ASSOCIATION OF RETAINED COUNCIL HOUSING

National Federation of ALMOs

Together we serve the interest of more than a million homes in England

"Social Housing We Can All Be Proud Of": the case for investment 2019 Spending Review Submission

About ARCH and the NFA

165 councils in England own nearly 1.6 million homes, either managing them directly or through Arm's Length Management Organisations. ARCH represents councils that have chosen to retain ownership of council housing and manage it directly. The National Federation of ALMOs represents the 31 Arm's Length Management Organisations managing around 420,000 homes in 34 local authorities. Together we represent over a million council homes, one third of the social housing in England.

Summary of Key Asks

- **To invest in social rented housing, increase grant levels and the total grant available to build new social rented homes.**
- **Continue to support a council house building renaissance allowing local authority control over the self-financing HRA.**
- **Reform right to buy to ensure one for one replacement and an equitable and sustainable home ownership offer for council tenants into the future.**

A New Deal for Social Housing

We share the Government's ambition, as expressed in the Green Paper published last year, of a new deal for social housing, inspired by a vision we welcome and support, of "social housing we can all be proud of", as the then Secretary of State, Sajid Javid, expressed it when he announced the Government's intention to prepare a Green Paper. We are still waiting for the Government's formal response to consultation on the Green Paper and so this submission is based on the assumption that its main proposals, most of which gained wide support, including from local authorities and local authority tenants, will be implemented substantially unamended. We focus in this submission on those with the biggest financial implications for local authority housing, namely, investment in repair and improvement of the existing stock and the construction of the "new generation of council homes" to which the Government is committed.

Investment in social rented housing

Building 100,000 social rent homes a year would save the country billions whatever happens to the economy post-Brexit according to research published by ARCH, the National Federation of ALMOs (NFA), The Local Government Association (LGA) and SHOUT (the campaign for social housing). The report published in 2016 by City consultancy Capital Economics assessed the impact of future investment in social rented housing on the UK economy in the light of Brexit.

Analysing the potential future direction for borrowing costs and economic growth, the new analysis **Building New Social Rent Homes An Updated Economic Appraisal** presents four scenarios for the economy post-Brexit ("Britain becomes Japan"; "Back to the 1970s", "Strong Economic Growth" and "Capacity Constraints"). The research finds that in each of the scenarios funding new social housing would deliver long term savings to the Government of up to £300 billion.

The original research **Building New Social Rent Homes: An Economic Appraisal** concluded that *"the government would achieve better value for taxpayers' money, as well as improve the living standards of many low-income households, if it were to part fund the delivery of 100,000 new social rent homes each year rather than continue with its existing policy."* And none of the fundamental assumptions in this research have changed, in fact, demand for low cost rented housing has only increased since we published it.

The report also points out that "The construction sector is particularly good at stimulating knock-on activity elsewhere in the economy and, therefore, generating further tax revenue." A report for the UK Contractors Group estimated that every pound spent on construction output stimulates an increase of £2.84 in gross domestic product. A large proportion of construction revenues remain in the domestic economy and so it is a particularly beneficial area for government to invest in, allowing counter cyclical development in the face of a downturn and providing a real boost to local economies.

We support the call by other sector organisations such as the CIH, the NHF, Shelter, Crisis and the Campaign for the Protection of Rural England for increased grant levels to build the number of new homes at social rent levels that the most recent evidence shows are needed. Research commissioned by the National Housing Federation and Crisis and carried out by Heriot Watt University in 2018 highlighted a need for 145,000 affordable homes per annum over the ten years 2021-31, of which 90,000 are for social rent and the remainder for low-cost homeownership or intermediate renting. The projections show that any programme has to be heavily skewed towards southern England (including London), which accounts for the majority of new need.

As the CIH summarise in their submission, "the total build cost for a programme of this size is an average of £46.2bn per year. The majority of this would be met from a combination of private borrowing, cross subsidy from sales, the implied cross subsidy from s.106 contributions by private developers, and discounted land values. **The remainder (£14.6bn per year on average, or £12.8bn in today's prices) must be met via capital grant from the government."**
They also conclude that "**the average grant will need to be 44 per cent, with an average grant per unit of £183,000 for a social rent, £99,000 for affordable rent and £32,000 for shared ownership**."

A New Generation of Council Housing

The Conservative Government has a commitment to build “a new generation of council homes to help fix our broken housing market”, and “get back to the scale of social housing that will deliver a real difference to communities”. We believe that, within its overall target to increase housebuilding to 300,000 homes a year, the Government should set an explicit target for new council housing and, more widely, new social housing at genuinely affordable rents. Glen Bramley, in research for Crisis and the National Housing Federation, has made a convincing case that the latter target should be around 100,000 homes a year[1]. We argue that local authorities should be tasked to provide at least a third of these to start with rising to at least half over time.

In the last decade, councils and ALMOs have started to build on a small but growing scale. The abolition of HRA borrowing caps, which we warmly welcome, will enable them to do substantially more, and we see no reason to disagree with the estimate in the 2018 Budget that output is likely to rise to 10,000 a year by 2022. This, however, is half the 20,000 a year optimistically predicted in 2012 (which assumed borrowing caps would remain). It is also less than the 12-13,000 homes sold annually since the reinvigoration of the Right to Buy and barely enough to match the additional sales to which the one-for-one replacement policy strictly applies. It is not sufficient to deliver the “new generation” of council homes the Government wants to see or make a “real difference” to communities. The next Budget needs to include a costed and funded action plan to expand council housebuilding, over time, first to 30,000 a year, the number necessary to replace Right to Buy sales and end the homelessness crisis, and then to 50,000 or beyond.

The economic case for such a plan is strong. In 2015 ARCH and the NFA joined with SHOUT and others to commission independent analysis by Capital Economics of the impact of building 100,000 new genuinely affordable rented homes a year. The analysis was published in June 2015 as *Building New Social Rent Homes: an Economic Appraisal,* followed by an update in October 2016 re-evaluating the analysis in the light of the European referendum result.[2] From our perspective the key conclusions are that expansion of the development programmes of councils and housing associations on that scale would:

- offer a pathway out of expensive and insecure private renting, and on towards ownership – in part via the Right to Buy – for those hardworking households who are “just managing”;
- over time, reduce the cost to government of meeting the housing needs of low-income households;
- make a major contribution to the Government’s ambition of 300,000 new homes a year, and
- help address pressure on public services, notably health and social care, driven by poor housing conditions.

A plan to increase council housebuilding to 50,000 homes a year could be funded from a range of sources:

- increased borrowing by local authorities, within prudential limits, repaid from future rent income on social rent housing, or cross-subsidy from the HRA or from market housing for rent or sale also provided by local authorities within the HRA;
- receipts from Right to Buy and other sales of council land and housing, including the portion of receipts currently reclaimed by the Treasury;

- Contributions from private developers through section 106 agreements or similar arrangements, representing a share of the appreciation in land value triggered by grant of planning permission for housing;
- Contributions from Government through grants.

We argue below that the capacity of local authorities to finance new housing through cross subsidy from HRA rental income has been severely reduced by shifts in Government rent policy, and introduction of an enhanced Decent Homes Standard is likely to reduce it still further. We believe this source of subsidy is unlikely to support more than 10,000 homes a year. Total Right to Buy receipts over the last 5 years have averaged just less than £1 bn a year (£952 million in the five years 2013/14 – 2018/19), in principle sufficient to support a further 10,000 homes a year. We await the Government's response to its consultation last year on the use of Right to Buy receipts; there is an opportunity here to provide real help to enable councils to expand construction. The key reforms are:

- To allow all councils to use receipts to fund construction of housing for social, not just affordable, rent;
- To allow all councils to supplement receipts with Affordable Housing Grant, especially in low-house price areas;
- To extend the period within which current and future receipts can be used to five years.
- To enable local authorities to transfer receipts to ALMOs as they can to housing associations.

We believe local authorities should be able to retain 100% of the net receipts from RTB sales and use them to finance replacement housing – the current restriction of the replacement policy to "additional" receipts arising from reinvigoration of the Right to Buy is mystifying to the non-expert and no longer has any convincing rationale.

We also believe there is a case for a wider review of RTB discount and eligibility rules, particularly to consider the merits of more local variation. Imposition of the same maximum discount to all areas outside London provides RTB purchasers in many low house-price areas with discounts they arguably do not need in order to buy and leaves the relevant authorities with insufficient receipts to fund replacement homes. Recent research by Savills for the LGA makes a convincing argument that lowering the discount in such areas would have a limited impact on the volume of sales yet lead to a substantial increase in the receipts available for investment. There is also a case for extending the cost floor mechanism from 15 to 30 years to better protect councils from financial loss when newer homes are sold.

Case studies: Derby Homes and Stoke City Council

Data from Derby and Stoke illustrate the difficulty of funding replacement homes in low house-price areas. The graph below shows the percentage of the housing stock sold in each year since 2008/09 in Derby and Stoke; data for London and England are shown for comparison. The graph shows the scale of the increase in sales since 2012, but it also shows that, while the rate of sales has tailed off in London since 2016, it has continued to increase in Derby and Stoke, probably because the discounted price of homes is so low. However, the other side of this coin is that the net proceeds from sales are quite inadequate to fund replacement homes, falling well short of the 30% contribution to the cost of replacement assumed in current policy, as is shown clearly in the table below.

Graph: Percentage of housing stock sold under Right to Buy since 2008/09

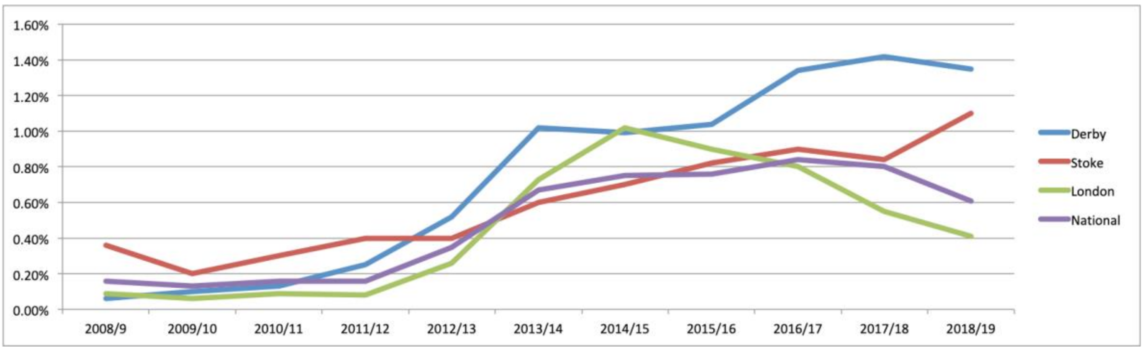

Table: Net proceeds available to finance replacement homes in Derby and Stoke[3]

	Derby		Stoke	
	Flat	House	Flat	House
Market Valuation	52000	110,000	44,750	74,600
Average discount	70%	70%	59%	47%
Sale proceeds	15,600	33,000	18,350	39,540
Admin allowance	-1300	-1300	-1300	-1300
Average debt	17,252	24,996	-4017	-6649
Net amount available for replacement	2,952	6,704	13,033	31,591

Making the most of a major public asset

Council housing is a major public asset, yielding a rental income of over £7 billion a year that is available both to repair and improve the existing council stock and to contribute to the construction of new council homes. The HRA self-financing settlement initiated by the Localism Act in 2012, with the support of both Government and Opposition parties in Parliament, would, as originally introduced, have enabled the 165 councils with housing to maintain their existing stock to the Decent Homes Standard and build around 20,000 new homes a year[4].

The settlement was intended to endure for the long term, enabling council landlords to plan for the future through the development of robust and sustainable 30-year housing business plans financed from borrowing, where necessary, that could be repaid from anticipated rent income. However, since April 2012, successive Government decisions have significantly reduced the rental income councils can expect to be available to them.

The original self-financing settlement was based on the assumption, used by the Government in deciding how much debt each council could afford to take on as part of the settlement, that rents would rise annually by 0.5% above inflation as measured by the Retail Prices Index, throughout the business plan period of 30 years. However:

- In June 2013, the Government announced that from April 2015 the rent increase formula would be based, not on the Retail Price Index, but on the Consumer Prices Index plus 1%, and the allowance of an additional £2 per week per unit to achieve convergence with housing association rents ended.

- In July 2015, the Government announced plans, later enacted in the Welfare Reform and Work Act 2016, to reduce council and housing association rents by 1% a year for four years from April 2016. By April 2020 rents will be 10% lower than they were in April 2016.

- In October 2017, the Government announced that, from April 2020, local authorities will once again be able to raise rents by CPI + 1% for at least 5 years; however, this implies that rents will remain 10% below where they would have been before the rent reductions were applied.

- Since 2012, successive welfare reforms – the under-occupation charge, benefit cap, and roll-out of Universal Credit – have made it more difficult to collect rent from growing numbers of council tenants. (NFA and ARCH Welfare Reform Survey)

We warmly welcome the steps the Government has taken since 2016 to restore more favourable conditions for council housing investment, particularly the decision to abolish HRA debt caps. There is no doubt, however, that the prolonged period of uncertainty about rent policy from 2020 and the possibility of a levy on higher value assets forced many councils to put major investment decisions on hold for too long. This uncertainty has largely been resolved, although extending the new rent policy to cover a minimum of 10 years from 2020 would significantly improve the confidence with which councils can plan for the future. But it remains the case that the rental income councils can expect over the business plan period is now very substantially less than was envisaged when the self-financing settlement was introduced, with significant impact on their capacity to fund capital investment.

Decent Homes and Beyond

The self-financing settlement was designed to enable all local authorities to bring all stock up to the Decent Homes Standard and keep it there and by and large they are doing that. The latest local authority returns show that, as at 1 April 2018, there were 70,300 non-decent local authority-owned homes (4.4%), a decrease of 11% from the previous year and a 91% decrease from 2006 when the decent homes standard was updated[5].

In responding to the Green Paper *A New Deal for Council Housing* ARCH and the NFA supported the proposal that social landlords should be expected to meet the same requirements in relation to smoke and carbon monoxide alarms and periodic electrical testing as apply to private landlords. We also agreed that the Decent Homes Standard should be updated and extended to include clearly defined standards for the maintenance of common parts, particularly in view of the need for the new standard to include comprehensive requirements to ensure fire safety. These enhancements are, we believe, the minimum necessary to give all tenants confidence that their homes are safe from fire, but will come at significant cost and will need to be financed.

We also agree that the new standard should include improved requirements for energy efficiency: we support the aim to ensure that all dwellings reach EPC Band C by 2030 at the latest. This too, has significant financial implications: figures from the Energy Saving Trust suggest that only 55% of social rented homes currently meet EPC Band C or above. It may be particularly difficult to achieve Band C in medium and high-rise blocks without cladding.

We are not able at this stage to attempt a costing of these proposals, other than to note that the cost will be substantial. As the precise specification of the updated, enhanced Decent Homes Standard is developed, we expect to work with Government to agree a well-evidenced, robust estimate of the cost of implementing it alongside a realistic timetable for implementation, together with proposals for financing it.

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[1] https://www.crisis.org.uk/media/239700/crisis_housing_supply_requirements_across_great_britain_2018.pdf

[2] Capital Economics for SHOUT and the NFA *Building New Social Rent Homes - An Economic Appraisal,* 26 August 2015; *Building New Social Rent Homes 2016 Update*d**,** 2 October 2016
http://www.almos.org.uk/news_docs.php?page=1&subtypeid=24

[3] Figures for Derby are particular examples: flat sold in November 2018, house sold in May 2018; figures for Stoke are averages for all sales since April 2012.

[4] "The original self-financing model showed potential capacity for authorities to build more than 550,000 units over 30 years." John Perry and Glenn Smith (2016) *Investing in Council Housing: the impact on council business plans*, London, CIPFA & CIH

Association of Retained Council Housing
4 Riley Court, Millburn Hill Road
University of Warwick Science Park, CV4 7HP
Tel:024 7647 2711

info@arch-housing.org.uk
www.arch-housing.org.uk
@ARCH_housing
Company Reg.No:07970258

National Federation of ALMOs
4 Riley Court, Millburn Hill Road
University of Warwick Science Park, CV4 7HP
Tel:024 7647 2729

info@almos.org.uk
www.almos.org.uk
@NFA_ALMOs
Company Reg. No:6781539

[5]https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/773079/Local_Authority_Housing_Statistics_England_year_ending_March_2018.pdf