



ARCH Member Briefing: January 2009

Consultation on changes to revenue and capital rules for new council housing

Key issues:

1. Changes proposed to enable councils to retain more locally raised income.
2. Government's intention is to promote councils as affordable housing provider.
3. Retained income to be spent on affordable housing and regeneration programmes only.

1. Introduction

The current review of Council Housing Finance is looking at all aspects of the HRA finance system and will report to Ministers this year. As part of this the government have brought forward earlier consultation on proposals that councils should be able to keep all the rental income from any new homes they build.

A consultation paper has been issued titled "Changes to the revenue and capital rules for new council housing; Consultation on excluding new council housing from Housing Revenue Account Subsidy and Pooling" and a copy is available from the link below <http://www.communities.gov.uk/documents/housing/pdf/capitalruleschanges.pdf>

2. Context of the proposed changes

The role of councils as providers of new housing for rent has diminished drastically since the 1970's prior to which councils built many thousands of homes across the UK. The impact of the Right to Buy and the transfer of many council homes away from councils to registered social landlords or to arms length management organisations has reduced the stock of houses under direct council control. A number of councils have increased their own stock through building council homes in recent years, or have plans to do so, although the numbers built and planned are still relatively small.

However there remain nearly 1 million council houses and their council landlords are operating in a financial environment which is disadvantageous to them compared with other providers and provides no incentive to assist with the current shortage of affordable housing . As a number of housing associations face funding difficulties, resources for PFI schemes dry up and the capacity of private sector builders to meet housing demand reduces markedly, the potential role of councils as providers of affordable housing is being seen in a new light. Government attempts to prompt the economy out of recession have included references to new public sector capital programmes designed to stimulate the construction sector and this fits well with calls for councils to build houses again.

3. Government objectives

This consultation paper claims that Government wants local authorities to play a bigger role in securing the supply of new affordable housing and that this should include new opportunities for councils to develop housing directly where this offers value for money in comparison with other options.

The purpose of the paper is to set out proposals for removing some disincentives to local authority investment in new council housing within the current financial framework.

At present, the council housing finance system redistributes the revenue (through Housing Revenue Account Subsidy (HRAS)) and capital returns (through pooling) from new and existing housing on the same basis. Neither pooling nor the HRAS distinguishes between homes which were built in the past with an element of central Government financial support and new homes which represent a largely local investment.

In July 2007, the Housing green paper, *Homes for the future, more affordable, more sustainable*¹, said that "*Where councils choose to invest their own money in new [housing] supply, we think they*

should be able to keep the income and capital returns from those additional homes.”

The changes to the treatment of income from new homes can now be made using powers in section 80B of the Local Government and Housing Act 1989, which was inserted by section 313 of the Housing and Regeneration Act 2008. This provides for exclusions of specified properties or descriptions of property, including future properties, from the HRA subsidy system. This would in effect make the properties “invisible” to the current HRA subsidy system whilst leaving them within the Housing Revenue Account.

Section 80B of the Local Government and Housing Act 1989 (as inserted by Section 313 of the Housing and Regeneration Act 2008) provides for agreements between the Secretary of State and a local authority which would have the effect of excluding either a local authority’s whole housing stock or specified properties (including future properties) from the operation of the Housing Revenue Account subsidy system.

Agreements under this section would not have any impact on the operation of the Housing Revenue Account itself. The rules requiring councils to maintain a ring-fenced landlord account – the Housing Revenue Account – would continue, and the homes excluded from the subsidy system would remain within the Housing Revenue Account.

There is currently no provision made in the formulae within the HRA subsidy system for financing the capital costs of new council housing (other than PFI).

As a result, if a local authority builds or acquires a new dwelling, the allowances for that council increase only by the running costs associated with the new property (mainly allowances for management, maintenance and major repairs). If, as is likely with newly built dwellings, the assumed rental income for those properties exceeds the assumed need to spend as prescribed by these allowances, the difference is deemed to be a surplus. Where such surpluses accumulate across an authority’s Housing Revenue Account there will be an equivalent reduction in net subsidy, even where the council’s subsidy position as a whole is in deficit.

If the provisions were used to exclude new council homes from the HRA subsidy system, this would increase a council’s retained rental income by the difference in the subsidy formulae between the allowances and the assumed rents for those properties.

The impact of the provisions would depend on the allowances that a particular property attracts and its guideline rent. In aggregate nationally, management, maintenance and major repairs

allowances are currently equivalent to around 72 per cent of assumed rental income this year. (Most of the remainder is used to meet the costs of servicing HRA debt.) For a dwelling with a similar profile of rent and allowances, the provisions would therefore allow the council to retain the remaining 28 per cent of assumed rent from each new home.

The value to a council of the provisions would be the same, whether or not it sets the actual rent in line with the notional rent used in the HRA subsidy formulae. It would also be the same regardless of whether a council was a net contributor or beneficiary of the HRA subsidy system.

4. Properties to be covered by the agreements

It is proposed that section 80B agreements should be offered for

- New build properties
- Properties purchased or otherwise acquired
- Derelict or uninhabitable properties brought back into use as a result of significant council investment

All of the above would be held outside of the HRA subsidy system but inside the ring fenced HRA.

The intention is to allow a council to retain the return from its own investment in new housing. This is why the paper proposes that the exclusions should cover properties that have required a large local investment to bring back into use. For the same reason the following types of properties should not qualify for exclusion from the subsidy system:

- Properties which are temporarily vacated to allow refurbishment or remodelling work to take place
- Properties which are vacant whilst awaiting minor works to make them suitable for occupation
- Social housing transferred from one social landlord to another.

5. The process of securing a section 80B agreement

The aim is to keep burden of securing an exclusion from the HRA subsidy system as to a minimum, commensurate with ensuring the powers are used properly and effectively.

It is proposed that councils apply for an exclusion for schemes or bundles of schemes, wherever possible, rather than for individual properties and where authorities acquire properties one by one or a few at a time, that they bundle them together when seeking a section 80B agreement.

As schemes are subject to change up to delivery, it is also proposed that agreements allow for a reasonable level of variation

in delivery, for example in the number and types of properties to be covered and the timing of starts and completions. It is not expected that agreements will be entered into based on early speculative outlines of schemes; applications should contain sufficient information about the properties to establish that they will meet the criteria for exclusion.

Criteria against which an application would be considered

In granting an exclusion from the HRA subsidy system, evidence that appropriate local decision-making processes have been applied, including a robust options appraisal, and that the option chosen offered value for money would be expected.

The powers in the Act provide for agreements to contain terms and conditions. Applications should include details about the scheme, including design and quality standards, rents and allocations policies. Properties would only be excluded which conform to all Government policies regarding council housing, including rents and allocations policies, and would expect the application to include such commitments.

In considering whether to enter into agreements to exclude council properties from the HRA subsidy system, Government must also consider the overall impact on government's fiscal policies as local authority spending and borrowing are part of overall public expenditure. Increases in spending and borrowing made possible by exclusions must therefore be affordable within national as well as local spending plans and policies.

Government propose to ask the Homes and Communities Agency to review all applications for a section 80B agreement, and to advise the Secretary of State as to whether applications meet the criteria for exclusion. The final decision on applications will be made by the Secretary of State.

6. Rules on capital receipts

The 2007 Housing green paper, *Homes for the future: more affordable, more sustainable*, also proposed that councils should keep the full capital receipt of new build properties subsequently sold under Right to Buy. At present, 75 per cent of those net receipts are paid to Government and pooled centrally. This figure was set roughly to reflect the historic split between national and local investment in council housing.

This is perceived as unfair for new local authority properties that are financed wholly locally. A council currently risks losing most of its own capital investment if a tenant exercises their statutory Right

to Buy, but would of course still retain the debt associated with the investment.

The paper is also seeking feedback on proposed changes to the *Local Government (Capital Finance and Accounting) (England) Regulations 2003*. These changes would allow councils to retain all of the receipts from a subsequent sale of a property covered by an exclusion from the HRA subsidy system made under section 80B, provided that the receipts were used for affordable housing and regeneration projects. This would effectively extend the existing provision for receipts arising from the sale of vacant housing land and other housing assets that are not dwellings.

7. ARCH Comment

ARCH wishes to highlight some issues which could form the basis of our response to the consultation paper and which member authorities may wish to bear in mind when formulating their response.

ARCH welcomes the approach taken to enable councils to retain more rental income from their existing council stock and so have more resources to allocate to building new homes. The intention to remove some of the financial barriers stopping councils from building new properties and increasing their housing stock is also welcomed. The consultation paper poses a number of specific questions and ARCH members are invited to consider the issues raised and respond to the initial ARCH views as set out below.

QUESTION 1: Given the objectives of the policy, what types of properties should qualify to be excluded from the HRA subsidy system and pooling requirements?

ARCH supports the proposal to enable the defined types of properties to be held outside of the HRA subsidy system.

However there may be issues of clarification over the definition of “derelict or uninhabitable properties brought back into use as a result of significant council investment”. It is assumed this applies to long term vacant properties in the private sector and councils should be given flexibility in determining application of this definition. There are foreseeable circumstances where an authority may commit significant resources on remodelling or converting properties that are not yet at the stage of being “derelict or uninhabitable” and such properties should also qualify to be excluded from the HRA subsidy system where it can be demonstrated that remodelling and/or conversion will bring additional net provision and/or meet specific housing needs such as supported housing.

Given that the “intention is to allow a council to retain the return from its own investment in new housing” and that some councils have been addressing the issue of affordable housing supply by building new houses, acquiring them and investing to bring derelict properties back into use in the recent past, it would seem reasonable that those councils who have already taken local action should be allowed to apply for retrospective exemption for schemes delivered or commissioned since the introduction of the Housing Green Paper where such schemes meet the defined criteria.

QUESTION 2: In your view, what types of properties should not qualify to be held outside the HRA subsidy system and pooling requirements?

This consultation relates to new council housing and there is a very good case, enunciated within the paper, for making specific arrangements for new council housing.

The 3 categories of properties that section 80B agreements will be offered for appear to give councils wide flexibility and this flexibility should not be constrained by application of detailed rules or regulation. The key is to enable councils to provide more affordable housing.

ARCH trusts that the proposals in this consultation paper will be reflected in the final outcome of the review of the Housing Finance system and the applicability of the national HRA subsidy system which is widely recognised as unfair, penalises far more councils than it supports and undermines local accountability for spending locally raised funds.

QUESTION 3: Do you think that that the proposed process for applying for a section 80B exclusion is the right one to adopt? If not, what would be a better alternative?

ARCH welcomes the intention to minimise the amount of bureaucracy associated with this scheme. The application process should be simple and straightforward and the awarding body should consider the applications in the context of the need for more affordable housing and not insist spurious detail within the application.

QUESTION 4: What factors should be taken into account by the Secretary of State in considering whether to enter into an agreement to exclude properties?

The paper notes that “evidence that appropriate local decision-making processes have been applied, including a robust options appraisal, and that the option chosen offered value for money would be expected” as part of the application.

A clear definition of “value for money” should be provided which takes into account issues of finance, local demand and supply

The decisions made by councils which result in homes being built, purchased or brought back into use are taken within the context of local circumstances and these must be considered when making agreements. The application process should be flexible enough to take account of local circumstances and differences.

QUESTION 5: What terms and conditions do you think should be included in exclusion agreements?

The paper notes that “Government must also consider the overall impact on government’s fiscal policies as local authority spending and borrowing are part of overall public expenditure” when deciding whether to enter into agreements. In order to minimise the amount of time and effort potentially wasted on the application exercise, Government should consider the impact on national fiscal policies prior to drawing up the guidance so that they know how many and what type of application are likely to be accepted and inform local authorities of this.

ARCH welcomes the intention to establish criteria around design and quality standards, rents and allocations policies providing these are not overly prescriptive. ARCH suggests that schemes should also be considered against wider criteria such as whether community benefits were built into the schemes and each scheme should be judged on its overall contribution made to the local neighbourhood incorporating a range of local economic, environmental, physical, community as well as housing criteria.

QUESTION 6: Do you agree that properties excluded from the HRA subsidy system under section 80B should also be exempted from the requirements to pool capital receipts?

This paper notes that the current arrangement whereby 75 per cent of net receipts from Right to Buy are paid to Government and pooled centrally is perceived as unfair for existing local authority properties let alone any new local authority properties provided under this proposal which would be initiated and financed at local level.

ARCH agrees with this approach and feels that councils should be allowed to retain all of the receipts from a subsequent sale of a property covered by an exclusion from the HRA subsidy system made under section 80B.

QUESTION 7: Do you agree with the proposed conditions attached to the exemption from pooling, which require receipts to be used for affordable housing and regeneration?

The definition of regeneration needs clarification as it means different things in different councils and should include use to achieve and maintain the Decent Homes Standard. If this requirement is wide enough to mean that local authorities can use receipts for any affordable housing or regeneration related activity then this would be acceptable and would back up the statement in the paper "How a local authority chooses to invest its own resources is essentially a local matter". It is inappropriate for the Government to promote the concept of local accountability and removal of these receipts from a national redistribution scheme and then to place limitations upon how it should be spent.

It is accepted that any receipts should remain within the HRA but there should be no limitations placed on how these receipts are spent within that account.

Further comment

Although ARCH welcomes the spirit within which these changes are proposed, the gap between demand and supply of affordable housing remains the major issue. These powers will provide councils with some limited extra resources and incentives to build council houses but they are unlikely to be sufficient enough to make a significant difference to local authority's ability to build houses. If the Government is serious about meeting the 3 million homes target, in the current economic climate, it must be willing to provide further substantial powers and incentives to local authorities so they are able to make a sizeable contribution to the target.

Although ARCH feels that the direct impact of these proposed changes will be relatively small in the context of the whole council housing sector, the spirit behind them (combined with other recent developments) does show a willingness to enable large scale building schemes to be put forward by councils.

Access to Social Housing Grant, the development of local housing companies and the allocation of funds to enable councils to purchase homes, which are not moving in the private market, are some such developments. Schemes whereby councils provide land, private contractors build homes (council houses, homes for sale and/or homes for private rent) and the income from homes for sale offsets the costs of building the council houses maybe one way forward. This would tempt construction firms looking for work, improve unemployment figures, bring brownfield land back into use, generate activity in the construction sector and the economy in general as well as increase housing supply. The fact that councils can provide mortgages would be a further fact to consider, as would the influence that Government now has over major banks to encourage them to lend.

ARCH would encourage councils to put forward schemes they feel are workable to test the limits of the changes proposed here and Government's approach to the wider issues noted above

ARCH believes these proposals are long overdue and as a first step in recognising the role that stock retaining authorities can play in contributing to the Government's national housing targets but as always the devil will be in the detail and ARCH would urge government to manage the process with a lighter pro-active touch without losing sight of the principle objective i.e. to enable councils to provide more affordable housing to meet housing need and play a key role in stimulating the construction industry in the current economic recession.

7. Consultation response

ARCH intends to respond to this consultation on behalf of members and asks for all comments to be incorporated in an ARCH response to be sent through to arch@lincoln.gov.uk by 31st March 2009, in order to respond prior to the deadline.

The final date for all responses to this consultation paper is 17th April 2009.

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