RIGHT TO BUY AND ONE-FOR-ONE REPLACEMENT: INFORMATION FOR LOCAL AUTHORITIES ON HOW THE "LOCAL WITH AGREEMENT" DELIVERY MODEL WILL WORK

The following information - and supporting draft technical agreement - is being issued for short informal consultation. **Comments are invited by Friday 20 April to housingassets_consultation @communities.gsi.gov.uk**. Copies of the final agreement and supporting guidance will be issued by Friday 4 May to all stock holding authorities, for return by 22 June. Final agreements, signed by the Secretary of State, will be returned to authorities by 29 June.

1. On 12 March 2012 Ministers announced that the cap on Right to Buy discounts would be raised to £75,000, and that receipts from the additional sales this would generate would be used to fund replacement stock on a one-for-one basis. At the same time Ministers announced that their favoured option of delivering these new homes would be through local authorities retaining receipts to spend in their areas.

2. In order for your authority to keep these additional receipts it will be necessary for it to enter into an agreement with the Secretary of State for Communities and Local Government.

3. This paper seeks to give a simple overview of how such agreements will work. As such it is not a substitute for the agreements themselves nor the more detailed guidance we will be providing to your finance officers.

4. The agreements will be made under powers provided by section 11(6) of the Local Government Act 2003 (as inserted by section 174 of the Localism Act 2011).

5. In short the Secretary of State will agree to
   i. allow your authority to retain additional Right to Buy receipts to fund the provision of replacement stock, and
   ii. allow your authority two years (from commencement of the agreement) to invest those receipts before asking for the money to be returned.

6. It is worth emphasising that the agreement will not require a local authority to complete the building of any home within two years. All that is required is that the local authority should have incurred expenditure sufficient that Right to Buy receipts form no more than 30% of it.

7. In return your authority will agree
   i. that Right to Buy receipts will not make up more than 30% of total spend on replacement stock, and
   ii. to return any used receipts to the Secretary of State with interest.

<u>The process</u>

8. Our main aim is to make the process as light touch as possible with minimal inspection or interference in your business activities. The agreements are concerned therefore solely with the flow of money in from receipts and out in investment in replacement stock.

9. Under the capital finance regulations that came into effect on 31st March 2012 your authority will (having deducted certain permissible amounts) have to surrender Right to Buy receipts to the Secretary of State. This sum will comprise two elements:
   i. HM Treasury's share (i.e. the funding HM Treasury was expecting to receive had the policy on Right to Buy not changed) and
   ii. funds available to invest in replacement stock (if receipts are sufficiently high).

10. However the Secretary of State is willing to enter into agreements with those local authorities wishing to invest in replacement stock to retain receipts above HM Treasury's share.

11. It will be entirely the decision of your authority whether to enter into such agreements and entirely its decision as to how much of the surplus receipt it retains.

12. Should your authority not wish to enter into an agreement then any surplus receipts arising in your area will be surrendered to the Secretary of State and passed to the Homes and Communities Agency (or, in London, the Greater London Authority) for them to invest in replacement stock.

13. As set out above, the only condition in the agreement will be that the retained Right to Buy receipts must not constitute more than 30% of the total amount invested in replacement stock (which could mean newly built council homes, newly acquired council homes (i.e. existing homes bought on the open market) or social housing provided through local authority grants to housing associations).

14. The 30% cap is necessary to ensure that we get maximum value for money from the Right to Buy receipts and enable the building of as many new homes as possible (indeed, more than one-for-one if that is feasible). Your authority (or the housing association you are grant funding) will be expected to fund the remaining 70% from its own reserves or through borrowing serviced by the anticipated rental income from the new homes built. To maximise borrowing it may be necessary to charge an Affordable Rent (i.e. up to 80% of market rent), but, in the case of new council homes, that is a decision for your authority.

15. We have considered historic data, which confirms that 30% is realistic and achievable.

16. Where retained receipts exceed 30%, then your authority will agree to return the additional receipt (i.e. the receipt above 30%) to the Secretary of State with interest.

How will this work?

17. Taking into account advice from the Homes and Communities Agency, we consider that two years is sufficient time to develop proposals and invest in replacement / new stock. (As set out above, the agreement will not require a local authority to complete the building of any home within two years. All that is required is that the local authority should have incurred expenditure sufficient that Right to Buy receipts form no more than 30% of it.)

18. Each financial quarter your authority will report to the Department the cumulative sum it has *retained* for replacement stock and the cumulative amount it has *spent* on replacement stock.

19. There will be no requirement to return receipts in the first two years of the agreement, but in Quarter 1 of 2014/15 [1] your authority will have to compare
    - the total amount spent on replacement stock from the start of the agreement to the end of that quarter, with
    - the total amount it has retained from Right to Buy receipts in Quarter 1 of 2012/13 (i.e. receipts it has had two years to spend).

    Where the latter is 30% or less than the former then no further action is necessary.

20. In Quarter 2 of 2014/15 the comparison will be between the total spent on replacement stock since the agreement began with the total it retained in Quarters 1 and 2 in 2012/13. And so forth for each subsequent quarter.

Grants to Housing Associations

21. Your authority may choose not to build itself, but instead to grant fund another body. Where this is the case, we would encourage your authority not to pay grant until scheme completion. This will mean that your authority will be able to demonstrate clearly to your auditors your contribution (and the contribution of other public bodies) did not constitute more than 30% of total scheme costs.

Returning receipts to the Secretary of State

22. Where in Quarter 1 of 2014/15 retained receipts in Quarter 1 of 2012/13 are more than 30% of total spend then the surplus (i.e. the amount above 30%) must be surrendered to the Secretary of State. Your authority's retained amount for Quarter 1 of 2012/13 will be reduced by the amount surrendered and interest calculated back to that Quarter.

[1] This example assumes the agreement began in Quarter 1 of 2012/13

23. Any surplus identified in Quarter 2 of 2014/15 will result in Quarter 2 of 2012/13 being reduced and interest calculated back to that Quarter. And so on.

24. A worked example Is attached at Annex 1

The early return of receipts

25. Your authority will be free to make payments to the Department whenever it wishes. In so doing it will identify the Quarter it wishes to adjust and interest will be calculated back to that Quarter.

26. This will be useful where your authority may recognise that it will be compelled to return receipts after two years and so wish to reduce the amount of interest it must pay by paying it back early.

27. Returned receipts will be given to the Homes and Communities Agency or the Greater London Authority (as appropriate) for investment into Affordable Rented Housing. Further detail on how the allocation process will work will follow (which could be to local authorities that have entered into these agreements too).

Interest

28. We will charge interest at 4% above the base rate on a day to day basis compounded with three-monthly rests: i.e. at the end of each three monthly period interest will start to accrue interest.

29. We have set a rate of interest deliberately, we hope, high enough to encourage local authorities to invest more in replacement stock. The rate is specifically designed to discourage local authorities from retaining receipts until such time that they are required to surrender them. The means to avoid paying interest will be in your control and it should therefore be possible to avoid having to pay interest at all.

30. It is our intention that any interest returned to the Department will be used to support the provision of new affordable rented homes.

Terminating Agreements

31. The Secretary of State can terminate an agreement at any time, but would expect to do so only in extreme circumstances (for example, where there was absolutely no evidence that a local authority was commencing activity). The effect of termination would mean that your authority could, from that point, no longer retain any receipts but would still have the two years from the start of the agreement to invest the receipts it had already retained (or have to return them).

32. Equally your authority can terminate an agreement either by voluntarily returning all future receipts (and paying back what it had already retained) or by requesting the Secretary of State to terminate as set out above.

Entering into Agreements

33. It is our intention, following a short informal period of consultation, by 4th May to invite local authorities to enter into agreements with us, with a deadline for their return to the Department of 22nd June. This will enable us to send signed copies back to local authorities by 29th June.

34. You will wish to note that local authorities that enter agreements after Quarter 1 in 2012/13 will not be able to claim back receipts already surrendered. Similarly where a local authority decides in any quarter not to retain the full amount, but instead decides to return some or all of it, it cannot subsequently claim that money back.

35. This is because the receipts will already have been allocated to the Homes and Communities Agency or Greater London Authority as appropriate for investment.

36. If you have any questions on this paper please e-mail us at the Department for Communities and Local Government at housingassets_consultation@communities.gsi.gov.uk.

April 2012
Department for Communities and Local Government

Annex 1

Any Town District Council (ATDC) keeps Right to Buy (RtB) receipts and spends money on new social housing as following

		Receipts (£k) (Cumulative totals in brackets)	Spend (£k)
2012/13	Quarter 1	100 (100)	0 (0)
	Quarter 2	100 (200)	0 (0)
	Quarter 3	100 (300)	50 (50)
	Quarter 4	100 (400)	100 (150)
2013/14	Quarter 1	100 (500)	100 (250)
	Quarter 2	100 (600)	100 (350)
	Quarter 3	0 (600)	50 (400)
	Quarter 4	0 (600)	50 (450)
2014/15	Quarter 1	0 (600)	50 (500)
	Quarter 2	0 (600)	50 (550)
	Quarter 3	0 (600)	50 (600)

After two years of the Agreement ATDC must compare the amount it has spent on social housing since the Agreement began with the amount it had retained two years earlier to determine whether it owes anything to the Secretary of State.

In this example this calculation happens first at the end of Quarter 1 of 2014/15.

To understand how the process works we need to define certain terms

> "**the reckonable quarter**" means the quarter 8 quarters prior to the relevant quarter;
>
> "**quarter 1**" means the quarter in which the commencement date falls;
>
> **A** is the total of the retained amounts for all quarters from quarter 1 to the reckonable quarter;
>
> "**the total amount spent on the provision of social housing**" is the amount spent on the provision of social housing from quarter 1 to the last day of the relevant quarter;
>
> **R** is the total of the amounts returned to the Secretary of State for all the quarters from quarter 1 to the reckonable quarter.

Quarter 1 of 2014/15

In Quarter 1 of 2014/15

“**the reckonable quarter**” is Quarter 1 of 2012/13;

“**quarter 1**” is, also, Quarter 1 of 2012/ 13;

A is £100k;

“**the total amount spent on the provision of social housing**” is £500k;

R is 0.

30% of £500k (the total amount spent on the provision of social housing) is £150k. This is more than £100k (A) less £0 (R), which means ATDC has complied with the conditions of the Agreement and no payments are due to the Secretary of State.

<u>Quarter 2 of 2014/15</u>

At the end of Quarter 2 of 2014/15 ATDC must again consider whether it needs to pay anything back to the Secretary of State.

In this quarter….

“**the reckonable quarter**” is Quarter 2 of 2012/13;

“**quarter 1**” remains Quarter 1 of 2012/ 13;

A is £200k;

“**the total amount spent on the provision of social housing**” is £550k;

R is 0.

The **reckonable retained amount** in this case is A (£200k) less R (£0k), which is **£**200k.

30% of £550k (the reckonable amount spent on the provision of social housing) is £165k. This is less than £200k (the reckonable retained amount), which means ATDC has not complied with the conditions of the Agreement and must pay the Secretary of State the difference: i.e. £35k.

ATDC will not only have to pay £35k, but also interest on that amount (4% above the base rate calculated back to Quarter 2 of 2012/13 compounded with three monthly breaks).

(However, ATDC could avoid having to pay the Secretary of State anything (and avoid interest) by buying a flat or house on the open market for £117k (of which £35k is 30%.)

Quarter 3 of 2014/15

In this quarter….

> “**the reckonable quarter**” is Quarter 3 of 2012/13;
>
> “**quarter 1**” remains Quarter 1 of 2012/ 13;
>
> **A** is £300k;
>
> “**the total amount spent on the provision of social housing**” is £600k;
>
> **R** is £35k (the amount they had to return last quarter).

The **reckonable retained amount** in this case is A (£300k) less R (£35k), which is £265k.

30% of £600k (the total amount spent on the provision of social housing) is £180k. This is less than £265k (the reckonable retained amount), which means ATDC has again not complied with the conditions of the Agreement and must again pay the Secretary of State the difference: i.e. £85k.

Again interest will be charged.