Welfare Reform and Work Bill: Clauses 19 to 22 – Reduction in Social Housing Rents

ASSOCIATION OF RETAINED COUNCIL HOUSING

Submission to the Public Bill Committee by the Association of Retained Council Housing

ARCH represents councils in England and Wales that have chosen to retain ownership of council housing and manage it themselves. 162 English councils (exactly half the number of housing authorities) own over 1.6 million dwellings which are home to over four million people. 11 Welsh councils own a further 88,000 homes.

Our submission calls for the deletion of Clauses 19 to 22 of the Bill which would impose a one percent reduction in social housing rents for four years starting 2016/17. In summary, we argue that:

- It is disappointing that the government is proposing to abandon the principles of self-financing for council housing agreed, with the support of all political parties, by the last government little over three years ago as a key plank of its localism agenda, together with the ten-year commitment on social rents it made only two years ago;
- As a minimum, we would urge the government to make a new ten-year commitment on social rents to give councils and housing associations a firm basis on which to plan for the future; this commitment should include a return to rent increases at CPI + 1% after 2020;
- A one percent reduction in council rents for four years would mean that by 2020/21 councils will suffer an income loss of £2.4 billion, and a further £30 billion over the remainder of the 30 year business plan period;
- This loss cannot be accommodated through efficiency savings alone; we anticipate that 20,000 new homes that council are currently planning would not be built;
- At a time when the government is committed to increasing the volume of new housebuilding, it is counterproductive to introduce measures that will have the effect of preventing councils and housing associations from making a real contribution to this ambition; loss of new council housing supply will mean greater numbers of tenants reliant on securing accommodation at higher rents in the private rented sector reducing disposable income for those working people in lower paid employment and increasing the cost of housing benefits payable for those entitled to support under the government's wider welfare reforms;
- The proposals in clause 19 to prescribe the rents payable by individual social sector tenants undermine the coherence of national and local rent policy by locking in existing rent anomalies for a further four years.
- The proposal to cut the rent paid by council tenants earning any amount less than £30,000 a year (£40,000 in London) but to increase the rent of any tenant with a household income above these thresholds to a market or near market rent will create substantial work disincentives for tenants near these limits. We want to work with the government to develop a better scheme for linking rents to tenants' incomes that avoids these problems and which enables councils to retain and invest the additional rent collected from higher-income tenants.

Background

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 based on a formula which took into account notional income from rents charged in accordance with government guidelines and notional expenditure on management and maintenance and servicing housing debt. If notional income was less than notional expenditure, a council received a payment of subsidy; if it was more the council was required to pay the difference to the government.

After 1987, when government of the time decided that housing associations should be the main providers of new social housing, councils built few new homes and so took on relatively little new debt. Rents assumed in the subsidy calculation rose 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 most or all of outstanding debt, beyond which point they were expected to pay surplus income over to the government.

From the turn of the century, this housing subsidy system was seen by local authorities and tenants as increasingly 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 the major parties in Parliament and, in April 2012, the housing revenue account 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 that gave a total value of £29.2 billion to council housing in England, 136 councils took on new debt to make payments to the government of £13 billion, while 34 received government payments of £5 billion to reduce their housing debt.

The essence of the deal was that councils would be relieved of any future need to give to or receive from government any payments of housing subsidy in exchange for a one-off debt settlement which was intended to leave each council with a debt equal to the net present value of their 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.

HRA self-financing was a central plank of the last 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 it three decades. An ARCH-led survey of councils published in 2013 showed that councils were planning to build 5000 new homes a year over the next ten years. In 2013/14 councils started construction of 2,200 homes, more than in any year since 1992.

It is therefore deeply disappointing that the government now proposes to tear up the principles underpinning the self-financing settlement it entered into with stock retained councils little over three years ago, to impose national restrictions on council rents regardless of what may have been agreed locally between councils and tenants, and to claim for the exchequer the additional rent proposed to be collected from higher-income tenants.

Council rents since self-financing

Historically, the rents charged by different councils and housing associations for similar properties varied widely as a result of local policy and the financial arrangements under which the homes were first provided. In 2000, the Labour Government adopted a rent restructuring policy intended, over time, to eliminate systematic variation between the rents charged by different landlords for similar properties, while still allowing room for local choice. Formula rents were calculated for each property based on property values and local earnings. Each year the government set guideline rent increases that were originally intended to ensure that rents converged with target rents by 2012. In 2007, the timetable for convergence was extended to 2016/17.[i]

Formula rents were increased annually by one percent more than the Retail Prices Index; guideline rents were increased by the same amount, but with an additional allowance of up to £2 a week so long as the actual rent remained below the formula rent. This rule applied to the rents that

could be charged to existing tenants; councils could charge formula rents to new tenants irrespective of the rent previously paid for the property.

Government policy on formula and guideline rents is set out in non-statutory guidance to which local authorities must have regard; but they do not have to follow it. Section 24 of Housing Act 1985 enables councils to "make such reasonable charges as they may determine" and requires them to review rents from time to time and make any necessary changes; it is open to councils to operate local rent schemes which do not follow the principles in guidance, although few have chosen to do so. In particular, it is legal for councils to charge rents above guideline levels. However, they cannot reclaim rent rebate subsidy from the DWP in respect of housing benefit paid on the amount by which rents exceed rent limits set each year by the DWP with reference to formula rents.

In announcing the proposal to cut social housing rents, the Budget report made much of the fact that rents in the social sector had risen by 20% over the three years from 2010/11.[ii] So far as the council sector is concerned, this was directly in line with the policy just described, as the table below demonstrates.

Table 1: Council rents 2010/11 to 2014/15

Regime	Year	RPI increase (%)	Average guideline increase (RPI + ½ +£2) (%)	Average rent[iii] (£ per week)	Average actual rent increase (%)	Average HA rent[iv]
HRA subsidy system	2010/11	-1.4	3.1	67.83	2.7	£77.91
	2011/12	4.6	6.8	73.58	8.4	£78.28
Self-financing	2012/13	2.6	8.0	78.55	6.8	
	2013/14	3.2	5	82.44	5.0	

Over the four years shown, the guideline rent prescribed in government policy (including the allowance for convergence) increased by 24.8%. Although the average rent increases actually implemented by councils departed from the guideline in individual years, the actual increase over the four years taken together was exactly the same percentage – 24.8% - as the guideline increase. It should also be noted that, on average, council rents remain lower than housing association rents.

In the 2013 Budget, as part of a deal intended to give councils and housing associations certainty on rent levels for a 10-year period the government announced that, from 2015/16, the future basis for rent setting would be the Consumer Prices Index (CPI), with councils allowed to increase rents by one percent more than the annual change in CPI. There would, however, be no further allowance for convergence – not because the policy of convergence had been abandoned but because the government believed it had been substantially achieved. Because, over the next ten years, CPI was expected to rise annually by 1.4% less than RPI[v], this decision implied a significant loss of income over the 30 year business plan period. Nevertheless, councils accepted these changes and adjusted their business plans to accommodate them, including by making savings in spending on housing management and maintenance.

Impact of the 1% rent reduction

The current proposal to cut rents by one percent each year from 2016/17 to 2019/20 cannot be accommodated so easily. If they go ahead, councils will have suffered an income loss of £2.4 billion compared with previous expectations, and, even if rent setting returned to the previous basis of CPI + 1% thereafter, a further £30 billion would be lost over the remaining years of the business plan. If these changes had been anticipated in the self-financing settlement, council housing would

been valued, not at £29 billion, but at £6 billion less. Councils have a legitimate case to argue that the Government should now return this £6 billion to them.

Councils are still in the process of reviewing business plans, and identifying where further savings might be made, with the aim of protecting core services to tenants. They are looking at their spending both on management and repairs and maintenance. It is likely that some of the added value services currently provide to help tenants into work or reduce fuel poverty will have to be scaled back or cut altogether to concentrate on maintaining homes to the government's minimum Decent Homes Standard, with an adverse impact on the welfare spending the government is seeking to reduce.

Councils have already taken very significant measures to cut costs by sharing back office services and restructuring senior management, but the scope for further efficiency savings of this nature is limited. It is unrealistic to imagine, as suggested in the Budget document, that the rent loss can be accommodated through efficiency savings alone. Since management and maintenance expenditure equals only 60% of rent income, the required 12% reduction in rent income by 2020 equates to a 20% reduction in management and maintenance. There will inevitably be a severe impact on council investment plans, particularly new construction. On previous rent expectations, councils were planning to build around 5000 homes a year and with greater freedom to borrow could have built more. Many councils have already paused new build plans while they assess the impact of the government's proposals; early indications are that no more than a small fraction of planned schemes will go ahead, principally on schemes where contracts have already been let.

At a time when the government is committed to increase the overall volume of new housebuilding, and where it recognizes that a proportion of the new supply must be affordable by households on lower incomes, it counterproductive to bring forward proposals that will prevent councils, and housing associations as well, from making as effective a contribution as they could. Worse, the implication of a reduced supply of new council housing is that more low income households will be forced to rely on private rented accommodation where they will need help from housing benefit or Universal Credit to pay market rents averaging 60% more than council rents.

The government has set out its revised social rent policy to 2020, but councils need certainty for a longer period to provide a firm basis on which to plan for the future. The government recognized this fact in 2013 when it set out what was intended to be a ten-year commitment on social rents. We would urge the government to make a new 10-year commitment based on the principle that annual rent increases will return to CPI + 1% after 2020.

Proposals for implementing the rent cuts

For the reasons given above, ARCH would urge the government to reconsider its decision to impose rent cuts on councils and housing associations. However, if it decides to press on with the policy regardless, we would urge a rethink of the proposed method of implementing the cuts.

Clause 19 of the Bill proposes that the rent payable by each individual tenant of a council or housing association should be reduced by one percent from the amount payable on 8 July 2015 each year from 2016/17 to 2020/21. This would apply regardless whether the rent payable is a social rent (average 60% or market rent) or an affordable rent (up to 80% of market rent); if it is a social rent, it would apply whether the rent is at, or above or below the formula rent prescribed in Government guidance. And it would apply whether or not the tenant is in receipt of housing benefit or Universal Credit.

The only proposed exception would be tenants with household income in excess of £30,000 (£40,000 in London). The Chancellor announced in the Budget that proposals will be brought forward to require councils and housing associations to charge such tenants a market or near market rent. Taken together with the proposals in the current Bill, this implies that any tenant with a household income even the smallest amount less than £30,000 can expect to see their rent

reduced by one percent a year for the next four years, while a tenant with household income of just a few pounds more would be looking at a considerable rent increase.

There is a further issue in relation to new tenancies. Where there has been a sitting tenant, councils have been constrained by the £2 p.w. limit on individual rent increases to achieve convergence; however, on change of tenancy they have been free to re-let to the new tenant at formula rent. Clause 19 (4) as drafted appears to remove this freedom, requiring them to charge the new tenant one percent less than the rent paid by the previous tenant, even if below formula.

While we recognise that the government wishes both to reduce spending on housing benefit and the overall level of council rents, the chosen method of achieving this has the effect of locking in outstanding rent anomalies – primarily the deviation of individual rents from target rents – for a further four years. This is unnecessary. The government could better achieve its objectives by requiring councils to reduce overall rent income by a prescribed amount but allow them to decide locally how the reduction should be distributed among tenants. This would have the advantage of leaving councils free to set rents for individual properties that reflect their size, quality and location and to decide whether to apply the same percentage rent reduction, if any, to tenants payable affordable as opposed to social rents.

ARCH would also welcome the opportunity to work with government to develop a more coherent and workable scheme for linking rents to tenants' incomes, which avoids the work disincentives inherent in the cliff-edge implied by current proposals at the proposed income threshold of £30,000 (£40,000 in London). If the government proceed with its proposals to introduce a mandatory 'pay to stay' scheme alongside the proposed rent reductions we would urge that councils be allowed to retain the additional income operating such rent schemes, as housing associations will be able to, to underpin local investment.

The purpose of imposing a year on year rent reduction for social housing tenants is to deliver an estimated £1.4billion saving in the housing benefit bill as a contribution to the government's target of saving £12billion on the Welfare Bill by 2020. Social housing rents are already typically 20% to 40% below equivalent market rents and it makes no economic sense in the long term to reduce social rents still further below equivalent market rents starving the sector of much needed resources for investment in both the existing stock and in new social housing.

The government have also proposed a freeze in the Local Housing Allowance for the next four years. Accepting that the government's overriding priority is to reduce the budget deficit it would nevertheless make sense in housing policy terms, and maintain a balance between Social Housing Rents and Rents charged in the private rented sector to those in receipt of housing benefit, to impose a similar freeze in Social Housing Rents for the next four years (as opposed to the proposed a one percent rent reduction).

---

[i] The House of Commons Library Briefing Paper *Rent Setting: social housing (England)* provides a more detailed explanation of the principles and issues covered in this section.

[ii] Summer Budget 2015, paragraph 1.140

[iii] https://www.gov.uk/government/statistics/local-authority-housing-statistics-year-ending-march-2014

[iv] Ibid

[v] See *Rent-setting: social housing (England),* section 2.5