work disincentives at almost all wages up to the point where the top 'moderate income' rebate rate applies and where public housing eligibility is lost. It is a wide trap.
- Work disincentives persist in the range of wages above the eligibility threshold, because the incomes at which tenants become ineligible is too low for them to rent in the suburbs of the inner and middle rings of Sydney LGAs without cutting their disposable income. This makes the trap even wider.
- Though the work disincentives faced by a single person are discouraging, those experienced by a single parent are generally more discouraging.

Conclusions – work disincentives in public housing

- Work disincentives in the lower half of the range wages are largely the result of the withdrawal of Centrelink benefits, in interaction with the tax and housing systems.
- The persistence of work disincentives in the upper half of the range is largely the result of the interaction of the housing and tax systems (and, where Family Tax Benefits are paid, the reduction of FTBA). In particular, the RPH reforms are the largest contributor to these disincentives.
- At any wage between \$125 pw and the top moderate income threshold (\$688 pw), a single person is subject to an EATR between 69 per cent 77 per cent.
- At any wage between \$125 pw and that at the top moderate income threshold (\$766.19 pw), a single parent with two children is subject to an EATR between 69 per cent and 76 per cent.
- Single persons on a 'moderate income' are subject to an EMTR of 81 or 84 per cent.
- Single parents with two children on a 'moderate income' are subject to an EMTR of 72, 93 or 100 per cent.

Conclusions – work disincentives on becoming ineligible for public housing

- Losing public housing at the second moderate income threshold is a significant work disincentive. On losing public housing, people face the loss of disposable income resulting from living in particular areas, or locational constraints when looking for affordable private rental housing.
- Single persons who move out of public housing to a 'middle of the road' one-bedroom flat in the inner ring suburbs face a cut in their disposable income of up to \$92.92.
- Single parents who move out of public housing to a 'middle of the road' three-bedroom house in the inner ring suburbs face a cut in their disposable income of up to \$165.28 pw.
- Single persons moving into the private rental market (inner and middle Sydney) encounter lower EATRs only when their wage is more than \$800 pw.
- Single parents moving into the private rental market (inner Sydney) encounter lower EATRs only when their wage is more than \$1 200 pw.

The respective cases of Louis and Melanie are not encouraging for those future public housing tenants who will be subject to the Welfare to Work changes and RPH. Public housing tenants will, if they want to remain in public housing, be limited to a range of jobs pay little financial reward: most cases, more than 70 per cent of their wage is lost. Getting a job paying more will mean moving out of public housing and – unless the person earns a lot more – facing significant constraints as to where they can afford to live, or costs that consume almost all of their additional income. If RPH is implemented on the terms indicated by the Government, it appears that the new 'shape' of public housing will be a wide and depressing trap of unemployment and poverty.

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Abbreviations

EATR	effective average tax rate
EMTR	effective marginal tax rate
ENA	Enhanced Newstart Allowance
FTBA	Family Tax Benefit Part A
FTBB	Family Tax Benefit Part B
LGA	local government area
pw	per week
RPH	reshaping public housing
RR	replacement ratio

Notes

1. As noted in the paper, the graphs of Louis's and Melanie's respective incomes and costs (and hence RRs, EATRs and EMTRs) turn upon a number of points: each represents an event in either the tax, social security or housing systems. These events are as follows:

Louis	Melanie
<p>At point 1, Louis is unwaged, and in receipt of ENA.</p>	<p>At point 1, Melanie is unwaged, and in receipt of ENA and Family Tax Benefit Parts A and B.</p>
<p>If Louis earns a wage past point 2 (\$30.50), his ENA is reduced at a rate of 50 cents for every dollar that amount. Past point 3 (\$125 pw), his ENA is reduced at a rate of 60 cents for every dollar over \$125.</p>	<p>If Melanie earns a wage past point 2 (\$30.50 pw), her ENA is reduced at a rate of 50 cents for every dollar over \$31. Past point 3 (\$125 pw), her ENA is reduced at a rate of 60 cents for every dollar over \$125.</p>
<p>Past point 4 (\$191.70 pw), Louis's ENA has fallen such that a portion of the tax-free threshold will thereafter apply to his wage income.</p>	<p>Past point 4 (\$219.55 pw), Melanie's ENA has fallen such that the tax-free threshold will thereafter apply to her wage income.</p>
<p>Past point 5 (187.50 pw), Louis begins to pay the Medicare levy. The levy is phased in at 20 cents in the dollars until point 6 (\$249.23 pw), after which the rate of 1.5 per cent applies.</p>	<p>Past point 5 (\$411.33 pw), Melanie becomes ineligible for ENA and the payment is withdrawn altogether.</p>
<p>Past point 7 (\$383.33 pw), Louis becomes ineligible for ENA and the payment is withdrawn altogether.</p>	<p>Past the point 6 (\$414.27 pw), Melanie's income becomes subject to a higher marginal tax rate (30 cents in the dollar).</p>
<p>Past point 8 (\$414.27 pw), Louis's income becomes subject to a higher marginal tax rate (30 cents in the dollar).</p>	<p>Past point 7 (\$556.92 pw), Melanie's income enters the range of 'moderate incomes' introduced to the rent rebate system by RPH. Melanie will pay rent at a higher rate according to a sliding scale, increasing to 30 per cent at point 10.</p>
<p>Past point 9 (\$550 pw), Louis's income enters the range of 'moderate incomes' introduced to the rent rebate system by RPH. Louis will pay rent at a higher rate according to a sliding scale, increasing to 30 per cent at point 11.</p>	<p>At point 8 (\$568.76 pw), Melanie's water charge is \$7 pw. Thereafter it remains at that amount.</p>
<p>At point 10 (\$625.89 pw), Louis's water charge is \$7 pw. Thereafter it remains at that amount.</p>	<p>Past point 9 (\$609.18 pw), Melanie begins to pay the Medicare levy. The levy is phased in at a rate of 20 cents in the dollar until point 11 (\$658.55 pw), after which the rate of 1.5 per cent applies.</p>
<p>At point 11 (\$688 pw), Louis's rent rebate rate reaches 30 per cent. Past this point, Louis becomes ineligible for public housing and his tenancy will be terminated at the end of the fixed term.</p>	<p>Past point 10 (\$639.84 pw), Melanie's Family Tax Benefit Part A is reduced by 20 cents in the dollar.</p>
	<p>At point 12 (\$766.19 pw), Melanie's rent rebate rate reaches 30 per cent. Past this point, Melanie becomes ineligible for public housing and her tenancy will be terminated at the end of the fixed term.</p>

2. A significant qualification on the calculations presented should be noted, especially in relation to considerations of the effect of the loss of eligibility for, and eviction from, public housing. Under RPH, it is proposed that reviews as to eligibility and terminations on grounds of ineligibility will occur at the end of the fixed terms of tenancies commenced after 1 July 2005. It is also proposed that the fixed terms will be for periods of up to two, five and 10 years, so the first reviews and terminations may not take place until July 2007. By that time, it is very likely that social security payment rates, tax rates, median rents and (less likely) moderate income thresholds and income eligibility thresholds will have changed. At least some of these changes (for example, increases in median rents) have the potential to make the situations of tenants worse than those presented in this paper. We believe that the calculations presented in this paper are indicative of the contours of the effects produced by future interactions between the social security, tax and housing systems, as these systems are currently set.
3. A number of assumptions are made in Melanie's case. The calculations presented are made on the basis that Melanie receives no maintenance from the father of her children, and has not had her Family Tax Benefit payments reduced because of the maintenance action test. Also, the calculations are made on the basis that Melanie has no costs in relation to child care, and does not receive Child Care Benefit.
4. The paper uses ENA payment rates based on the Newstart Allowance payment rates published by Centrelink (2006) for the period 1 January – 19 March 2006, and the taper rates for ENA published by Centrelink at 10 October 2005. ENA is proposed to commence 1 July 2006, by which time the payment rates may change from the January–March rates used here. We also assume that ENA will be treated as taxable income subject to the Beneficiary Tax Offset, as Newstart Allowance is.
5. The paper uses Family Tax Benefit payment rates and Rent Assistance rates published by the Family Assistance Office (2005) for the period 20 September 2005 – 19 March 2006. The Family Tax Benefit annual supplement is not considered in the calculations presented.
6. The paper uses the tax rates and thresholds for 2005-06, published by the Australian Tax Office. The Beneficiary Tax Offset is included in the calculations presented, but not the Low Income Tax Rebate. HECS payments are not considered in the calculations presented.
7. The paper uses rent rebate rates and thresholds, and the water charge rate and cap, published by the Department of Housing at 5 December 2005.

8. The paper uses median rent data for September quarter of 2005, from the 'Rent and Sales Report' no 73, published by the Department of Housing. The area groupings 'inner ring', 'middle ring' and 'outer ring' also come from the Rent and Sales Report, and comprise the following Local Government Areas:

Inner ring	Middle ring	Outer ring
Ashfield	Auburn	Baulkham Hills
Botany Bay	Bankstown	Blacktown
Lane Cove	Burwood	Blue Mountains
Leichhardt	Canterbury	Camden
Marrickville	Canada Bay	Campbelltown
Mosman	Hunters Hill	Fairfield
North Sydney	Hurstville	Gosford
Randwick	Kogarah	Hawkesbury
South Sydney	Ku-ring-gai	Holroyd
Sydney	Manly	Hornsby
Waverley	Parramatta	Liverpool
Woollahra	Rockdale	Penrith
	Ryde	Pittwater
	Strathfield	Sutherland
	Willoughby	Warringah
		Wollondilly
		Wyong