Submission to the CLG Select Committee Inquiry into the proposed extension of the Right to Buy to housing association tenants

1. ARCH represents councils in England and Wales which have chosen to retain ownership of council housing. 162 English councils (exactly half the total number of housing authorities) own 1.6 million dwellings which are home to over 4 million people. Eleven Welsh councils own a further 88,000 homes. Our submission to the Committee focuses on the lessons to be drawn from the experience of Right to Buy for local authority tenants, and the proposal to force councils to sell homes in high value areas to help fund the extension of Right to Buy to housing association tenants.

Key points

2. ARCH recognizes that the Conservative government was elected on a manifesto pledge to extend the Right to Buy to housing association tenants but argues that the proposal to fund this policy by forcing council to sell homes in high value areas is both unfair and ill-conceived. It is contrary to the principles of localism and the self-financing settlement entered into in good faith by local government in 2012.

3. Councils have never received government funding towards the cost of providing discounts to council tenants exercising their Right to Buy; the financial impact has in effect been borne by the remaining tenants who do not wish, or cannot afford, to exercise the Right to Buy. It is doubly unfair that councils and their tenants should be asked to help fund the payment of discounts to housing association tenants or the construction of replacement homes.

4. ARCH has conducted a survey among councils to assess the likely impact of the proposal to force sale of council homes in high value areas published with the Conservative manifesto. On the basis of the survey results and other evidence, we believe this proposal would be unlikely to raise more than £1.5 billion a year, a third of the claimed £4.5 billion.

5. Local one-for-one replacement of the homes councils are forced to sell, as promised in the Conservative manifesto, should be the first call on the sales receipt. Provided this promise is honoured, ARCH believes the net receipts available to support extension of the Right to Buy to housing associations will be too small to justify the forced sales policy. ARCH urges the government to look elsewhere for the finance needed to support the extension of the Right to Buy to housing association tenants.

The Right to Buy for council tenants

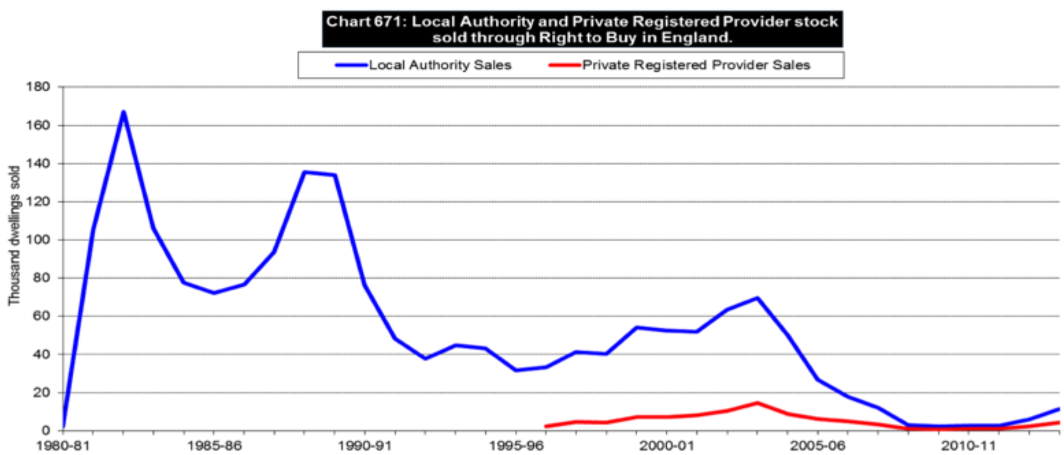
6. The Right to Buy for local authority tenants was introduced by the Housing Act 1980. Originally, tenants qualified for the Right to Buy after three years tenancy, and received a discount of 33% on the market price, plus 1% for each additional year's tenancy, up to a maximum of 50%. The discounts were later increased by the Housing and Planning Act 1986. For houses, the maximum discount was increased from 50% to 60%. Higher discounts were introduced for flats, starting at 45% after three years' tenancy and increasing by 2% a year up to a maximum of 70%.

7. The Housing Act 2004 increased the qualifying period from 3 to 5 years' tenancy, but, in compensation, increased the starting discounts to 35% for houses and 50% for flats. It also introduced caps on the maximum discount set at different levels reflecting the housing stress in different areas. These varied from £16,000 in Wales and parts of the South East to £38,000 in the rest of the South East.

8. From 2011 on, successive steps were taken by the Coalition Government to re-invigorate the Right to Buy for council tenants in England:

- From 2 April 2012, regional discount caps were replaced by a single national limit of £75,000.
- From 25 March 2013 the maximum discount in London was increased to £100,000.
- In January 2014, the government announced its intention to increase the maximum discount annually in line with increases in the Consumer Prices Index.
- From 21 July 2014 to 5 April 2015, the maximum discounts were increased to £102,700 in London and £77,000 in the rest of England.
- Maximum discount on houses increased to 70%.
- From 5 April 2015 the maximum discounts were increased to £103,900 in London and £77,900 in the rest of England.

9. The chart below shows take up of the Right to Buy since its introduction[i].



10. It shows a sharp peak in sales shortly after the scheme was introduced, followed by a second peak in the late 1980s following the introduction of higher discounts for flats. Sales then fell to a lower level probably reflecting problems in the wider housing market and economy during the early 1990s. A slow increase can be seen from the late 1990s, reversed from 2004, probably because of the introduction of the regional caps on discounts. Since "reinvigoration", sales in England have increased significantly compared with pre-2011 levels, but, at 12,000 in 2014/15, are still well below the volume of sales achieved in the early years of the scheme.

11. In Wales, the maximum Right to Buy discount of £16,000, in force since 2003, was reduced to £8000 from 14 July 2015. Local authorities where there is high pressure on housing can apply for a suspension of the Right to Buy for up to five years. The Welsh Government is planning to bring forward primary legislation to end the Right to Buy altogether.[ii]

Implications for take up of Right to Buy by housing association tenants

12. It seems likely that extension of the scheme to housing association tenants will lead to an initial surge in take up, as with the local authority scheme. Right to Buy sales in the first five years of the scheme totaled around 10% of the stock. However, there are significant differences between the two cases which pull in opposite directions. The discounts available to local authority tenants in the first five years of Right to Buy were substantially less generous than those which are available now, as described above. Conversely, around half of local authority tenant household heads were employed at that time, compared with around a third of housing association tenant household heads today. A further factor is the impact of the proposed Pay to Stay scheme, announced in the Summer Budget, which will require tenant households with incomes over £30,000 (£40,000 in London) to pay a market or near-market rent if they choose not to buy.

Financial arrangements for local authority Right to Buy

13. The financial arrangements for local authority Right to Buy have been quite different from those which seem likely to be proposed for housing associations. Until April 2012, councils were subject to a housing revenue account subsidy system based on annual payments of subsidy to the council, or for a growing number of councils from 1990 onwards, from the council to the government. Subsidy payable was calculated according to a formula which took into account notional income from rents charged in accordance with government guidelines and notional expenditure on management and maintenance and on servicing a notional amount of housing debt. If notional income was less than notional expenditure, the council received a payment of subsidy; if it was more, the council was required to pay the difference to the government.

14. The Right to Buy was nowhere explicitly recognized in the subsidy calculation. Councils were required to use 75% of the net receipts from Right to Buy sales to repay outstanding housing debt, and the sold dwellings were reflected in a lower stock number used in the income and management and maintenance calculations. Rents assumed in the subsidy calculation increased broadly in line with inflation during the 1990s, yielding a growing surplus over assumed management and maintenance costs. Together with receipts from Right to Buy sales, this was more than enough for many councils to repay all outstanding debt, beyond which point they were expected to pay surplus income over to the government. With hindsight, it is clear that the management and maintenance allowances were set too low, so that councils were being required to send money to the government that should have been used to maintain and improve the housing stock.

15. From the turn of the century, this housing subsidy system was increasingly seen by local authorities and tenants as unfair, in that a growing proportion of rent income was diverted to central government at a time when it was badly needed to help bring all council homes up to a decent standard. Annual determination of subsidy payments also left councils unable to plan for the long term for the future of the housing stock. By 2010 the case for reform was accepted by all major parties in Parliament, and, in April 2012, the housing subsidy system was abolished and replaced by a new system of housing revenue account self-financing. Based on a valuation of each council's housing stock which gave a total value of £29.2 billion to council housing in England, 136 councils took on new debt of £13 billion to make payments to the government, while 34 received government payments of £5 billion to reduce their housing debt.

16. The essence of the deal was that councils were relieved of any future need to give to or receive from government any payments of HRA subsidy in exchange for a one-off debt settlement which was designed to leave each council with a debt equal to the net present value of its housing stock, roughly equivalent to the amount the council could afford to repay over 30 years from rent income, after allowing for the costs of managing the stock and keeping it in a good state of repair over that period. In return, councils won the right to keep rent income in full and invest it as agreed with tenants and residents locally.

17. HRA self-financing was a central plank of the Coalition Government's commitment to localism. It was warmly welcomed by councils and tenants as opening a new era for council housing in which councils would have a secure basis from which to plan long-term, including the opportunity to build new homes on a significant scale for the first time in three decades.

One-for-one replacement

18. Replacement of homes sold under the Right to Buy was not a government policy objective before 2011. However, the then government's proposals to reinvigorate the Right to Buy included a commitment that the additional homes sold as a result of the increased discounts available from April 2012 would be replaced one-for-one, not necessarily in every local authority area, but nationally in total. Councils were given the opportunity to use RTB receipts to help finance replacement homes provided they were spent within three years of receipt. RTB receipts could be used to fund up to 30% of expenditure on new dwellings, but not in conjunction with other receipts or grants totaling above 30% of expenditure. The remaining 70% is expected to be funded through borrowing, in anticipation that the new homes will be let at affordable rents of up to 80% of market rents.

19. For the purposes of self-financing, the value of local authority housing was calculated on the basis that homes would remain in rented occupation for at least 30 years. Thus the valuation was based on the net present value of the rental stream over that period less management and maintenance costs over the same period. This valuation is substantially less than the value of the stock if sold with vacant possession on the open market. Councils will shortly be required to publish an estimate of the market value of their housing stock, but as yet insufficient information has been published to inform a national estimate. As a rough indication, the market value of homes is likely to be in the same proportion to the self-financing valuation as local authority rents to market rents.

20. With local authority rents on average around 40% less than market rents, this implies that, provided the average discount to Right to Buy purchasers does not exceed roughly 40%, a council's Housing Revenue Account is not adversely affected by the sale of dwellings. If discounts are above this amount, however, receipts will be insufficient to fully compensate for the future loss of rent income from the sold dwellings, leaving the remaining tenants to bear an increasing share of costs.

21. Many ARCH members have reported difficulties in achieving one-for-one replacement of homes sold under the reinvigorated Right to Buy. The reasons are clear. With the average discount on recent Right to Buy sales exceeding 50%, the net receipt is usually insufficient, once administration costs and the outstanding debt on the property have been paid, to meet 30% of the costs of a replacement home, particularly in areas where the market value of council dwellings is less than the cost of building new ones. Even where councils can fund 30% of the

cost of a replacement, they may have difficulties borrowing the remaining 70% within the debt caps imposed as part of the self-financing settlement.

The new government's policies for council housing

22. This submission is primarily concerned with the proposal to require councils to sell homes in high-value areas to help meet the costs of extending the Right to Buy to housing association tenants. However, this policy should be seen in the context of the other policies for council housing announced in the summer Budget. These were the proposals:

    - to cut local authority and housing association rents by 1% a year for the next four years, now included in the Welfare Reform and Work Bill currently before Parliament;
    - for a compulsory Pay-to-Stay scheme which would require local authority and housing association tenants with household incomes above £30,000 (£40,000 in London) to pay market or near-market rents. Local authorities will be required to pay the additional rent recovered to central government while housing associations will be able to invest it in new housing;
    - for a review of the use of lifetime tenancies in social housing.

23. Taken together these proposals mark a fundamental departure from the principles underlying the self-financing settlement made little over three years ago. The proposal to cut rents seriously undermines the financial basis of the settlement, which had already been eroded in 2013 by the move from RPI to CPI as the basis for rent setting and the abandonment of convergence to target rents – both of which had been assumed in the self-financing debt calculation. It will result in a loss of over £2.4 billion in rent income over the next four years, and an additional £30 billion over the remaining years of the 30 year business plan assumed in the settlement. It is likely to put an end to councils' capacity to build new homes except where contracts have already been let or new homes are funded as part of wider regeneration schemes. In some areas it may also jeopardise planned improvements to the existing stock promised to tenants as part of the 30-year business plan.

24. Compulsory Pay to Stay and the forced sales of homes mark the abandonment of localism and a return to a Treasury-led approach that sees council housing as an asset to be utilised in pursuit of central government policy and the rents paid by council tenants as an income stream to be used to support general government expenditure. Council tenants are already taxpayers; it is now proposed they will pay twice – through their rents as well as taxes – for the services provided by central government.

Forced sale of council homes in high value areas

25. Council tenants have been expected to meet much of the financial impact of Right to Buy on council housing revenue accounts, as shown above. It is particularly unfair that, through the forced sale of council homes, they should now be expected to help fund its extension to housing association tenants.

26. Although the government has confirmed that measures to extend the Right to Buy to housing association tenants and force councils to sell high-value homes will be included in a Housing Bill to be introduced this Autumn, the only details of the proposals published to date are those

included in the Conservative manifesto and an accompanying press briefing issued on the day it was launched. The Conservative manifesto promised to give housing association tenants the Right to Buy and "fund the replacement of properties sold … by requiring local authorities to manage their housing assets more efficiently with the most expensive properties sold off and replaced as they become vacant"[iii].

27. The Press Briefing[iv] provides more detail:

> *"A Conservative Government will legislate to require local authorities to manage their housing assets more efficiently, by selling off expensive properties – only when they become vacant – which will then be replaced with normal affordable housing. Local authority properties which rank among the most expensive third of all properties of that type in their area – including private housing – will be sold off and replaced with new affordable housing on a one-for-one basis. But this will only happen as they become vacant."*

28. In a separate section proposing the creation of a Brownfield Regeneration Fund, the Briefing states that replacement local authority homes would be "in the same area" as those they replace.

29. The Briefing then provides a table setting out price thresholds by dwelling size for each of the English regions. Councils would be expected to sell homes worth more than these thresholds.

30. The Briefing states that in total there are over 210,000 local authority properties which meet these criteria. This is described as representing 5.2% of all affordable housing in England; it accounts for 12.4% of the local authority stock. 15,000 of these are claimed to fall vacant each year, and their sale would be expected to raise £4.5 billion a year – an average of £300,000 each – which would be used to pay off outstanding debt on the sold homes, replace sold stock with new affordable housing on a one-for-one basis, extend the Right to Buy and creating the Brownfield Regeneration Fund.

31. Several of the assumptions underlying these calculations are questionable, and in ARCH's view it is likely that a policy along the proposed lines would yield only around a third of the claimed £4.5 billion.

32. The source of the estimate that there are over 210,000 "expensive" local authority properties is not given. The most likely source is that used in a Policy Exchange report published in 2012[v] proposing a similar policy of forced sales (that would, however, have applied to housing association as well as council housing), which was based on English Housing Survey data on the market value of homes collected in 2008/9 and not repeated since. In June 2015, Savills published a Housing Market note which revisited this survey data[vi]. This shows that approximately 10% of local authority housing in England is above the 70th percentile value for all housing, a finding consistent with 12.5% being above the 67th percentile, as the Conservative Briefing asserts. However, it is clear from further analysis that this is very largely accounted for by house price variation among areas, not by the fact that some council houses are among the most expensive third of homes (public and private) in their local authority area. Thus Savills find that the proportion of local authority housing above the 70th percentile varies widely across the country, from none in the East Midlands to 14% in London, as one would expect given general house price levels in London compared with other regions.

33. It is therefore not accurate to describe the policy as a proposal to force councils to sell their most expensive homes. This would imply that the policy is intended to apply to excessively spacious or luxurious homes, perhaps Georgian terraces or Victorian villas acquired under municipalisation programmes in the 1970s and retained by councils to meet local housing needs. However, a tiny fraction of council homes are valued in the top third of house prices in the immediate area in which they are located. Where such homes exist, councils are already selling and replacing them as part of a strategic asset management plans. These are not representative of the great majority of the homes that would be affected by the policy, which are only "expensive" compared with the price of homes in cheaper areas. In reality the effect of the government's proposal is to force sale of council housing in the most expensive areas. The great majority of the homes that would be affected, on current plans, are ordinary council homes – modest houses and flats – distinguished from similar council housing elsewhere only by the fact that they are located in an area where house prices are relatively high. A further implication is that the impact of the policy would be concentrated in a small minority of councils.

34. Having noted that 10% of council homes are above the 70th percentile value for all housing in England, the Savills note goes on to model the introduction of the regional value thresholds proposed in the Conservative briefing. This has the effect of reducing the number of homes above threshold to 78,000, a third of the Conservative manifesto estimate. The estimated proportion of homes affected in each local authority area is shown in a map, which brings out a further feature of the proposed policy. The extent to which councils are affected by the proposals depends not on the absolute level of house prices in their area compared with others in the region, but on the degree of dispersion of house prices across the region. Thus in London, the map shows that in several Inner London boroughs over half the stock is worth more than the London thresholds, while most Outer London boroughs would not be expected to sell any of their stock. This reflects the wide variation between house prices in Central and Outer London. In the South West region, in contrast, there is less variation between house prices in different parts of the region and the Savills analysis suggests that no local authority would be affected by the forced sales policy as currently proposed.

35. A further implication of the proposed regional thresholds is that local authorities on the fringes of higher value regions – in particular those just outside London – are likely to be particularly affected. Thus Epping Forest estimates that it would be required to sell over 30% of homes becoming vacant because it is included in the East region where the price thresholds are little over half those for London, while neighbouring Enfield, where prices are no lower, would be required to sell a handful of homes, if any, because London thresholds apply.

36. The Conservative manifesto estimate that 15,000 homes would become available for sale each year also depends on the assumption of an annual vacancy rate of over 7% a year. While this reflects the average void rate for local authority housing across England as a whole, it fails to take account of regional variation, which ranges from 10% in the North to 4.5% in London, and will tend to be lower in the areas most affected by the policy. These are predominantly areas of high housing demand and stress where alternative housing opportunities are limited. It is also reasonable to expect that properties in the higher value areas are more popular and likely to become vacant less often than others in the same local authority.

37. ARCH has surveyed all stock-owning councils in England asking them to review the properties that became vacant in 2014/15 and confirm the number of these properties that would be worth more than the proposed thresholds, and the total receipt that would be realized from their sale.

Based on returns from 55 authorities, it is clear that the impact of the policy is extremely variable, as would be expected from the Savills analysis summarized above. The majority of responding authorities expected to be unaffected or hardly affected by the price thresholds proposed; a minority, however, would be heavily affected, several being forced to sell 30% or more of stock becoming vacant. However, all estimates of the number of such properties becoming vacant each year were well below the 7% assumed in the Conservative briefing, with an average of around 3.5%. Based on these returns, ARCH would estimate that introduction of the policy as proposed would be unlikely to yield more than £1.5 billion a year.

38. On any reasonable assumption, the first call on this diminished pool of receipts should be the replacement of the local authority dwellings. It would be wholly unfair and inequitable for any government to fund the sale and replacement of housing association homes by selling council homes and not replacing them.

39. The Conservative manifesto committed to one-for-one replacement of sold council homes "in the same area". It is essential that this commitment is met if councils affected are not to permanently lose the capacity to meet their statutory housing duties. However, replacement in the same local authority area will be precluded – except in a tiny fraction of cases where land values vary widely within the same local authority area – by the fact that the cost of constructing replacement homes on a like-for-like basis will be near to or greater than the value of the homes they replace, yielding no surplus or one too small to justify the exercise. The Policy Exchange report, mentioned above, which first suggested a forced sales policy, claimed that all high value homes sold could be replaced in cheaper areas no more than 30 miles away. But this is not what any normal person would understand by "in the same area".

40. Even where sale and provision of a replacement home not too far away could be expected to yield a significant net surplus, the impact of the lag between sale and the provision of a replacement home should be taken into account. Current rules on replacement of homes sold under the reinvigorated Right to Buy allow for a three-year lag between sale and replacement. Applying the same assumption to forced sales would imply that if, as in the Conservative estimate, 15,000 homes were sold each year, there would be a permanent loss of 45,000 council lettings that would otherwise be available to house homeless households and applicants from the waiting list. These lost lettings would be concentrated in a minority of local authority areas, some of which could lose a third or more of their dwelling supply for a three year period. There would be a dramatic impact on temporary accommodation costs, and many applicants would be forced to remain in unsatisfactory housing conditions for much longer.

41. Forced sale of stock would also result in a significant rent loss at least until the promised replacements are provided. This will be in addition to the impact of the proposal to reduce rents by 1% a year for the next four years.

42. In the absence of any safeguards to prevent it, a significant proportion of the homes sold is likely to be purchased by private landlords rather than home owners. Recent estimates suggest that 40% of the homes sold under Right to Buy are now privately let. Given the reduced supply of council lettings in the area, it is also likely that some of these homes would be occupied by tenants claiming housing benefit. The overall effect would be contrary to two high-priority government policies – to promote home ownership and cut welfare spending.

43. In conclusion, ARCH would argue that the forced sale of council homes to help fund extension of the Right to Buy to housing association tenants is both unfair and ill-conceived. Unfair in that it would force councils and council tenants, who have already borne the impact of financing local authority Right to Buy, to bear, in addition, part of the cost of extending the policy to housing associations. Ill-conceived, in that the proposals as advanced are unlikely to yield more than a fraction of the claimed £4.5 billion a year, or to justify the disruption of council housing services that they would imply. ARCH would argue strongly that the government should look elsewhere for the finance needed to support the extension of Right to Buy for housing associations.

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[i] https://www.gov.uk/government/statistical-data-sets/live-tables-on-social-housing-sales#right-to-buy-sales

[ii] See House of Commons Library Briefing Paper 07174 http://researchbriefings.parliament.uk/ResearchBriefing/Summary/CBP-7174

[iii] Conservative Manifesto page 51

[iv]

[v] *Ending expensive social tenancies,* Policy Exchange 2012

[vi] http://www.savills.co.uk/research_articles/141280/189182-0