Review of Council Housing Finance

Impact assessment

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Summary: Intervention and options

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What is the problem under consideration? Why is government intervention necessary?

The housing revenue account subsidy (HRAS) system is the current redistributive system for financing council housing. The system redistributes income from areas where there is assumed to be a surplus to areas where the income does not match needs. This system though is not sustainable into the future - it will not deliver sufficient funding to maintain council homes to a good standard, and it is volatile which prevents any long-term planning. The review aims to find a new system that is sustainable, long-term and consistent with wider housing policy.

What are the policy objectives and the intended effects?

The policy objectives are to produce a system for financing council housing that is: fair, transparent and sustainable in the long-term. A system that supports tenant involvement in decisions about their homes and locality and enables councils to deliver efficient and effective housing services in their area. The system should be affordable for the taxpayer and it should integrate with wider housing policy and the role of the regulator.

What policy options have been considered? Please justify any preferred option.

Two broad options beyond do nothing:

1. Improved subsidy redistribution system with reduced volatility for longer-term planning and fairer allocations, uplifted allowances and continuation of the decent homes standard.

2. Self-financing system - a one off settlement would deliver self-financing for all councils for delivery of landlord service, councils would keep all their income after one-off debt redistribution.

Option 2 - Self-financing is the preferred option. It meets the principles set out at the start of the review. It will allow authorities greater freedom, and tenants more say in how their rents are spent.

When will the policy be reviewed to establish the actual costs and benefits and the achievement of the desired effects?

The options are in consultation during summer 2009, implemented over the following three years, full implementation unlikely till 2012-13. Will be reviewed after 2-3 years likely in 2014-15 or 2015-16.

Ministerial sign-off For consultation stage impact assessments:

I have read the impact assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible minister:

....Date: 21 July 2009

Summary: Analysis and evidence

Policy Option: 1
Improved Redistribution mode

Description: An improved version of the current system - with increased allowances, and reduced volatility.

COSTS

ANNUAL COSTS	
One-off (Transition)	**Yrs**
£ 16.2m	1
Average Annual Cost (excluding one-off)	
£ 700m	

Description and scale of **key monetised costs** by 'main affected groups' Cost to Exchequer of annual cost of increased management and maintenance and major repair (annual average - £700m)

Cost to local authorities of implementing new system - negotiation of business plans (£16.2m).

Total Cost (PV) **£ 12.3bn**

Other **key non-monetised costs** by 'main affected groups'

Costs if debt is redistributed - early repayment charges, costs to debt-free authorities. Change to rules of Right to Buy receipts.

BENEFITS

ANNUAL BENEFITS	
One-off	**Yrs**
£ 4bn	10
Average Annual Benefit (excluding one-off)	
£ 0.3bn	

Description and scale of **key monetised benefits** by 'main affected groups'

Efficiency savings due to long-term plan and optimal repair cycle (£2.6bn)

Homes maintained to a Decent Standard (£12.2bn)

Total Benefit (PV) **£ 14.8bn**

Other **key non-monetised benefits** by 'main affected groups'

Improved quality of housing and knock-on effects, new council houses built spreading benefit to more people - health, employment opportunities. Better disabled faciilities, improved leaseholder management. More new build and subsequent income from rent and sales.

Key Assumptions/Sensitivities/Risks Stock levels will stay at current level, overall national rent policy will remain, management and maintenance costs, and major repairs cost needs at the level of need indicated by review research. Risks - whether there is the capacity and capability of LAs to change to new system.

Price Base Year 2008	Time Period Years 30	**Net Benefit Range** (NPV) **£ £1.6bn to £6.5bn**	**NET BENEFIT** (NPV Best estimate) **£ 2.5bn**

What is the geographic coverage of the policy/option?			England	
On what date will the policy be implemented?			2012-13	
Which organisation(s) will enforce the policy?			TSA and CLG	
What is the total annual cost of enforcement for these organisations?			£	
Does enforcement comply with Hampton principles?			Yes	
Will implementation go beyond minimum EU requirements?			Yes	
What is the value of the proposed offsetting measure per year?			£	
What is the value of changes in greenhouse gas emissions?			£	
Will the proposal have a significant impact on competition?			No	
Annual cost (£-£) per organisation (excluding one-off)	Micro	Small	Medium	Large
Are any of these organisations exempt?	No	No	N/A	N/A

Impact on Admin Burdens Baseline (2005 Prices) (Increase - Decrease)

Increase of	£	Decrease of	£	**Net Impact**	**£**

Key: **Annual costs and benefits: Constant Prices** **(Net) Present Value**

Summary: Analysis and evidence

Policy Option: Self-financing

Description: Every local authority would keep the money they raise locally to run council housing in their area. End to redistributive subsidy.

COSTS

ANNUAL COSTS		Description and scale of **key monetised costs** by 'main affected groups'
One-off (Transition)	**Yrs**	
£ 32.4m	1	Cost to Exchequer of annual cost of increased management and maintenance and major repairs (£700m).
Average Annual Cost (excluding one-off)		Cost of implementing new system - negotiation of business plans (£32.4m).
£ 700m		**Total Cost** (PV) **£ 12.3bn**

Other **key non-monetised costs** by 'main affected groups'

Cost of rescuing failing authorities if system does not work. Costs if debt is redistributed - early repayment charges, costs to debt-free authorities. Change to rules of Right to Buy receipts.

BENEFITS

ANNUAL BENEFITS		Description and scale of **key monetised benefits** by 'main affected groups'
One-off	**Yrs**	
£ 4bn	10	Efficiency savings due to long-term plan and optimal cycle (£5.2bn)
Average Annual Benefit (excluding one-off)		Homes maintained to a Decent Standard (£12.2bn)
£ 0.7bn		**Total Benefit** (PV) **£ £17.4bn**

Other **key non-monetised benefits** by 'main affected groups'

Improved quality of housing and knock-on effects, new council houses built spreading benefit to more people - health, employment opportunities. More new build and subsequent income from rent and sales.

Key Assumptions/Sensitivities/Risks

Stock levels will stay at current level, national rent policy will remain, management and maintenance costs, and major repairs cost needs at the level of need indicated by review research.

Price Base Year 2008	Time Period Years 30	**Net Benefit Range** (NPV) **£ 3.4bn to £10.1bn**	**NET BENEFIT** (NPV Best estimate) **£ 5.1bn**

What is the geographic coverage of the policy/option?			England	
On what date will the policy be implemented?			2012-13	
Which organisation(s) will enforce the policy?			TSA and CLG	
What is the total annual cost of enforcement for these organisations?			£	
Does enforcement comply with Hampton principles?			Yes	
Will implementation go beyond minimum EU requirements?			Yes	
What is the value of the proposed offsetting measure per year?			£	
What is the value of changes in greenhouse gas emissions?			£	
Will the proposal have a significant impact on competition?			No	
Annual cost (£-£) per organisation (excluding one-off)	Micro	Small	Medium	Large
Are any of these organisations exempt?	No	No	N/A	N/A

Impact on Admin Burdens Baseline (2005 Prices) (Increase - Decrease)

Increase of £ Decrease of £ **Net Impact £**

Key: | Annual costs and benefits: Constant Prices | (Net) Present Value

Evidence Base (for summary sheets)

Background to the review

1. The joint CLG/HMT review of Council Housing Finance was announced in a written statement to the House of Commons by the housing minister on 12 December 2007[1].

The purpose of the review was:

2. To develop a sustainable, long term system for financing council housing, one that is consistent with wider housing policy, including the establishment of a regulator of social housing.

3. Any new proposals had to conform to the following conditions:

    - fairness and affordability for both tenants and taxpayers
    - transparency, giving a clear and accurate picture of the balance of support from local and central government
    - agreed minimum standards of service and accommodation
    - social rents can provide a platform for social and economic mobility to tenants
    - landlords will continue to improve the quality and efficiency of services
    - government is not exposed to unacceptable fiscal risks
    - there will be more certainty and less volatility in the funding of council housing

4. The review had the following guiding principles:

    - tenant involvement in local decision-making about the homes in which they live should be strengthened, with greater choice and mobility introduced into the system
    - standards and services at similar costs should be provided to all tenants regardless of which landlord (local authority or housing association) owns the property
    - similar properties should have similar rents regardless of landlord and that we should work towards achieving this in a timescale which maintains affordability for tenants
    - were appropriate, the system should allow more flexibility and greater devolution to the local level, supported by some degree of control and appropriate safeguards
    - the system of funding council houses should not work against the broader policy of helping more tenants into work
    - local authorities will continue to be landlords
    - there will be a single cross-domain regulator
    - the system should enable landlords to deliver improved efficiency and cost effectiveness in services
    - to introduce greater transparency into the system and reduce administrative burden where possible

5. The work was divided into four work-streams:

[1] http://www.communities.gov.uk/news/corporate/718043

- costs and standards – examined how much it costs to run the landlord business, and whether there should be a set standard for the homes
- rents and services charges – looked at policy on how rents and service charges are set
- rules of the housing revenue account – concerning the rules around the ring-fenced account
- funding mechanisms – looked at the current subsidy system and whether there were alternative models that could be used

The current system

Subsidy system

6. The housing revenue account subsidy (HRAS) system is the current redistributive system for financing council housing. It is a notional system, which means that the Government calculates the spending need of each local authority and compares it with their net income.

7. The assumed spending needs are made up of the following components:

- management and maintenance allowance
- major repairs allowance
- ALMO allowance
- PFI allowance
- Rental constraint allowance
- Interest on debt (historic and new borrowing)

8. These are notional amounts based on formulae that calculate the assumed need. The formulae for the management, maintenance and major repairs allowance calculate the amount an authority needs based on the number of households of different types with adjustments for other factors such as crime levels and deprivation.

9. If assumed income falls short of assumed need, the government provides subsidy to make up the shortfall. If assumed income exceeds need, the excess is recycled into the subsidy system to support those councils requiring subsidy. If any surplus money is left over it is returned to Treasury.

Treatment of debt

10. Debt levels vary greatly within local authorities with an average of about £7,000 per property. However about a quarter of local authorities are debt free, but some have very large levels of debt to a maximum of about £30,000 per property. Approximately two-thirds of this debt is estimated to be historical, dating back to before 2001, its distribution reflects spending patterns from many years ago and is very uneven. Payment of debt is one of the factors in the subsidy calculation and is thus one of the key drivers to the current system. The national cost of servicing current debt is over £1.1bn a year.

Capital receipts

11. For sales under Right to Buy (RTB) and other sales of dwellings to owner-occupiers 75 per cent of receipts are paid over to the Secretary of State, subject to a few concessions covering the retention of administrative and recent improvement costs. The remaining 25 per cent is retained by the local authority and may be used for any capital purpose.

12. For sales of dwellings which are not to owner-occupiers and sales of other housing assets (e.g. shops, garages and vacant housing land), authorities may retain all the receipt, provided they are used for affordable housing or regeneration projects. Any receipts not used in this way are paid to the Secretary of State: 75 per cent from disposals of dwellings and 50 per cent from the sale of other assets.

13. For sales under social homebuy local authorities retain 100 per cent of the receipt provided it is used for affordable housing.

14. The receipts pooled to central government are recycled to local authorities as part of larger housing grants. Retained receipts can be used by local authorities for any capital project.

Rents policy

15. Government currently has a set of policies that rents should be set at a level that facilitates work incentives within the current housing benefit system; should be fair both within districts and around the country; should be affordable to people who pay their own rents but should not be so low as to overly increase the costs of new social supply nor cause problems to the viability of RSLs. The policy is based on the principal of 'similar rents for similar properties in similar areas'. The level is set by a national formula based on property values (30 per cent) and local earnings (70 per cent) with an adjustment for the number of bedrooms. It was introduced in 2002 alongside the rent restructuring mechanism that aims to achieve parity between LA and RSL rents over a 10 year period.

Rationale for intervention

16. The current housing revenue account subsidy system is not delivering funding to council housing in an effective and sustainable manner. It is unpopular because:

- it is volatile and does not allow long term planning
- in the future, it will not deliver sufficient funding to maintain homes to a good standard
- many councils dislike their rents being distributed to their areas with any money leftover going back to government
- it is complex and difficult to understand
- there is concern over the relationship between rents and the services that are being provided. Rents are increasing but tenants are not seeing that increase passed on to services.

17. Without Government intervention the system will not change and it will continue to be both unpopular and ineffective in delivering funding to council housing. It also has an impact on the RSL sector since they are affected by the rents policy, so any changes will impact both the public and private secor.

Do nothing scenario

18. As stated in the rationale there are a number of issues with the current system that need to be addressed. If nothing were done to change the system the following problems would arise:

- There would be insufficient funding to maintain homes to a decent standard. Homes would gradually fall into a state of disrepair, meaning either the standard of living would deteriorate considerably with subsequent knock-on effects, or there would need to be a very large capital investment in the future much like the recent decent homes programme to bring the homes back up to a habitable standard.

- There would continue to be volatility in annual determination, meaning authorities can not plan effectively into the future. This will mean inefficient contracts will continue to exist and works will be carried out when the money is available rather than when they are needed.
- There will be less local ability to build new homes with the extra housing that would provide, the extra income it would raise from rents and the extra income it would raise from sales.

Options for change

19. The Review has examined a range of options for reform within two broad models for financing council housing in future:

- **improvements to a national system for funding** council housing in which revenues continue to flow between local and central Government as a result of ongoing assumptions made by Government about landlord costs and income

- **a devolved system (self-financing)** in which rents are retained by councils to spend on their own services, in exchange for a one-off redistribution of debt

20. All the options would share a number of characteristics:

- costs, standards and rents would be based on the same principles

- local authorities would be required to draw up 30 year business plans based on update stock condition surveys following the completion of their Decent Homes programme

- all housing capital receipts would be retained locally and would be accounted for alongside housing revenues

- any option which is taken forward following the consultation process will be fully compliant with the Government's new burdens procedures

Option 1 - Improvements to the current system

21. A key criticism of the current system is the unpredictability and volatility inherent in an annual subsidy determination process. This, it is argued, makes it hard to plan long term.

22. One option for addressing this would be to move to longer determination periods, of between three to five years, during which time assumptions made about costs and income would not change. It would facilitate management and enable plans for maintenance and repairs to be drawn up and stuck to with greater certainty than currently applies. It should also assist procurement, and in practice would improve the incentives for local authorities in running the stock.

23. These efficiencies generated could be used in a number of ways:
- to support new build
- to support capital improvements beyond Decent Homes
- to fund non-core services currently being paid out of the HRA such as supporting the worklessness agenda

24. Alternatively, it would be possible to include some triggers in the determination so that if a variable, for example inflation, moved outside a range, it would trigger a revised determination. However the inclusion of such mechanisms would tend to undermine the original purpose of a multi-year determination.

25. There is a risk that a three to five year subsidy determination could result in greater volatility at the end of each determination period, but this might be mitigated by an increased use of rolling averages for indicators.

Self-financing options

26. Under self-financing, each local authority would keep the money raised locally from rents and use it to run their stock.

27. Self-financing would require a one-off redistribution of housing debt in order to put all councils in a position where they could support their stock from their rental income in future. Without this redistribution of debt, some councils would either have to cut services or increase rents.

28. The aim would be to achieve fiscal neutrality for central Government between options which, as a result of a one-off redistribution of debt, remove the need for redistribution of incomes and options which continue to redistribute income through a national subsidy system.

29. Thus housing debt would be allocated to councils on the basis of each council's ability to service it, using the same updated figures for costs of management, maintenance, major repairs and income that would be used to calculate subsidy if we were to continue with a subsidy system.

30. In principle, the total debt allocated to councils under self-financing could be higher or lower than the current level of debt in the system. This would depend on the value to the landlord of the stock, which in turn is determined by the assumptions made about future costs and rental income.

31. The opening debt level would be one based on the tenanted market value of the stock. Under this option:

- Each council would produce a 30 year business plan. The investment needs in the plan would be based on common service standards and evidence from the review about the costs of delivering those standards. Assumptions about income in the plan would be based on rent levels set in line with Government social rent policy.

- The value of the stock would be calculated from the present value of the cash flows in the business plan.

- Each council's housing debt would be adjusted to reflect the value of its stock, entailing either a capital payment to or from Government.

Summary of costs and benefits

32. The following table details the estimated costs and benefits for each of the options:

	Costs	Benefits
Improved Redistribution Model Option 1 **Net Benefit £2.5bn** (Est. range £1.6bn to +£6.5bn)	▪ Increased management and maintenance, major repairs - £700m per year for 30 years – NPV £12.3bn. ▪ Cost of implementing new system. New formula. Estimated cost £16.2m (based on £90,000 per LA). ▪ Possible cost of loss of pooled Right to Buy receipts – not possible to monetise. **Total = £12.3bn**	▪ Efficiency savings due to ability to plan long-term and optimise the cycle of repairs and replacements planned over 30 years. Due to reduced volatility in system. Est. NPV £2.6bn (50 per cent of SF savings). ▪ Improvements to quality of life, health and work opportunities – not possible to be monetised. ▪ Homes are maintained to Decent Homes standard, saving need for large separate capital programme. Est. NPV from £12.2bn. ▪ More ability to build new homes – with subsequent increased income and sales. Not possible to accurately monetise and allocate to change to housing finance system. **Total = £14.8bn** + improvement to quality of life. (range £13.9bn to £18.8bn)
Self-financing model Option 2 **Net Benefit £5.1bn** Est. range (£3.4bn to +£10.1bn)	▪ Increased management and maintenance, major repairs - £700m per year for 30 years – NPV £12.3bn. ▪ Cost of implementing new system. Business plan. Estimated £32.4m. (based on £180,000/LA) ▪ Cost of rescuing failing authority – not possible to cost. ▪ Cost to possible debt re-distribution – not possible to monetise. ▪ Possible cost of loss of pooled Right to Buy receipts. **Total = £12.3bn** + cost of rescuing failing LAs	▪ Efficiency savings due to ability to plan long-term and optimise the cycle of repairs and replacements planned over 30 years. Est. NPV £5.2bn. ▪ Improvements to quality of life, health and work opportunities – not possible to be monetised. ▪ Homes are maintained to Decent Homes standard, saving need for large separate capital programme. Est. NPV from £12.2bn. ▪ More ability to build new homes – with subsequent increased income and sales. Not possible to accurately monetise and allocate to change to housing finance system. **Total = £17.4bn** + improvement to quality of life (Est. range £15.7bn to £22.4bn)

Sources and details of costs and benefits

Costs

a) Increased management and maintenance costs and major repairs allowance

33. This is based upon research commissioned during the Review of Council Housing Finance (*Evaluation of Management and Maintenance Costs in Local Authorities* (Housing Quality

Network[2]), *Review of the Major Repairs Allowance*[3] (Building Research Establishment)). This research indicated the management and maintenance allowance currently given to local authorities should be increased by 5 per cent and the major repairs allowance should be increased by an average of 24 per cent over 30 years. Together this is the equivalent of an average extra £700m per year cost to the exchequer. This is an average over 30 years; the amount will increase over time from around £500m to over £1bn at the end. See Annex for details of the annual costs and calculation of the NPV.

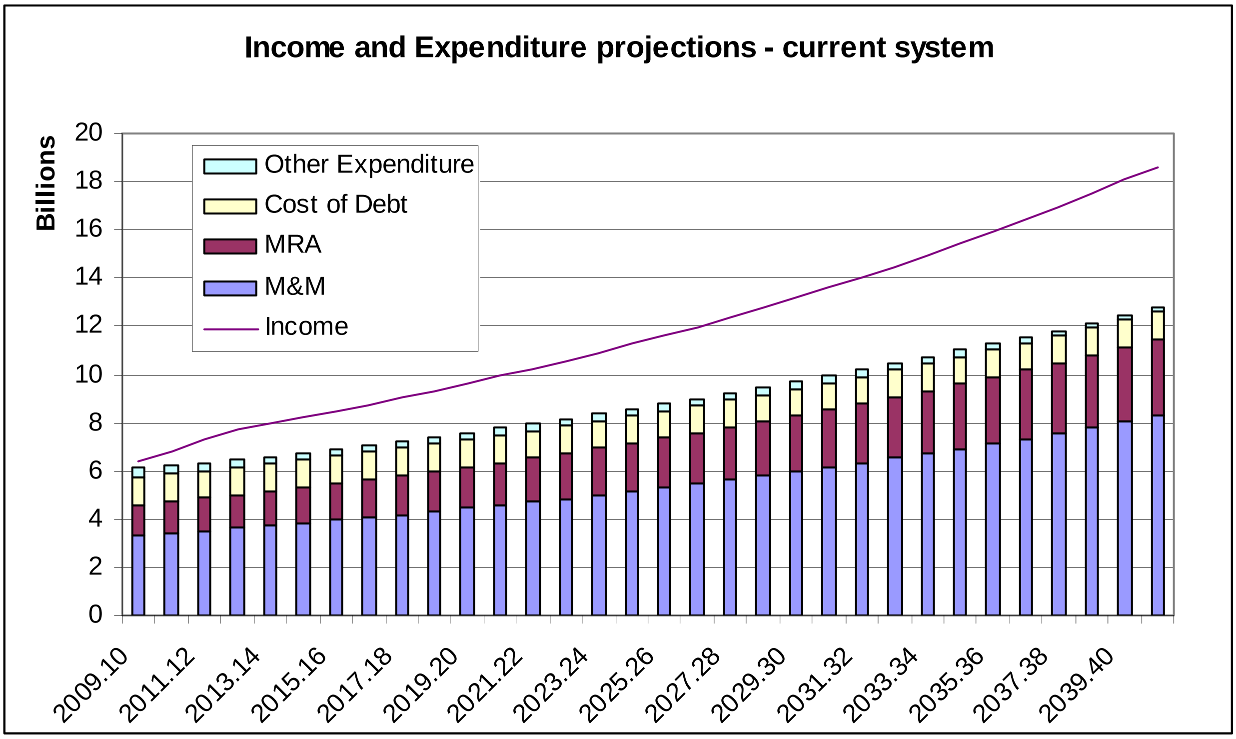
34. However all this money would come from and remain in the public sector. In addition it is complicated by the fact that council housing is a money raising activity through rents so the majority of the increase in cost will be self-funding rather than from some other government source.

35. The £12.3bn is based upon the difference in management and maintenance costs and major repairs allowance between what the current allowance levels would provide over 30 years and the level that the commissioned research suggested these should be uplifted. The research suggests M&M allowances should be increased nationally by 5 per cent and the MRA should be increased nationally by 24 per cent. However further work is needed to determine the costs at the local level.

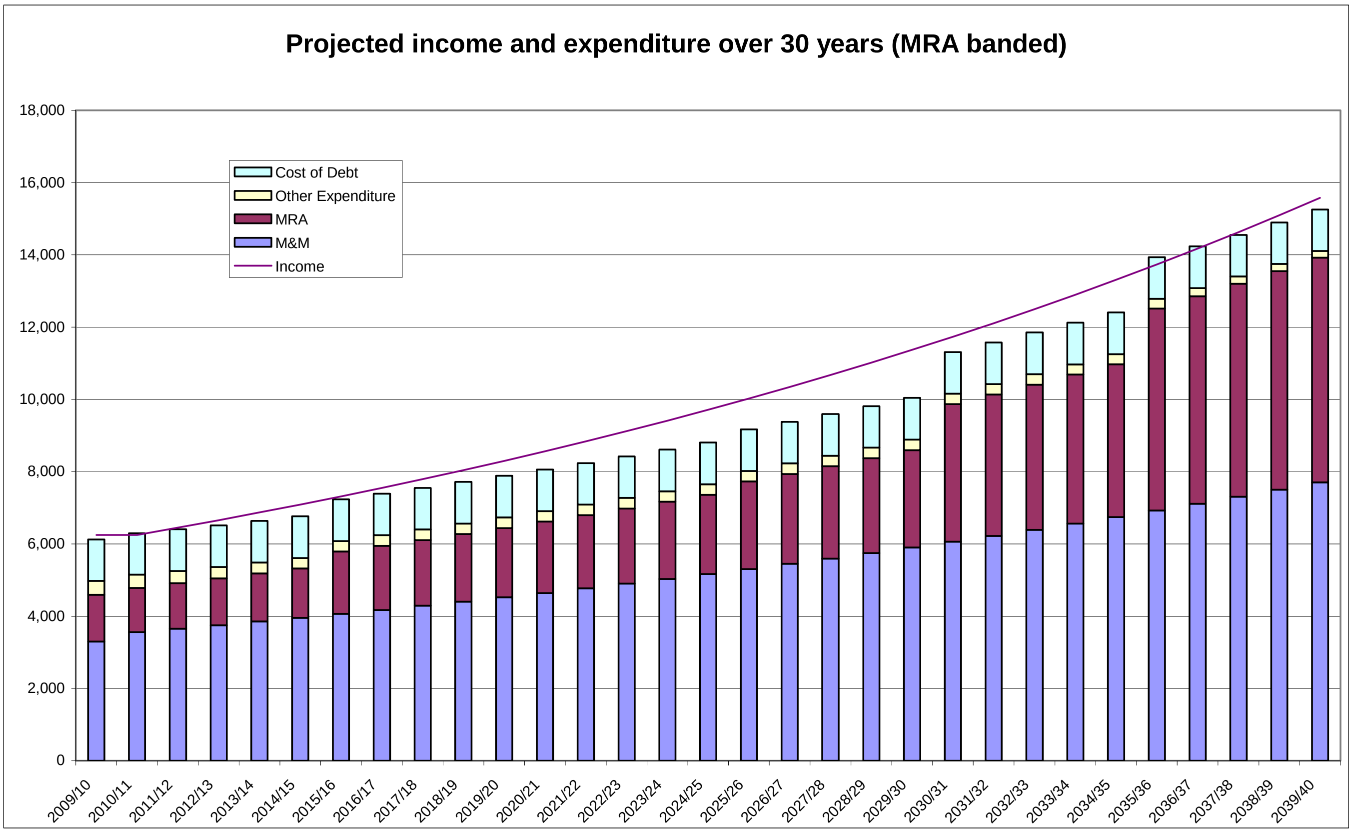
36. The MRA has been evened out so that the same amount is allocated in each of the 30 years. An alternative scenario is for the money to be allocated on the basis of the predicted year that the repairs and money will be needed. This approach would increase the NPV of the costs to £16.5bn.

37. The majority of these extra costs will be self-generated by the system from rental income. Exactly how much depends on decisions made on rent policy and inflation rates. However of this rental income 60 per cent is paid for by housing benefit.

38. The two charts below show the expected income and expenditure over 30 years – firstly if the current funding level were to continue and secondly under an increased level of management and maintenance and major repairs as indicated by the research.



2 CLG research, *Evaluation of Management and Maintenance Costs in Local Authorities*
3 CLG research, *Review of the Major Repairs Allowance*



Do you agree that the cost assumptions associated with increased management, maintenance and major repair spending are fair? Do they represent a real cost?

b) Cost of implementing new system

39. This is an estimate of the increased staff time it would take to implement a new system and the cost of any processes or increased regulation.

40. It is based on information collected for the impact assessment for exempting some local authorities from the HRA subsidy system published by CLG in November 2008[4] as part of the wider assessment for the Housing and Regeneration Act. This estimated a cost of £180,000 per authority for setting up a self-financing system. This is broken down to producing a business plan (£20,000), consulting with tenants/residents (£60,000), and a stock condition survey (£100,000).

41. The information was based upon estimates from 6 local authorities that represented a wide range of local circumstances. The detailed modelling work by the six authorities was based on

updated stock condition surveys. It tests a range of assumptions and sensitivities.

Their work was scrutinised and supported by a group of representatives from a range of housing bodies and other experts in the field, meeting regularly as a contact group.

42. The cost for option 2 on self-financing has used the full £180,000 estimate for a self-financing business plan. The cost would be less for the option 1 as this is an amendment to the current system rather than full self-financing hence the cost of any change is likely to be less. There is not sufficient evidence available to make a robust estimate, we have estimated the cost will be 50 per cent (£90,000) of full self-financing.

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4 http://www.communities.gov.uk/publications/housing/housingregenactimpactassess

43. The assumption is that 180 authorities will be subject to the reform, giving a total of £16.2m for option 1 and £32.4m for option 2.

Do you agree that the assumptions on the cost of implementing a new system are fair? Do the 6 local authorities used in the evidence base provide a representative sample for all?

d)Non-monetised costs.

44. There are also several costs that there is insufficient information to monetise:

- Cost of debt re-distribution amongst local authorities. There is likely to be a small cost to the early repayment of debt in some local authorities. This will depend on the details of the debt agreement and it is not possible at this stage to cost how much this will be. In addition there is likely to be a small cost to debt-free authorities to set up a process for managing debt they did not previously hold.
- There is a possible cost to the loss of capital receipts from right to buy sales. Previously 75 per cent of the receipts have been pooled and re-distributed to areas of most need, by keeping the receipts locally some areas, the money may not be allocated most efficiently to the areas of most need.
- For option 2 there is a potential cost of rescuing failed authorities if the new system does not work, or unforeseen circumstances occur that make the system unsustainable. The Modelling carried out during the review suggests this is unlikely to happen but it is not impossible.

Are there any other unmonetised costs that should be considered?

Benefits

a) Efficiency savings due to the ability to plan long-term and optimise the cycle of repairs and replacements planned over 30 years.

45. In the current HRA subsidy system the volatility of the annual determination cycle does not allow long-term spending plans as authorities are unsure how much money they will have from year to year. Under any of the proposed models there will be greater ability to plan into the future and as such works can be carried out at the optimal time and with the most efficient contracts in place. There is the possibility of savings of 10-20 per cent.

46. For option 2 the estimated benefit will be £5.2bn over 30 years based upon evidence collected for the impact assessment of exempting some local authorities from the HRA subsidy system published in November 2008. As in the costs above this was based on modelling of six local authorities and the estimated benefit they could accrue from the ability to plan long-term. The average NPV savings per local authority over 30 years was £29.1m, which for an estimated 180 authorities over 30 year is equal to £5.2bn. The estimated range has been calculated from a low of £20m savings per authority to a high of £40m, it is difficult to predict accurately how much saving there will be.

47. As with the costs the savings are likely to be lower for option 1 than a full self-financing model. Under this model there are still 3-5 year settlement periods which despite providing more certainty that the current system will not match self-financing. Again there is no robust evidence on how much the potential savings will be for the model. An assumption has been made that the saving will be 50 per cent (£2.6bn) of a full self-financing model. Option 1 is

likely to have lower savings since some authorities will still need to rely on a positive subsidy and hence will not be able to plan with certainty until that has been confirmed.

Do you agree that the assumptions on efficiency savings are fair? Are the six local authorities on whom the evidence is based representative?

b) Maintaining homes to a Decent Standard

48. The uplifted allowances will have the primary impact of maintaining homes to a decent standard. If current funding levels were forwarded into the future the homes would gradually fall into a state of disrepair which would eventually either become unfit for habitation or would require a separate large capital program to bring them up to standard.

49. By 2010 the current Decent Homes program will have cost over £40bn bringing more than one million homes up to a decent standard. It is not unreasonable to estimate than a program of a similar size would be required in 30 years time to bring the homes back up to standard if allowances are maintained at their current level. For the estimates in this assessment we have spread this £40bn over 10 years from year 30 to year 40. The NPV of such savings is £12.2bn, calculations are included in the annex.

50. It is likely that the cost in the future could be even higher than the £40bn of the current decent homes program. In the future with a bigger population there are likely to be more homes to work on, and there is also likely to be a higher expectation of what a decent home should include. Therefore the estimated range for these saving is from £40bn to £50bn, an NPV of £12.2bn to £15.2bn.

Do you agree with these assumed benefits for maintaining homes at the Decent Standard?

c) Non-monetised benefits for which there is insufficient evidence.

51. Some of the potentially biggest benefits can not be effectively monetised. These include the improvements to quality of life any new model would bring about. An improved housing finance system should improve the quality of the stock, and it should improve affordability of rents. This could lead on to subsequent benefits of improved health, work and education opportunities for tenants and their families. According to Shelter[5], 8 per cent of children living in sub-standard accommodation lose out on a quarter of their schooling, and those living in poor housing are more than twice as likely to suffer from poor health.

52. An improved model for council housing finance would along with other policies potentially increase the ability of councils to build new homes. Councils could benefit from increased rental income and sale proceeds from newly built homes. However it would be difficult to distinguish the impact a new council housing finance model would have on this ability compared to other policies such as funding announced in *Building Britain's Future*[6], the 2009 budget and previous initiatives already in place to exclude new build from the subsidy system[7]. The impact assessment for exempting some local authorities from the HRA subsidy system published by CLG in November 2008 suggested potential benefits of over £50m per authority could be generated from extra rents and sales of new build if the appropriate policies were put in place. Some of that benefit could be achieved through a reformed council housing finance system however it is not possible to quantify how much in comparison to other policies and funding announcements.

[5] www.shelter.org.uk
[6] http://www.hmg.gov.uk/buildingbritainsfuture.aspx
[7] http://www.communities.gov.uk/publications/housing/capitalruleschanges

53. Other potential benefits include better provision of disabled facilities, and more effective leaseholder management.

Are there any other unmonetised benefits that should be considered?

Key sources of evidence

54. There are several sources of evidence that have been vital components in deciding the options available for the review and the likely costs.

Evaluation of management and maintenance costs

55. The review commissioned the Housing Quality Network to evaluate the costs of the landlord business in day to day management and ongoing maintenance. Headline findings were:

- LAs are spending about 5 per cent more on management and maintenance than allocated in their allowances
- this difference is made up by a gap of 8 per cent on management compared to the allowance and 3 per cent on maintenance
- expenditure on management in local authorities is some 5 per cent lower overall than comparable expenditure in the RSL sector
- however maintenance expenditure is 4 per cent more than in large scale voluntary transfer RSLs (the most direct comparators)
- efficiency savings in core management costs (e.g. rent collection, allocating homes etc), and increasing demands from tenants and government have led to an increasing amount of spend of management costs on traditionally ‘non-core’ services (e.g. anti-social behaviour activities, helping tenants get into work etc). It is estimate that these ‘non-core’ activities now make up approximately 40 per cent of all management costs

56. From these findings the review concluded that the need to spend on management and maintenance was 5 per cent higher than current allowances. It is these costs that have been used in each of the options above. Further work will be needed to assess the costs at an individual local authority area before any new model can be implemented.

Review of the major repairs allowance

57. As part of the review the Building Research Establishment carried out a review of the current major repairs allowance and whether it was delivering sufficient funding to maintain homes to a decent standard over a 30 year period. It looked at the cost of maintaining homes to at least the current decent homes standard and included additional aspects such as maintenance of lifts and the external environment. Headline findings were:

- the current MRA is out of date. Both the lifetimes used, the assumed costs, and the components included do not reflect current or future needs
- the MRA should be increased by an average of 24 per cent over 30 years. Although the large part of that spending is likely to be needed towards the end of that 30 year period

58. The costs in this paper assume the need to spend is 24 per cent higher than the current allowance. Further work at the local level will be needed before any new model can be implemented.

Rents and service charges

59. Work carried out:

- Analysis of affordability of rents and changes over time – suggested that affordability levels of rents had stayed at about the same level since 2000 compared to both average earnings and the private rented sector. LA rents are about 63 per cent of the level of their market value[8].
- International comparison of rents policies – there are broadly four ways in which social rents are set across Europe each with their pros and cons. Several countries are moving towards a more property based system similar to England.
- Investigation of impact of increasing rent levels, and changing rent formula – 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. There are options for changing the rent formula to an increased bedroom weight as well as updating the values from 1999 to current.

60. What the evidence suggests we should do:

- the principle of similar rents for similar properties should remain in place and rent restructuring should deliver equalisation – it is generally supported by tenants and is delivering rents that are affordable
- but need to consider updating formulae and maintain updating – the formula is based upon 1999 data
- set greater differentials for bedroom numbers – the rent differentials between small and large homes in the social sector are much lower than in private and owner market
- create more flexibility by setting overall local rent envelope - to contain HB bill but allow greater local variation
- greater use could be made of service charges but these ought to be consulted upon with tenants

Debt

61. As part of the review work was commissioned to identify the possible options for dealing with debt and their implications for local authorities. The work developed a model that projects the costs and debt for every local authority over 30 years[9].

62. For successful implementation of the self-financing or the national council housing model debt would have to be moved from its current location and redistributed. Either by taking it into central government and charging a levy or redistributing it amongst local authorities. Either way the redistribution should be on the basis of a tenanted market value – which in effect is the amount of debt each local authority can afford to take on based upon their spending needs over a 30 year period.

Implementation plan

63. Depending on the outcome of this consultation, the Government would wish to move swiftly to have a self financing option up and running. We have already moved to create a self financing mechanism for local authority new build properties.

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[8] CLG research, *Analysis of Rents for the Review of Council Housing Finance*
[9] CLG research, *Analysis of Debt Options*

64. We are making the changes to the revenue and capital rules for new build using powers in the Housing and Regeneration Act 2008 and through secondary legislation. The powers in the 2008 Act allow for individually negotiated agreements between local authorities and central Government to exclude specified stock from the HRA subsidy system. This would not however be appropriate for a national settlement covering all council stock and all local authorities.

65. Implementing a self financing system with debt redistribution for the whole of the council housing stock would require primary legislation. This is because the settlement will have to be a national one, imposed, subject to consultation and it would, in any case be impractical to conduct negotiation with over 200 local authorities. We would aim to conduct as much of the information and practicalities to get a fair debt settlement while legislation was being prepared. Subject to parliamentary time, a self financing system could be legislated for and be in for operation from 2012-13. This would mean that there would need to be a continuation of the HRA subsidy system to 2011-12.

66. Subject to decisions on priorities in the next spending review, it would be possible to move to a position where from 2011-12 local authorities kept for housing the 75% of Right to Buy receipts currently pooled.

Specific impact tests

Competition assessment

Review does not have an impact on competition. Social Housing is not a competitive market.

Small firms impact test

Some of the smallest RSL may be considered small firms. They will be affected by the rental policy however any change will not be substantial.

Legal aid

No immediate legal impact. However if it is decided to increase rents, there could eventually lead to more tenants running up arrears and ending up in court.

Sustainable development

The increased allowances will provide improvements to the environmental standard of the homes. The review also sets out the cost and funding options for further environmental improvements with the aim to almost eliminate carbon emissions from homes by 2050.

Health impact assessment

An improved funding mechanism for council housing will improve the standard of the home which has been shown to have large positive health impacts. According to Shelter, 8 per cent of children living in sub-standard accommodation lose out on a quarter of their schooling, and those living in poor housing are more than twice as likely to suffer from poor health.

Race/disability/gender equality

A key aim of the review is to provide a system that is fair to both the tenant and the taxpayer. This includes people of all races, disability and gender equally. Disabled people may benefit by the clarification of the funding streams available for disabled adaptations. The consultation document will seek views on whether there will be a disproportionate negative or positive impact on any of these groups. If so a full equality impact assessment may follow.

Human rights

The review does not have any human rights implications

Rural proofing

The allowances take account of rural/urban locations and adjust needs accordingly. All areas will benefit from increased allowances.

Specific Impact Tests: Checklist

Type of testing undertaken	***Results in Evidence Base?***	***Results annexed?***
Competition Assessment	Yes	No
Small Firms Impact Test	Yes	No
Legal Aid	Yes	No
Sustainable Development	Yes	No
Carbon Assessment	Yes	No
Other Environment	Yes	No
Health Impact Assessment	Yes	No
Race Equality	Yes	No
Disability Equality	Yes	No
Gender Equality	Yes	No
Human Rights	Yes	No
Rural Proofing	Yes	No

Annexes

Calculation of Net Present Value Figures

a) £12.3bn cost of increasing the allowances

Year		Discount factor	Current Allowance Total (000s) [1]	Uplifted Allowance [2]	Extra cost per year	NPV of extra cost
0	2009/10	1	4,592	4,592	0	0
1	2010/11	0.966184	4,716	5,190	475	459
2	2011/12	0.933511	4,843	5,331	487	455
3	2012/13	0.901943	4,974	5,475	501	451
4	2013/14	0.871442	5,108	5,622	514	448
5	2014/15	0.841973	5,246	5,774	528	444
6	2015/16	0.813501	5,388	5,930	542	441
7	2016/17	0.785991	5,533	6,090	557	438
8	2017/18	0.759412	5,683	6,255	572	434
9	2018/19	0.733731	5,836	6,423	587	431
10	2019/20	0.708919	5,994	6,597	603	428
11	2020/21	0.684946	6,156	6,775	619	424
12	2021/22	0.661783	6,322	6,958	636	421
13	2022/23	0.639404	6,493	7,146	653	418
14	2023/24	0.617782	6,668	7,339	671	415
15	2024/25	0.596891	6,848	7,537	689	411
16	2025/26	0.576706	7,033	7,740	708	408
17	2026/27	0.557204	7,223	7,949	727	405
18	2027/28	0.538361	7,418	8,164	746	402
19	2028/29	0.520156	7,618	8,384	767	399
20	2029/30	0.502566	7,824	8,611	787	396
21	2030/31	0.485571	8,035	8,843	809	393
22	2031/32	0.469151	8,252	9,082	830	390
23	2032/33	0.453286	8,475	9,327	853	387
24	2033/34	0.437957	8,703	9,579	876	384
25	2034/35	0.423147	8,938	9,838	899	381
26	2035/36	0.408838	9,180	10,103	924	378
27	2036/37	0.395012	9,428	10,376	949	375
28	2037/38	0.381654	9,682	10,656	974	372
29	2038/39	0.368748	9,944	10,944	1,001	369
30	2039/40	0.356278	10,212	11,240	1,028	366
Total						**12,319**
	[1] Current level inflated by 2.5% per year (GDP inflator assumption)					
	[2] Assumed 5% increase in M&M, 24% increase MRA					

b) Efficiency savings

30 year NPV of efficiency savings per local authority - £29.1m, based upon a pilot study of six local authorities during the original self-financing project in 2008.

Estimated 180 local authorities will stay within the system giving a total of 29.1*180 = £5.2b.

The range has been calculated from an estimated low of £20m per authority to a high of £40m per authority. For option 2 this gives a range of £3.6b to £7.2b. For option 1 the savings have been estimated as 50% of option 2.

c) Benefits of maintaining homes to a decent standard

If homes are not maintain to a decent standard, there will need to be a large capital expenditure program in the future to bring them back to a standard fit for habitation. For this paper we have assumed a £40bn programme (the same spend as the Decent Homes program) spread over 10 years from year 30 to year 40. This gives an NPV of £12.2bn.

	Year	Discount Rate	Capital spend (millions)	NPV of Capital spend (millions)
31	2040/41	0.345901	4000	1383
32	2041/42	0.335827	4000	1343
33	2042/43	0.326045	4000	1304
34	2043/44	0.316549	4000	1266
35	2044/45	0.307329	4000	1229
36	2045/46	0.298378	4000	1193
37	2046/47	0.289687	4000	1158
38	2047/48	0.281249	4000	1124
39	2048/49	0.273058	4000	1092
40	2049/50	0.265105	4000	1060
			Total	12,156

We have estimated a range for this benefit from £40bn to £50bn spread over 10 years giving a NPV range of £12.1bn to £15.2bn.