Consultation response

DCLG consultation

Pay to Stay: Fairer Rents in Social Housing

November 2015

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Shelter

Shelter helps millions of people every year struggling with bad housing or homelessness. We provide specialist advice and support on the phone, face to face and online, and our legal teams can attend court to defend people at risk of losing their home.

However at Shelter we understand that helping people with their immediate problems is not a long-term solution to the housing crisis. That's why we campaign to tackle the root causes, so that one day, no one will have to turn to us for help.

We're here so no one has to fight bad housing or homelessness on their own.

We provide practical advice and support to over 4 million homeless or badly housed people a year via our website, telephone helpline and network of advice services. We employ over 200 advisers and 40 solicitors to give advice and offer representation.

Introduction

The Government has decided that social housing tenants with household incomes of £40,000 and above in London, and £30,000 and above in the rest of England, will be required to pay an increased level of rent for their accommodation if their rent is currently set at below market rent levels.

Shelter understands the needs of social housing tenants and the sector as a whole. We advised 50,442 social tenants in 2014/15; almost 40% of all of our clients in this period lived in the social rented sector. More than 1.3 million households were on social housing waiting lists in England on the 1st April 2014.1 Almost 83,000 households were found to be homeless in England during 2014.[2]

Summary

The Government argues that the potential advantages of a mandatory Pay to Stay scheme will be:

- An increase in local authority rent revenues, which will deliver additional income to the Exchequer.
- Housing associations will be able to use the additional income to reinvest in new social housing.
- In those cases where higher-income tenants choose to leave the sector, they will 'free up' social housing for those with greater need.

Shelter is not against the principle of some social housing tenants paying slightly higher rents depending on their income and we acknowledge the above advantages. However, we are concerned that these possible benefits could be vastly outweighed by the potential disadvantages of this policy:

- The proposed income thresholds at which higher rents would apply are too low and so crudely applied as to increase dependency on benefits and reduce incentives to work, in contradiction of government policy objectives.
- The scheme could be overly bureaucratic and costly to administer.
- Although it is only likely to affect a small number of tenants, the impact on them could be severe.

We are therefore pleased that the Government wants to ensure that the policy supports work incentives, and is seeking views on how the policy can be designed to achieve this.

Shelter recommends that:

- To reduce administrative costs and ease bureaucracy, the Government should consider a model similar to that applied in Hong Kong, whereby income reviews are carried out every two years and only after ten years of tenancy.
- Income thresholds must take both income and household size (and needs) into account.
- Threshold-setting mechanisms must take into account the impact of fluctuating household incomes.
- Thresholds must be uprated each year by the higher of CPI or average earnings.
- The first income threshold must be set significantly above the level at which households lose housing benefit/universal credit entitlement.
- Households on housing benefit and/or universal credit should be exempted from Pay to Stay. altogether, to avoid the complexity of being caught up in two sets of tapers, and unintended consequences for work incentives and the benefit bill.
- Household income should be derived from the tenant and their spouse or partner. Using the incomes of adult children to determine rent levels risks seriously undermining aspiration and work incentives.
- Like housing associations, local authorities should also be able to keep the extra money generated from these changes to invest in affordable housing.

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[1] DCLG live tables on rents, lettings and tenancies: Table 600 Rents, lettings and tenancies: numbers of households on local authorities' housing waiting lists, by district: England 1997-2014.
[2] DCLG Live tables on homelessness: Table 770: Decisions taken by local authorities under the 1996 Housing Act on applications from eligible households

Social housing tenants

In the Government's own estimates, the number of households affected initially by Pay to Stay, if implemented now, would be 290,000, approximately 7.4% of households in the social rented sector. This is expected to rise to 440,000+ by 2017/18 and increase every year thereafter. This is a small percentage of social tenants.

Social housing provides a home for some of the poorest and most vulnerable people in society, many of whom have little or no real choices about their housing. Nearly 90 per cent of social renters are in the bottom three income quintiles:

Quintile distribution of income for working-age adults by tenure[3]

	Bottom quintile	Second quintile	Middle quintile	Fourth quintile	Top quintile	All working age adults (millions)
Tenure						
Own outright	19	14	18	22	27	7.2
Buying with mortgage	11	12	19	26	32	16.7
Social rented sector tenants	**39**	**29**	**21**	**9**	**2**	**5.4**
All rented privately	21	18	21	22	17	7.6

Source: DWP (2013) Households Below Average Income

The guiding principle for social housing was that rents would be based on a formula that combined local wages and local property values. For example, for much of Southern England, rents were set at around 50% of local market rents, and even lower in very expensive areas. Crucially, social housing rents have allowed people to work without being dependent on housing benefit.

It is important that social housing rent policy, via the Pay to Stay earnings thresholds, continues to allow people to work, and improve their earnings, without having to become benefit dependent.

Previous consultation and introduction of a voluntary scheme

Shelter responded[4] to DCLG's 2012 consultation on 'High Income Social Tenants: Pay to Stay'. The original proposal was to set the threshold at £100,000, reduced to £60,000 once the voluntary scheme was introduced. The original consultation recognised that 'linking rents to income would be breaking new ground'.

We are therefore concerned that, since the introduction of the voluntary scheme, there has been no evaluation of how many social housing providers have chosen to implement this scheme or what its impact has been. There could be risks in failing to analyse the impact of existing schemes before proposing a mandatory roll-out of this policy combined with a reduction the income thresholds.

An initial analysis of the Government's figures suggests that this policy would be of limited value in addressing housing need. In our view, the real solution is to provide more genuinely affordable housing, rather than creating an additional bureaucratic burden for social landlords forced to charge higher rents to a tiny proportion of social renters, who have all worked hard and done well.

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[3] These figures apply to the UK as a whole. National Statistics (2012) Households Below Average Income: an analysis of the income distribution 1994/5-2011/12, DWP

[4] Shelter (2012) Response to DCLG on Pay to Stay consultation

Number of tenants affected

There are currently 3.92 million social rented homes in England[5], 7.4% of whom will be affected by Pay to Stay.

The impact assessment of clauses 74-83 of the Housing and Planning Bill 2015, which introduces the mandatory Pay to Stay scheme and mandatory rents for higher income social housing tenants, estimates that:

- There are currently 350,000 council and housing association tenants with household earnings over £30,000.
- Of these 350,000 households, 130,000 local authority households and 160,000 housing association households would be required to pay a market, or near market (80%) rent if the scheme was introduced now – 290,000 households in total.
- The number of households affected is expected to rise further by April 2017 (the date of the planned introduction) because of rises in the National Minimum Wage/National Living Wage and wage rises more generally. By 2017/18:
  - The number of affected households in local authority properties is expected to increase by 70,000, to 200,000 households,
  - The number of affected households in housing association properties is expected to increase by 80,000 to 240,000 households, and
  - The total number of affected households will be 440,000, with more coming in each year following this.
- Council and housing association tenants affected will pay an extra £1.05billion per year in rent:
  - Council tenants will pay an extra £510million in rent, which will be paid over to central government
  - Housing association tenants will pay an extra £540million to their landlord which associations will be able to keep, to reinvest in new housing.

Our key areas of concern

1. Definition of 'high incomes' and the ability of households to access the housing market

It is difficult to make a full assessment of the impact of this proposal because the key question – what constitutes a high income – is yet to be confirmed. In fact, the consultation document suggests that this could be settled after the consultation closes.

DCLG has used the income thresholds in the Summer Budget announcement to model the proposals by way of illustration, but states that these are likely to change.

The incomes suggested in the consultation document are:

- Households on incomes of £40,000 or more (£50,000 in London) will pay 100% of the market rent;
- Households on incomes of £30-40,000 (£40-50,000 in London) will pay 80% of market rent.

These income thresholds are below those the Government has used elsewhere. Income levels are set much higher when defining who is eligible for help to buy their own home. For example:

- Households are eligible for support to purchase a three bedroom home under Shared Ownership if they earn less than £85,000 a year
- Households under 40 years can receive a 20% discount when buying a Starter Home if their income is close to £100,000, as homes up to £450,000 are eligible
- Tenants eligible for the Right to Buy extension will be able to access a discount of over £100,000 regardless of their income – the total discount could exceed the amount that they have ever paid for the property in rent.

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[5] DCLG (2015) English Housing Survey, 2013-14

We are concerned that social tenants with household incomes of £40,000 or even £50,000 will be unlikely to be able to access the home ownership market in many parts of the country, and so an increase in their social rent would simply reduce their ability to save for a deposit.

We therefore recommend that the income thresholds are set at a level above which other Government home ownership schemes would be genuinely affordable.

2. Definition of household income

The consultation defines income as the taxable income of the two highest-income individuals in the household.

However, the income assumed in this modelling (contained within a footnote in the impact assessment) is **gross annual income** as described in the glossary of the English Housing Survey.[6] This includes all income of all people in the household, including benefits and tax credits as well as earnings. As a result, a couple with two children earning £25,000 currently qualify for £5,000 in child tax credit and child benefit, potentially making them a higher income household. This would clearly be problematic.

We note the footnote states 'different definitions of household income will be considered for the detailed policy design following consultation'.

We recommend that the consultation definition of income (i.e. taxable income) should be used.

We also recommend that household income should be derived from the tenant and their spouse or partner. Using the incomes of adult children to determine rent levels risks seriously undermining aspiration and work incentives.

3. Relationship between income and housing need

We are concerned that blunt income thresholds and market-based rent setting fail to take account of individual household circumstances and local markets. For example, a single social tenant in Burnley, for example, might easily be able to afford a market rent. But a family in Wandsworth, with two dependent children and the same income, might struggle to afford a rent on a family home set at either 80% or 100% of market rents.

The consultation document and the impact assessment both refer to household income but not household size. Unlike any other means-test, the income thresholds do not include household size, disability or debt. There is no recognition that families with these incomes could be entitled to housing benefit and that payments will increase if rent increases.

We therefore recommend that lower mandatory income thresholds must be more nuanced in order to take into account household size (and needs) and the affordability of the local market.

4. Relationship between income thresholds and inflation

The impact assessment states that *'as earnings increase over time, households who are currently beneath the thresholds at which higher rents are charge will break through the thresholds and be added to the higher-income cohort.'*

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[6] DCLG (2010) English Housing Survey technical advice: glossary https://www.gov.uk/government/publications/english-housing-survey-technical-advice

Our reading of this is that the £30,000 and £40,000 thresholds will not be uprated for inflation. On the assumptions used in the impact assessment, this means that tens of thousands of tenants who may not think they earn enough to be 'high income social tenants' will eventually be caught by Pay to Stay. Eventually, if the thresholds are not uprated, it will catch households most people would consider to be on low incomes. For example:

- A couple who are both working full time on the 'actual' living wage of £7.85 would earn £32,656 p.a. and would fall into Pay to Stay.
- A couple working full time on the new Minimum Wage from Spring 2016 (£7.20) will have a household income of £29,952 pa. If one of them were to agree to a single overtime shift they would be pushed over the £30k threshold.

Pay to Stay will affect social tenants including nurses, paramedics and teachers as soon as the policy is introduced. If the income thresholds fail to keep pace with wage inflation, this will increasing push keyworkers to move away from the jobs considered vital to our communities.

As the National Minimum Wage rises, most social tenants in full-time work will eventually be paying market rent, or near-market rent. This would have a disastrous impact on work incentives – few people would seek to increase their hours or progress to higher paid work if the only reward was an increase in their housing costs, potentially cancelling out their higher earnings.

We therefore recommend that the income thresholds must be uprated each year by the higher of CPI or average earnings.

5. Interaction with the benefit system

We are concerned about the interaction of the proposed income thresholds for Pay to Stay with the benefit system.

Many households with an income of £40,000 or even £50,000 in London will still be entitled to housing benefit whilst on a Social or Affordable Rent and, therefore, increasing their rent as their earnings increase will add both complexity to their work incentives and increase the housing benefit bill. It is important to note that under Universal Credit, entitlement to support with rents will be available further up the income distribution, meaning more tenants affected by Pay to Stay will add to the benefit bill.

Other people, not previously in receipt of housing benefit, could be pushed on to housing benefit if their earnings rise above the Pay to Stay threshold. This is clearly undesirable. It is worth pointing out that 12% of social tenants entitled to housing benefit currently do not claim – these households could be forced to claim if their rent were to increase.[7] Modelling by East Thames Housing Association (fig. 1 below) shows the impact of rent increases on housing benefit entitlement.

Fig. 1: Two adults and three children, three-bed home in East London (average rents in Newham, 2015/16)

Rent level	**Housing benefit when earning £40,000**	**Housing benefit when earning £45,000**	**Housing benefit when earning £50,000**
Social rent £136 pw	£0	£0	£0
Affordable rent	£52.85	£13,60	£0

[7] http://www.ifs.org.uk/uploads/publications/comms/R108.pdf

£198 pw			
Market rent £248 pw	£112.85	£63.60	£27.35

Shelter analysis further illustrates the impact of raising rents to 80% of the market rent in four inner- and four outer-London boroughs, for a family with two children and both parents earning £20,000 a year. In each of the eight boroughs, this family would be entitled to housing benefit to cover any increase in their rent:

Figure 2: Two adults and two children with both parents earning £20,000 a year

Area	**Median**	**80%**	**HB claim weekly**	**HB claim monthly**
Inner London	2,189	1751.2		
Camden	2,817	2253.6	305.95	£ 1,325.78
Haringey	1,733	1386.4	105.83	£ 458.60
Newham	1,400	1120	44.35	£ 192.18
Tower Hamlets	2,080	1664	169.89	£ 736.19
Outer London	1,475	1180		
Barnet	1,690	1352	£97.89	£ 424.19
Brent	1,675	1340	£95.12	£ 412.19
Hillingdon	1,350	1080	£35.12	£ 152.19
Waltham Forest	1,450	1160	£53.58	£ 232.18

We therefore recommend that households on housing benefit and/or universal credit should be exempted from Pay to Stay, to avoid being caught up in two sets of tapers.

Shelter’s comments on specific consultation questions

Question 1: How the scheme can support incentives to work

Shelter strongly supports the Government’s desire to ensure that the policy supports work incentives.

However, as indicated above, we are concerned that blunt, national thresholds which fail to take into account household size or needs, could penalising hard-working households.

Our concerns about the interaction between Pay to Stay thresholds and the benefit system are set out above. In this section we examine the impact of the policy on work incentives.

Thresholds set too low could undermine work incentives

Social (low) rents play an important role in work incentives as they enable households to stop being dependent on housing benefit more quickly and keep more of any additional £1 that they earn. A household in receipt of housing benefit already has relatively weak work incentives, as they lose 65p in reduced benefit for every extra £1 that they earn. Work incentives are therefore better for tenants able to earn enough to take them out of benefit dependency.

Setting the first threshold (currently £40,000 in London and £30,000 elsewhere) significantly above the benefit threshold would ensure that families do not find themselves with weak work incentives throughout their working lives and would ensure that an increase in rent did not push them back into dependence on housing benefit.

Tapers

Work incentives can be affected by factors such as the extra costs of travel or childcare, and the nature of tapers can have a real impact on whether work is financially and practically worthwhile.

The consultation suggests that a gradual increase in rent for social tenants as their incomes rise may be a fairer system than blunt thresholds. It suggests that one way this could be achieved is through a system that would ensure that households earning in excess of minimum income thresholds would pay increasing amounts of rent as income increases, for example in the form of a simple taper.

We agree that a gradual increase in rents as incomes rise seems fairer that blunt thresholds.

However, it will be important that tapered rent rises are set to ensure that tenants still see financial gains for earning more. As a starting point, tapers should be no higher than current benefit tapers (65%), which can already lead to work disincentives.

Multiple thresholds, though potentially simpler, would run a risk of creating cliff edges, whereby for each extra £1 earned a household would lose more than this in their net income as a result of a rent rise.

Introducing a new rent taper alongside a Universal Credit taper, however, runs counter to the laudable aims of simplifying the benefit system and improving work incentives. Many households may struggle to understand why increasing their earnings will affect both their rent and their Universal Credit entitlement, which are interlinked.

Ultimately, it is difficult to see how a system of intermediate thresholds and tapers could work, without becoming so complicated as to remove any incentive to work. We would welcome more information about how the Government intends to manage this.

We therefore agree with the suggestion in the consultation that the starting threshold for Pay to Stay should be set in relation to eligibility for housing benefit.

Shelter strongly recommends that the policy only be applied to households who are not entitled to housing benefit or Universal Credit, otherwise the consequence will be both an increase in the benefit bill and increased complexity.

Using income of young people in 'highest income' calculations could undermine incentives to earn and save for home ownership

We are concerned by the suggestion that household income will be based on the two highest earning individuals whose joint income is at, or above, the threshold. This would mean that a tenant in receipt of welfare benefits might be charged a higher rent because the earnings of adult children living with them – perhaps in order to save up for a tenancy or mortgage deposit – exceed the income threshold.

Shelter therefore recommends that household income should be derived from the tenant and their spouse or partner. Using the incomes of adult children to determine rent levels risks seriously undermining aspiration and work incentives of young people.

Question 2: Evidence of administrative costs and challenges

The consultation proposes that local authorities will be allowed to recover any reasonable administrative costs before they are required to return additional income from increased rents to the exchequer. As housing associations will be retaining the income they receive from higher rent payments to invest in new housing, they will be expected to absorb the administrative costs.

Assessing incomes

We are concerned about the proportionality of expecting social landlords to collect evidence of income from all social tenants when only a small minority will have incomes over the Pay to Stay thresholds. Currently, around 7% of social tenants are likely to have incomes high enough to be above the proposed thresholds – in less affluent parts of the country this percentage is likely to be even lower.

International experience

International experience has shown that inspecting the incomes of everyone in social housing is intrusive and difficult. An international comparative study commissioned by Shelter[8] concluded that most countries that have charged increased rents have found them to be difficult and inefficient in practice, and to generate adverse consequences.

Most parts of Germany have stopped charging increased rents because the bureaucratic costs of implementation were found to be substantial, and self-reported income estimates are found to be unreliable and investigation costly. There were also concerns that it would increase the residualisation of social housing.

In Hong Kong, income reviews are carried out regularly (every two years) after 10 years of tenancy and increased rents can be charged or tenancies ended if the tenant's income has risen too far. However, higher levels of state surveillance are routine in Hong Kong, so income disclosure is viewed as normal by tenants and routine by housing officers. Even so, income ceilings are set so that few tenants are charged increased rents, and very few lose their tenancies.

Timeliness of income evidence

The consultation proposes that rents are likely to be set using income from the previous tax year. However, as rents are reviewed in April, it is likely that rents will need to be set based on incomes from two full years earlier, over which time income could have changed considerably. If household income was to fall considerably, housing benefit, for tenants entitled to it, would increase to cover the shortfall – further increasing both dependence on housing benefit and risking an increase to the benefit bill.

This highlights a further concern. Not only is the level of income at which the threshold is set too low, but it fails to recognise the impact of a fluctuating income. Social tenants on low incomes are likely to be moving in and out of work, on zero-hour contracts and in insecure and unpredictable employment – their income is likely to fluctuate considerably from one month to another.

Income of non-dependants

The consultation advises that income is to be gross household income. It stresses that, where there are several adults in the house, the two highest incomes will be taken into account. This means that councils and housing authorities would not only need to collect the incomes of their tenants but also those of other members of their household. As set out above, where adult children move in and out of their parent's home, taking their income into account could be a considerable disincentive to work and to save.

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[8] Fitzpatrick, S. and Pawson, H. (May 2011) Security of tenure in Social Housing: An International Review, pages 21-23 (http://www.sbe.hw.ac.uk/documents/Fitzpatrick_Pawson_2011_Security_of_Tenure.pdf)

Overlap with housing benefit entitlement

As highlighted above, the current proposals do not take account of property or household size, and therefore fail to recognise the differing financial needs of different sized households.

One way to ensure that household size is taken into account would be to exclude those in receipt of housing benefit. This is important for a number of reasons, set out in question 1 above.

In terms of administrative complexity, it is difficult to see how it would be possible to taper rent rises at the same time as tapering entitlement to housing benefit. Housing benefit goes up as rent rises and down as income rises – it would be complex to administer both at the same time, and almost impossible for tenants to understand. In addition, the 'income unit' used for housing benefit is a tenant and their partner, whereas the current proposal for Pay to Stay is the two highest paid earners in the wider household – to potentially include adult children or other relatives.

We therefore recommend that:

- To avoid unecessary bureaucracy and costs, the Government should consider a model similar to that applied in Hong Kong, whereby income reviews are carried out every two years only after ten years of tenancy
- Thresholds must take both income and household size (and needs) into account.
- Threshold-setting mechanisms must take into account the impact of fluctuating household incomes.
- The first income threshold must be set significantly above the level at which households lose housing benefit/universal credit entitlement.
- Households on housing benefit and/or universal credit should be exempted from Pay to Stay altogether, to avoid being caught up in two sets of tapers, and unintended consequences for work incentives, the benefit bill and complexity.
- Household income should be derived from the tenant and their spouse or partner. Using the incomes of adult children to determine rent levels risks seriously undermining aspiration and work incentives.

Conclusion

Shelter is not against the principle of some social housing tenants paying slightly higher rents depending on their income. However, we believe the proposed income thresholds are too low given how unaffordable market rents are in many parts of the country, particularly for family-sized homes. They could create work disincentives and prevent people from saving for owner-occupation.

The use of income thresholds must also be set against the practical implications of implementing Pay to Stay. Shelter does not believe that the proposal offers sufficient benefits to merit the inevitable costs of administering the scheme.

Before mandatory Pay to Stay is implemented, it is extremely important that the Government undertakes and publishes an analysis of the impact of the existing voluntary Pay to Stay scheme, with the threshold set at £60,000.

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