Consultation response

CLG consultation:
Council housing: a real future
Prospectus

July 2010

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Shelter is a national campaigning charity that provides practical advice, support and innovative services to over 170,000 homeless or badly housed people a year. This work gives us direct experience of the various problems caused by the shortage of affordable housing across all tenures. Our services include:

- A national network of over 40 advice services
- Shelter's free housing advice helpline which runs from 8am–8pm
- Shelter's website (shelter.org.uk/getadvice) which provides advice online
- The government-funded National Homelessness Advice Service, which provides specialist housing advice, training, consultancy, referral and information to other voluntary agencies, such as Citizens Advice Bureaux and members of Advice UK, who are approached by people seeking housing advice
- A number of specialist services promoting innovative solutions to particular homelessness and housing problems. These include Housing Support Services which work with formerly homeless families, and the Shelter Inclusion Project, which works with families, couples and single people who are alleged to have been involved in antisocial behaviour. The aim of these services is to sustain tenancies and ensure people live successfully in the community.

We also campaign for new laws and policies – as well as more investment – to improve the lives of homeless and badly housed people, now and in the future.

Shelter supports the replacement of the current Housing Revenue Account subsidy system, which is no longer financially sustainable to any local council. We are therefore very pleased that the Coalition Government is committed to action to overhaul the system[1].

With an estimated funding backlog of £3.2 billion to improve sub-standard council housing, 1.8 million households waiting for a council home, over a million children growing up in overcrowded conditions and millions of households struggling to meet their housing costs[2], it is essential that reform of the council housing finance system – along with this autumn's Comprehensive Spending Review – provides councils to with sufficient funds to:

- bring all homes up to current standards or repair and safety,
- meet future repair and modernisation needs,
- avoid unaffordable or unexpected rent rises to their tenants,
- build desperately needed new homes and
- remain financially viable as council landlords so that tenants' homes are not at risk.

1. What are your views on the proposed methodology for assessing income and spending needs under self-financing and for valuing each council's business?

Shelter supports the principle of a more transparent and accountable housing finance system that allows council landlords to plan for the building, management and maintenance of the homes they provide. However, we have some concerns about the impact of a self-financing system in exchange for a one-off allocation of the 'notional' debt. Self-financing is risky for local authorities and their tenants. The present national subsidy system protects tenants from macro-economic risks, with the impact of interest rates or inflation increases being borne by central government. Self-financing is also risky because councils are taking on (from central government) long-term maintenance and modernisation responsibility without any certainty about the capital resources available to bring homes up to current standards. Therefore, in our response to the original consultation, we urged the Government to remove 'notional' debt from the housing subsidy system altogether. We argued that this would be equitable to the write-off of overhanging debt that took place when councils transferred their homes to a registered social landlord[3].

A self-financing settlement would require councils to make business planning assumptions about inflation, interest rates, rents, 'Right to Buy' receipts and costs of services for the next 30 years. It is therefore essential that, if debt is allocated, the assumptions made in the settlement model are sufficient to meet spending needs and prevent undesirable rent increases.

Assessing income: rents

Our biggest concern is that the debt settlement and self-financing must ensure that tenants do not face the risk of unaffordable or unexpected rent rises. The settlement model assumes income from rents over a thirty year period for a given level of stock. If these assumptions are incorrect, then rent revenues will be affected, business plans could become unsustainable and councils may consequently be forced to implement above-inflation rent rises or sell their assets to another social landlord. Shelter cannot support a proposal that puts tenants' homes at risk as a result of an unsustainable business model or, in order to make the business model viable, puts them at risk of sharp rent rises.

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[1] CLG News Release, 8 June 2010, *Grant Shapps - Government will overhaul unfair council house finance system*
[2] Shelter, June 2008, *Breaking point: how unaffordable housing is pushing us to the limit* found that 2.8 million (11 per cent) of households have had to borrow money to meet their housing costs. Shelter, March 2010, *The human cost: how the lack of affordable housing impacts on all aspects of life* found that 26 per cent of respondents say they spend more than 30% of their household income on housing costs. Of these, 41 per cent said their housing costs cause stress and depression.
[3] Shelter, October 2009, *Response to the CLG consultation – Reform of council housing finance*, page 9 (debt)

The impact assessment accompanying the prospectus cites evidence from Professor Steve Wilcox that:

'an increase in rent would raise more funds for council housing but would have undesired costs in the increasing housing benefit bill, impacts on the inflation rate and wider economy and negative impacts on work incentives. It could also have negative social and health effects'.

The impact assessment concludes that this evidence suggests that 'the principle of similar rents for similar properties should remain in place and rent restructuring should deliver equalisation'[4]. However, we are concerned that under the central scenario modelled by PricewaterhouseCoopers for a self-financing offer, rents are expected to converge 5 years after the start of self-financing[5]. Rent convergence in this period may lead to unacceptable rent rises.

It is important that the Government retains control over social rent policy to ensure that social rents are affordable to tenants and to avoid undesired economic, welfare and social costs. We therefore strongly support the prospectus's proposal that:

- 'Under self-financing, local authority landlords will still be required to follow national social rent policy.'
- 'The model assumes adherence to this policy'.[6]

It is also very important that councils' thirty year business plans make accurate and realistic forecasts of rental incomes, repair and maintenance costs and debt-servicing. If business plans prove to be unviable, there is a risk, acknowledged in the impact assessment[7], that councils would request a bail out from Central Government or be forced to sell their housing stock. In our response to the initial consultation, we argued that there should be a public sector safety net as part of the self financing agreement to avoid the risk of tenants' homes being placed at risk by unsustainable lending.

Assessing spending needs: uplifts in repair, management and maintenance allowances

We welcome the proposal to implement a 'floor' to ensure that all councils get a minimum of 10 per cent aggregate uplift in their combined Management, Maintenance and Major Repairs Allowances. This will have the effect of smoothing out wide variations and resulting in uplifts that vary between six and 15 per cent.

We also welcome the proposal to increase the combined average management and maintenance uplift in allowance to 5.4 per cent and the average major repairs allowance to 27.4 per cent. This will give councils extra funding capacity.

However, as we noted in our response to the original consultation, previous government estimates and research found that:

- 'The 2004-05 level of allowances would have to increase by about 67 per cent in real terms to reach the estimated level of need.'[8]

- 'There is a need to raise M&M levels by a minimum of 10 per cent and the MRA by, at the very minimum, 43 per cent. Successive stock surveys and further BRE evidence show that an increase

[4] CLG, March 2010, *Council housing: a real future – impact assessment*, paragraph 81
[5] CLG, March 2010, *Council housing: a real future – impact assessment*, paragraph 23
[6] CLG, March 2010, *Council housing: a real future – prospectus*, paragraph 2.3 (income)
[7] , March 2010, *Council housing: a real future – impact assessment*, paragraph 58

[8] Parliamentary question 1705 03/04, 29 April 2004.

of at least 60 per cent would provide a sustainable long term platform for capital investment to meet the needs of the stock.'[9]

- 'To fully fund allowances based on this evidence would need a 75 per cent uplift in MRA and a 5 per cent uplift in M&M.'[10]

We believe that uplifts need to more accurately reflect real spending needs.

Assessing spending needs: completing the Decent Homes Programme

The prospectus accepts that 'there will still be some landlords who have a backlog of works needed to achieve the Decent Homes standard which will require extra capital funding in early years' and recognises 'that £3.2 billion of works are still needed to meet [the] Decent Homes commitment.'[11] This figure is substantially less than the £6 billion identified in the original consultation. The prospectus states that 'meeting this investment need will therefore be a central element of deliberations on investment priorities at the next Spending Review.' The prospectus also mentions that many of the responses to the July consultation paper raised other spending pressures on housing that are not funded via the HRA, including adaptation for disabled tenants, asbestos removal and the Housing Health and Safety Rating System. Again, the previous Government indicated that these spending pressures would also be considered as part of the Spending Review.

Council landlords must be in a position to fund the existing substantial backlog of repairs, as well as existing backlogs of investment in areas additional to the Decent Homes programme, which – in addition to those mentioned above – include work to make homes more energy efficient and safe from fire. But the settlement model valuation does not include funding for the work required to clear the existing substantial backlog of repairs and improvements needed because the previous Government's position was that capital grants would be made available for this. If such capital grants are not forthcoming in the autumn 2010 Comprehensive Spending Review (CSR), the exclusion of the backlog from the offer valuation will mean that either tenants will continue to live in substandard homes, or there will be a considerable impact on some council landlords to the point that their business plans may not be sustainable.

We support the view of the Chartered Institute of Housing[12] that the restriction of Decent Homes funding to a level of £3.2 billion 'is particularly disappointing as there is overwhelming evidence that there are backlogs of investment in areas additional to the Decent Homes standard' and that 'we should 'not lose sight of the need to clear the remaining backlog'. We urge the Government to ensure sustained funding to address the backlog of works to council tenants' homes is made available in the forthcoming CSR. Such investment will be money well-spent to avoid additional costs, for example to the Health budget, of tenants, including pensioners and children, living in dangerous, sub-standard and energy inefficient homes.

If this additional funding is not made available via capital grants from central government, then councils must be enabled to fund this work themselves by the backlog being taken into account as part of the final offer valuation.

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[9] Hall, D., Hilditch, S., Partridge, S, Perry, J and Wilcox, S (May 2009) *Paying its own way: a sustainable future for locally managed council housing – Submission to the Government's Review of Council Housing Finance*.
[10] House of Commons Council Housing Group (2009) Council Housing: *Time to Invest: Fair funding, investment and building of council housing – report to the Government's Review of Council Housing Finance*.
[11] CLG, March 2010, *Council housing: a real future – prospectus*, paragraph 2.33 and 2.36 (completing the Decent Homes programme)
[12] Chartered Institute of Housing, April 2010, HRA Reform: Council Housing – a real future, CIH Briefing, page 4 (capital grants and ALMO funding)

2. What are your views on the proposals for the financial, regulatory and accounting framework for self-financing?

Borrowing

The prospectus proposes to cap future HRA borrowing at the level of the opening debt settlement[13]. As noted in our response to the original consultation, we understand that in the current financial climate, the Government is concerned about levels of public debt. Currently, local authority housing debt is included in the definition of public debt: the Public Sector Net Cash Requirement. We believe that the ability of councils to borrow to build new homes should be improved by changing the calculation of public sector borrowing rules. Local authority borrowing could be determined locally and treated like other social housing borrowing, such as borrowing by housing associations. We understand that the Chartered Institute of Public Finance and Accounting is confident that, were this to be done, the provisions for prudential borrowing would continue to ensure that borrowing levels would remain sustainable. We would prefer this approach in favour of the proposed borrowing cap.

Prudential borrowing would allow councils to finance desperately needed new housing to meet current and future housing need. This would be particularly important in the light of any cuts to central government capital investment in housing. However, if council borrowing were coupled with sustained central government capital investment in new housing, then much more housing could be delivered to meet local need.

The Housing Revenue Account and the ring-fence

In our response to the original consultation, we strongly supported the proposal that the HRA ring fence should be strengthened. The ring fence should operate at both national and local level to ensure that housing revenue and capital receipts are spent on housing. It is of great concern to us that a significant part of local authority services, such as tackling anti-social behaviour, debt and employment services, are being met by council tenants' rents[14]. In our view, rents should pay for core, rather than non-core, management services: rent collection, repairs and lettings management. This should ensure that tenants receive a good standard of service from their landlord.

We support the principles on which the draft revised Circular 8/95 is based, which distinguish between the housing services to be paid for via the Housing Revenue Account and the General Fund[15]. The updating of this guidance is long-overdue. It will ensure greater local transparency and accountability, and will allow constructive consultation with tenants and other local residents.

3. How much new supply could this settlement enable you to deliver, if combined with social housing grant?

It is not applicable for Shelter to answer this specific question.

However, more generally, we welcome the increase in the discount factor in valuing the undertaking from 6.5 to 7 per cent[16]. The prospectus explicitly links the increased discount to providing 'headroom' for new-build council housing: stating that it should enable councils to deliver 10,000 new councils homes a year by 2014/15.

We strongly support the commitment within the proposed settlement to provide such 'headroom'. We also support the recognition that 'it would provide a capacity to deliver a substantial new build

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[13] CLG, March 2010, *Council housing: a real future – prospectus*, paragraph 3.22 (borrowing by self-financing landlords)
[14] Communities and Local Government (July 2009) *Review of council housing finance: summary of commissioned research*. The research conducted for the review showed that at least 40 per cent of general management costs are additional to defined 'core management costs' and only a proportion of these 'non-core' costs are met from income streams such as the general fund or service charges.
[15] CLG, March 2010, *Council housing: a real future – prospectus*, paragraph 3.60 (HRA and the ring-fence)
[16] CLG, March 2010, Council housing: a real future – prospectus, paragraph 1.7 (the vision for self-financing)

programme, when combined with Social Housing Grant.'[17] With 1.8 million households currently waiting for a social rented home and over one million children growing up in overcrowded housing, it is essential that reform of the council housing finance system ensures that councils have the financial capacity to build desperately needed new homes to meet local housing need.

However, there is a danger that with additional debt, inadequate capital funding and restricted borrowing, many councils will have insufficient funds to build new homes. It is therefore vital that the final settlement is sufficient to allow councils to build new homes where they are needed. We urge the Government to provide further clarification on how the discount factor is to be applied and implemented.

We also urge the Government to continue to provide capital funding to councils to build new homes in the autumn 2010 CSR. Such capital funding would have added benefits of providing local and national economic growth, jobs and apprenticeships. Recent research by Shelter found that every £1 of public investment in housing is currently generating £3.51 of economic output. For every £100 million cut from the capital investment budget, there would be 2,500 fewer jobs in the construction sector and this would have specific implications for youth unemployment[18].

4. Do you favour a self-financing system for council housing or the continuation of a nationally redistributive subsidy system?

We have concerns about ending the pooling of capital receipts. Whilst we strongly support stronger ring fencing of capital receipts to be reinvested solely in council housing, there is an argument for continuing to nationally pool receipts and allocating them to individual authorities on the basis of need for capital investment. This would allow new housing to be built in areas where it is most needed, rather than in areas where there may be less need that are required to spent ring-fenced capital receipts.

5. Would you wish to proceed to early voluntary implementation of self-financing on the basis of the methodology and principles proposed in this document? Would you be ready to implement self-financing in 2011-12? If not, how much time do you think is required to prepare for implementation?

It is not applicable for Shelter to answer this question.

6. If you favour self-financing but do not wish to proceed on the basis of the proposals in this document, what are the reasons?

It is not applicable for Shelter to answer this question.

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[17] CLG, March 2010, Council housing: a real future – prospectus, paragraph 3.32 (borrowing by self-financing landlords)
[18] Shelter Research Briefing, June 2010, *Housing Investment: Part 1*