RESEARCH PAPER 98/69
22 JUNE 1998

Rent levels, affordability and housing benefit

There is a general consensus amongst housing commentators that for the Government's Welfare to Work initiative to succeed policies will need to address the work disincentive effects of high social sector rent levels and the current housing benefit system.

This Research Paper explains why rents have risen in recent years and discusses some options for reform to tackle high rents and housing benefit dependency.

Wendy Wilson

SOCIAL POLICY SECTION

Bryn Morgan

SOCIAL AND GENERAL STATISTICS SECTION

HOUSE OF COMMONS LIBRARY

Recent Library Research Papers include:

List of Recent RPs

98/68	'Age of Consent' for Male Homosexual Acts	19.06.98
98/67	Unemployment by Constituency - May 1998	17.06.98
98/66	Council Tax Capping in 1998/99	16.06.98
98/65	Northern Ireland: The Release of Prisoners under the *Northern Ireland (Sentences) Bill* Bill 196 of 1997-98	15.06.98
98/64	GDP per capita in OECD countries: the UK's relative position	04.06.98
98/63	Bovine Tuberculosis	01.06.98
98/62	The *Registration of Political Parties Bill* Bill 188 of 1997-98	01.06.98
98/61	Parliamentary Pay and Allowances: Current Rates	18.05.98
98/60	Unemployment by Constituency: Welfare-to-Work Groups - April 1998	13.05.98
98/59	The local elections of 7 May 1998 and the London Referendum	12.05.98
98/58	Unemployment by Constituency - April 1998	13.05.98
98/57	Northern Ireland: political developments since 1972	11.05.98
98/56	EU Enlargement: The Financial Consequences	01.05.98
98/55	EU Enlargement: The Political Process	01.05.98
98/54	Economic Indicators	01.05.98

Research Papers are available as PDF files:

- *to members of the general public on the Parliamentary web site,*
  URL: ***http://www.parliament.uk***
- *within Parliament to users of the Parliamentary Intranet,*
  URL: ***http://hcl1.hclibrary.parliament.uk***

Library Research Papers are compiled for the benefit of Members of Parliament and their personal staff. Authors are available to discuss the contents of these papers with Members and their staff but cannot advise members of the general public.

CONTENTS

I Summary

The November 1997 Pre-Budget report stated that 'the Government is committed to streamlining and modernising the tax and benefit system to fulfil the objectives of promoting work incentives, reducing poverty and welfare dependency and strengthening family and community life.' Several elements of this strategy have already emerged, such as the national minimum wage, the working families tax credit, the reform of the National Insurance system and financial support for child care costs. Potential changes to the housing benefit scheme are yet to be unveiled.

Housing commentators have noted that the issue of rent levels, coupled with a new definition of affordability, have been missing from this debate. It has been suggested in some quarters that this omission could prove to be 'an achilles heel for New Labour's ambition'.

Rent levels in both the private and social rented sectors rose substantially in the late 1980s and early 1990s. These rises were not accompanied by equivalent rises in tenants' incomes; particularly for the occupants of social housing. Just over two-thirds of these tenants are in receipt of housing benefit; expenditure on housing benefit in 1996/97 reached £11.4 billion although it is forecast to fall slightly in real terms in 1998/99. The current system of housing benefit, under which claimants experience sharp withdrawals of benefit when their income rises above income support levels, is widely recognised as having certain work disincentive effects.

Attempts have been made to limit rent increases, mainly spurred on by the rising cost of housing benefit, but there is no agreed definition of an affordable rent or how affordable rent levels can be achieved. There is a general consensus in the housing world that in order for Welfare to Work to succeed it will be necessary to tackle the work disincentive effects of the current housing benefit system and to ensure affordable rent levels in social housing.

This paper explains why rent levels have increased and the efforts that have been made to curb them. It discusses the issue of affordability and goes on to look at the implications of rent cuts for social landlords. Finally, the paper presents some of the options that have been put forward for the reform of housing benefit.

II Rent level trends

A. Housing associations/Registered Social Landlords (RSLs)

Reliable data on housing association rents for all tenants in England have only been available since 1991/92. The available data, collected by the Housing Corporation, are shown in the table below.

Table 1

Average weekly housing association rents: England

	£ per week	£ per week at 1996/97 prices	*% increase over previous year in real terms*	Rent as percentage of average earnings
1991/92	30	34		9%
1992/93	34	38	12%	10%
1993/94	38	41	9%	11%
1994/95	41	43	4%	11%
1995/96	44	45	5%	12%
1996/97	47	47	4%	12%

Sources: Housing Corporation
New Earnings Survey

- housing association rents by 38% in real terms over the period 1991/92 to 1996/97
- increases since 1994/95 have been lower than those seen in 1992/93 and 1993/94

The table also shows rents increasing as a percentage of average earnings[1]. As the average incomes of households in housing association accommodation are below the average for all tenures, the proportion of their incomes spent on rent is higher than that shown in the table. In 1996/97, for households not receiving housing benefit, average weekly rent represented around 18% of household income[2]. Including households receiving housing benefit average weekly rent after benefit represented 15% of income compared with 13% in 1993/94.[3] Affordability will be discussed in more detail in chapter V.

---

1 As measured by average weekly male full-time earnings on adult rates at April
2 Income of household head and partner, excluding housing benefit payments
3 *Survey of English Housing*

Table 2 shows data from the National Housing Federation's CORE (continuous recording) system on average assured and fair rents in England. These data show average rents for properties let in each financial year, rather than for the whole stock. For the latest year these are based on around 100,000 lettings. These include both lettings of purpose-built or rehabilitated new lettings and relets of existing stock. Housing for Wales (Tai Cymru)[4] collects data using a similar system and these are also shown in the table.

Table 2

Housing Association Assured Rents

	1989/90	1990/91	1991/92	1992/93	1993/94	1994/95	1995/96	1996/97	1997/98
£ per week									
England[(a)]									
New lets	*29.40*	*36.70*	*43.30*	*48.00*	*52.30*	*54.00*	*57.00*	*59.30*	*59.80*
Relets	*24.20*	*27.40*	*31.80*	*36.40*	*39.50*	*42.00*	*44.70*	*47.40*	*49.30*
All lettings	25.90	30.00	35.30	41.10	45.10	46.50	48.90	50.60	51.90
Wales[(b)]	26.00	30.70	34.60	39.60	42.50	43.40	42.20	42.40	41.90
£ per week at 1997/98 prices									
England[(a)]									
New lets	*39.80*	*45.30*	*51.00*	*54.80*	*58.70*	*59.00*	*60.30*	*61.30*	*59.80*
Relets	*32.70*	*33.80*	*37.40*	*41.50*	*44.30*	*45.90*	*47.30*	*49.00*	*49.30*
All lettings	35.00	37.00	41.60	46.90	50.60	50.80	51.80	52.30	51.90
Wales[(b)]	35.20	37.90	40.80	45.20	47.70	47.50	44.60	43.80	41.90
% change real terms change over previous year									
England[(a)]									
New lets		14%	13%	7%	7%	1%	2%	2%	-2%
Relets		*3%*	*11%*	*11%*	*7%*	*4%*	*3%*	*4%*	*1%*
All lettings		*6%*	*12%*	*13%*	*8%*	*0%*	*2%*	*1%*	*-1%*
Wales[(b)]		8%	8%	11%	6%	-1%	-6%	-2%	-4%

Notes: (a) 1997/98 figure is for first nine months
(b) 1997/98 figure is for first six months

Sources: *National Housing Federation*
Housing for Wales (Tai Cymru)
Housing Finance Review 1997/98, Steve Wilcox, Joseph Rowntree Foundation

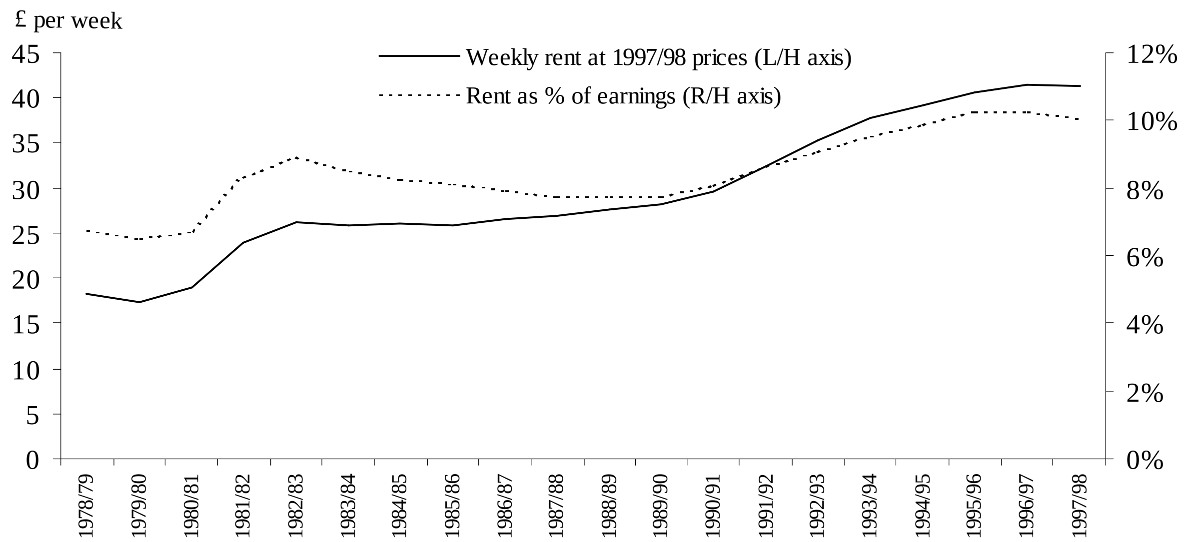
[4] The welsh equivalent of the Housing Corporation.

The table shows that between 1989/90 and 1992/93 average assured rents for new lettings increased by around 50% in real terms in England and by over 30% in Wales. However, since 1993/94, assured rents have fallen in real terms in Wales, and have increased at a much slower rate in England.

B. Local authority

Chart 1 and table 3 show the trend in local authority rents in England since 1978/79.

Chart 1: Local authority average weekly rents



- Local authority rents more than doubled in real terms between 1978/79 and 1997/98 with the largest increases occurring between 1980/81 and 1982/83 and between 1990/91 and 1993/94.

- The table also shows how rents have increased as a proportion of average earnings, from 7% in 1979/80 to 10% in 1997/98.

As with housing association tenants, average incomes for households in local authority accommodation are well below the national average. In households not receiving housing benefit, the average rent in 1996/97 represented around 18% of the average household income. For those households receiving benefit, average rent after benefit was around 11 of income. For all local authority tenants, the rent-to income ratio, after housing benefit, was around 15%. In 1993/94, the rent-to-income ratio for local authority tenants was 13%.[5]

Table 3

Average local authority rents in England: 1978/79 to 1997/98[(a)]

	£ per week	£ per week at 1997/98 prices[(b)]	*% increase over previous year in real terms*	Number of local authority dwellings (thousands)
1978/79	5.90	18.30		5,115
1979/80	6.50	17.40	*-5%*	5,140
1980/81	8.20	18.90	*9%*	5,119
1981/82	11.50	23.90	*26%*	5,118
1982/83	13.60	26.20	*10%*	4,886
1983/84	14.00	25.90	*-1%*	4,763
1984/85	14.80	26.00	*0%*	4,670
1985/86	15.60	25.90	*0%*	4,584
1986/87	16.50	26.50	*2%*	4,504
1987/88	17.40	26.90	*2%*	4,403
1988/89	19.00	27.70	*3%*	4,254
1989/90	20.90	28.20	*2%*	4,081
1990/91	23.90	29.50	*5%*	3,943
1991/92	27.60	32.50	*10%*	3,880
1992/93	30.80	35.20	*8%*	3,810
1993/94	33.70	37.80	*7%*	3,759
1994/95	35.80	39.10	*3%*	3,696
1995/96	38.40	40.60	*4%*	3,651
1996/97	40.20	41.50	*2%*	3,619
1997/98	41.20	41.20	*-1%*	3,604

Notes: (a) Rounded to nearest 10p
(b) Deflated using Retail Prices Index

Sources: HC Deb 20 December 1995 c1241w
HC Deb 24 April 1998 c708w
DETR

In Wales, local authority rents have increased slower than in England. At April 1989 rents in Wales were 8% higher than in England but by April 1997 they were 6% lower.[6]

5 Survey of English Housing
6 *CIPFA Rents Statistics at April 1997* and earlier editions

C. Private sector

Table 4 shows mean private sector rents by type of letting in England in 1988, 1990 and financial years from 1993/94.

Table 4

Average private rents by type of letting: England: 1988-1996/97

	Assured		Regulated		No access	Resident	No	**Total**
	Assured	Assured shorthold	With registered rent	Without registered rent	to public	landlord	security	
£ per week								
1988	..	..	18	33	28	22	26	**27**
1990	58	63	24	33	28	33	28	**40**
1993/94	60	82	31	32	43	40	..	**61**
1994/95	62	83	36	35	42	45	..	**65**
1995/96	66	91	40	37	34	44	..	**70**
1996/97	66	94	42	36	62	46	..	**76**
£ per week at 1996/97 prices (a)								
1988	..	..	26	47	40	32	37	**39**
1990	71	77	29	40	34	40	34	**49**
1993/94	65	89	34	35	47	43	..	**66**
1994/95	66	88	38	37	44	48	..	**69**
1995/96	68	93	41	38	35	45	..	**72**
1996/97	66	94	42	36	62	46	..	**76**

Notes: (a) Adjusted to 1996/97 prices using all items RPI

Sources: 1988 and 1990 Private Renters' Surveys, OPCS
Housing in England: 1996/97 and earlier editions, ONS

Between 1988 and 1996/97 average private sector rents almost doubled in real terms. Between 1988 and 1993/94, the average annual real terms increase was around 12%, compared with 5% between 1993/94 and 1996/97. Looking at the increases within individual letting groups, it is interesting to note that in none of them has the increase since 1990 been as great as in that of the overall average. This is because of the increase in the proportion of tenants covered by assured tenancies which have the highest rents of the groups shown. Table 5 shows the change in the number of tenants by type of letting.

Table 5

Private renting tenancies by type of letting: England: 1988 to 1996/97 Thousands

	Assured	Regulated	Not accessible to public: Rented	Not accessible to public: Rent free	Not accessible to public: Total	Resident landlord	No security	Protected shorthold / pre-1989 assured	**Total**
1988[(a)]	0	1,070	240	270	510	110	60	60	**1,810**
1990[(a)]	500	590	230	250	480	90	90	40	**1,790**
1993/94[(a)]	1,199	407	146	230	375	73	22	0	**2,077**
1993/94[(b)]	1,204	407	146	230	375	158	22	0	**2,166**
1994/95[(b)]	1,244	311	187	244	431	181	30	0	**2,197**
1995/96[(b)]	1,319	272	204	223	428	209	26	0	**2,254**
1996/97[(b)]	1,406	242	193	223	417	198	18	0	**2,280**

Notes: (a) Excludes lodgers forming part of owner-occupied or social renting households
(b) Includes all lodgers

Sources: 1988 and 1990 Private Renters' Surveys, OPCS
Housing in England: 1996/97 and earlier editions, ONS

Table 6 shows the change in private sector rents since 1988 by region.

Table 6

Private Sector rents by region
Mean weekly rent for all tenancies paying rent

	1988[(a)]	1990[(a)]	1993/94	1994/95	1995/96	1996/97
The North	20	28	46	46	58	56
The Midlands	20	27	43	51	50	54
London	40	61	93	95	101	122
Rest of the South	27	40	62	64	65	72
England	27	40	62	65	70	76

Notes: (a) Taken from OPCS Private Renters Surveys.

Sources: Housing and Construction Statistics: 1984-1994
Survey of English Housing: 1996/97 and earlier editions
DETR HDS division

Rents in London have increased more than threefold since 1988. The increases in the other regions are lower and are broadly similar to each other at between 160 and 180 per cent.

D. Conclusions

This chapter looked at trends in overall average rent levels in the three rented sectors. The period of the late 1980s and early 1990s saw significant real terms increases in rents in all sectors. In particular, average rents in the private sector increased by over 70% in real terms between 1988 and 1993/94.

In 1991/92, the first year when average rent figures for all housing association tenancies were available, rents were around £30 per week, a similar level to those of local authority dwellings. By 1996/97, housing association rents were around £47 compared with £40 for local authority dwellings. It is clear that at least until the last few years, housing association rents have increased more rapidly than local authority rents. Indeed, there is some evidence to suggest that in some areas, particularly the North, housing association rents are higher than those in the private sector.[7]

The reasons underlying these increases will be looked at in chapter III.

---

[7] Joseph Rowntree Foundation, *Housing Finance Review 1997/98*, p.152

III Why rents have increased

A. Housing associations/RSLs

1. Background

A central theme of the previous Government's housing policy from the late 1980s was the development of housing associations (now also known as registered social landlords), as opposed to local authorities, as the main providers of new social housing for rent. The *Housing Act 1988* introduced a financial regime for associations under which new development is financed by a mixture of public and private sector investment; the tenancies thereby created are free from rent controls. The aim of this regime was to increase the number of homes developed for any given level of public expenditure and to create incentives for associations to deliver housing and services in the most cost effective manner.

Prior to 1989/90, under the *Housing Act 1974*, associations received capital finance for new development in the form of a single grant (housing association grant)[8] payable on the completion of a project once the final out-turn costs were known. The rents on these developments were 'fair rents' set by an independent local Rent Officer. The income from each project was determined by calculating annual rental income net of service charges, less an allowance for voids and bad debt, and net of management and maintenance allowances. An annuity factor was then applied to the net rental income to calculate the loan it would service at a fixed interest rate over a period of 60 years for new build and 30 years for rehabilitation; this was known as the residual loan. The amount of HAG paid was the difference between the qualifying capital costs and the residual capitalised loan. Under this system HAG payments averaged over 85 per cent per scheme; scheme costs were controlled through a system of cost limits.

The regime imposed minimal risks on associations over and above those normally associated with the development process; as Helen Cope pointed out in *Housing Associations Policy and Practice*,[9] the cushioning of associations from risk in order to promote their success and expansion was a central objective of the capital funding system when introduced in 1974.

The residual HAG regime had its critics. It was argued that the lack of risk involved gave associations no incentive to pursue value for money objectives. The fact that most cost

8 HAG, now known as Social Housing Grant (SHG)

9 1990 edition

overruns on projects would be met by HAG, combined with the existence of revenue deficit subsidies, left associations open to the charge that they were unduly protected from the need to exercise proper financial control over their activities. In their defence associations argued that the generous subsidy system was justified by the need to produce housing at rent levels within the reach of their traditional client groups and that the Housing Corporation, through its system of cost limits,[10] ensured that resources were not squandered. Associations also argued that HAG was really determined by rental income and management and maintenance allowances, both of which were fixed independently by rent officers and the Department of the Environment (DoE) respectively, leaving associations with only limited control over the level of HAG required.

In 1987 the DoE published a consultation paper, *Finance for Housing Associations: The Government's Proposals*, which set out the following principal objectives:

- To increase the volume of housing that could be provided for a given amount of public money by mixing public and private finance;
- To increase value for money in the funding of housing association development by requiring associations to take on a greater proportion of the development risks;
- To target grant accurately whilst still taking into account scheme costs and ensuring that rents are kept within the means of tenants in low paid employment;
- To simplify the procedures and administrative requirements of the funding system.

The *1988 Housing Act* introduced the new financial regime for associations that was aimed at achieving the above objectives.

2. The new capital funding system

The 1988 Act ended residual HAG and introduced a system of pre-determined grant rates fixed at the outset of a scheme rather than at completion. This effectively fixed the amount of public capital subsidy that associations could receive. Scheme cost overruns and any scheme deficits must now be met from rents or reserves and not, as previously occurred, from public grants. These changes placed associations in a more commercial environment by making them responsible for the risks of development.

The Act also introduced 'mixed funding' under which a proportion of scheme costs must be met by private finance. Initially this percentage was set at an average of 25 per cent

[10] Total Indicative Costs (TICs)

nationally, the remainder being made up of 75 per cent HAG. Movements in the average HAG/SHG rate since the introduction of the new regime are set out below:

Year	Average headline HAG/SHG rate (%)
1989/90	75
1990/91	75
1991/92	73
1992/93	72
1993/94	67
1994/95	62
1995/96	58
1996/97	56
1997/98	56
1998/99	54

To enable associations to attract private investment and bear the risk of future cost overruns the Act abolished the regulation of rents on new lettings after 15 January 1989. Since then new association tenancies have been let on an assured basis and the rents have been set by associations free from external interference in the form of rent officer decisions. The rent levels on pre-15 January 1989 housing association lettings (secure tenancies) are discussed with private sector rents on page 22 below.

In addition, the Act ended public underwriting of future major repairs funding by abolishing major repair grants on new developments and making associations responsible for funding these repairs from rent. In so doing it was argued that this has created further upward pressure on rent levels.

The affordability of rents that the new financial regime was likely to produce became a crucial issue in discussions between the National Housing Federation[11], Housing Corporation and the DoE. Briefly, the housing association movement expressed concern over four features of the new regime that it believed would result in rent increases:

- The reduction in average grant rates and the need to raise a higher proportion of finance from private sources;
- The need to make provision for major repairs;
- The need to cover any cost overruns or unforeseen costs;

[11] Now the National Housing Federation (NHF)

- The likely need to mix a variety of low start and conventional loans in order to spread risks, with the result that cost rents would be higher than those produced by the Corporation's grant model which assumed all private funding to be on a deferred interest basis.

The movement lobbied unsuccessfully for the Bill to replace fair rents with a right to a non-market affordable rent:[12]

> 'The Federation believes that there are firm reasons why the abolition of the current right to fair rents should be replaced by a new right to non-market, affordable rent levels. These rents would establish a ceiling which housing associations could charge for new lettings and for re-lets. Such ceilings would relate to the known incomes of those likely to occupy the properties. We already have detailed information about incoming association tenants (and, indeed, hope to undertake another Tenant Census in early 1988 to ensure the results of our 1985 Survey are still valid).'

Although the Government made it clear during consultation over the Bill that rent levels were to be kept 'within the reach of those in low paid employment',[13] housing commentators were concerned that, in the absence of an accepted definition of affordability, tenants would find themselves unprotected from future financial pressures. The 1988 Act was passed with the debate over its impact on rent levels unresolved.

3. Developments under the new financial regime

Housing associations/RSLs have seen a reduction in the average HAG/SHG rate from 75% in 1989/90 to 54% in 1998/99. The previous Government justified cuts in the grant rate on the basis of lower construction costs.[14] When referring to the 1995/96 HAG rate reduction the then Housing Minister, David Curry, stated that because of interest rates and building costs being lower than previously forecast, this lower grant rate should not lead to rent increases for housing association tenants. It was also frequently pointed out that associations consistently bid at <u>below</u> the headline grant rate and overbid for the resources available.

In November 1992 the DoE's public expenditure announcement set out the then Government's objective of reducing grant rates to 60% in 1994/95 and 55% in 1995/96. The Government's objective in reducing the average HAG rates was: 'to maximise the number of new homes that

---

[12] *Rents, Risks and Rights,* NFHA, 1987
[13] William Waldegrave, Speech in Warrington, 6 June 1988
[14] HC Deb 17 October 1994 cc 18-19W

housing associations are able to provide from the available public resources.'[15] In response the NFHA launched a National Affordability Campaign in March 1993 in order to present its case for maintaining average grant rates at at least their current level (67% at that time). The NFHA predicted the following results from the achievement of Government's grant rate objectives:[16]

- An increase in 'headline' rents of 70% over four years with a 55% grant rate;
- A growth in housing benefit dependency and a deepening of the unemployment trap for housing association tenants;
- Increased security requirements from private lenders as associations' revenue stream becomes more dependent on housing benefit.

In the event the 1994/95 headline grant rate was set at 62%. Announcing the grant rate Sir George Young, the then Minister for Housing, said:[17]

> 'The Government announced last year an objective of reducing the average HAG rate for 1994/95 to 60% in order to increase the leverage in of private funds and the total of new houses that could be made available from the Corporation's ADP.[18] I have made clear on numerous occasions that our decision would be based on the likely impact on the affordability of housing association homes and the availability of private finance.
>
> I have considered very carefully advice from the Housing Corporation on the trends in procurement and other costs and on the availability of private finance, as recommended by the Environment Select Committee. I have also looked at their advice on the capacity of housing associations to reduce the impact of lower grant rates on future affordability by pooling rents across their stock, and by the likely impact of the new criteria introduced for the 1994/95 bidding round. In the light of these factors, I believe that by setting a ceiling of 62% for the average HAG rate, associations will continue to be able to develop the substantial programme of affordable housing for which we have made provision.'

After taking power, the new Labour Government announced a further reduction in the headline grant rate for 1998/99 from 56% to 54%. In a letter to the Housing Corporation Chairman, Peter Cooke, Hilary Armstrong explained the thinking behind this move:[19]

> 'Although rents have been taken into account when allocating ADP resources in the last two years, rent levels on new schemes funded through the ADP are substantially higher than the average level of rents charges by RSLs on their existing properties. Rents on new schemes have now reached a level where it is questionable whether they are affordable to those in low

[15] HC Deb 15 July 1993 c.590W
[16] NFHA, *The Affordable Housing Campaign: The next step*, 1993
[17] DoE press notice 1993/537, 4 August 1993
[18] Approved Development Programme
[19] DETR press notice ENV/321, 7 August 1997

> paid employment without assistance from Housing Benefit. It is one of the Government's key priorities to reduce benefit dependency and the level of rents charged by RSLs will be an important factor in achieving this.
>
> This year we have a significant opportunity to achieve a reduction in the rents proposed on schemes put forward for the 1998/99 ADP without sacrificing anticipated outputs from the programme. Over the past year the cost of private finance faced by RSLs has fallen substantially as a result of the reduction in long-term interest rates. Last year the average headline grant rate for social housing grant under the 1997/98 ADP was 56%. The Corporation's Grant Rate model indicates that after allowing for lower debt funding costs and other changes during the year, this would now be equivalent to an average headline grant rate of about 52%.
>
> Because of the priority which I attach to rents, I have decided that instead of reducing the headline grant rate to 52%, the reduction should be limited to 54%. This will allow a significant part of the benefit from lower private funding costs to be taken in lower rents on new ADP schemes than would otherwise be the case. A 54% headline grant rate should allow rents on schemes submitted for grant in the 1998/99 ADP to be held, on average, to no more than 3% above the average level of rents on schemes completed during 1996/97. As the first letting for schemes approved in the 1998/99 ADP round will occur around the third quarter of 1999, this in effect means that, after allowing for inflation, I am looking for a reduction in the average level of rents charged on new ADP schemes over a three year period from 1996/97 of about 4% in real terms. An initiative along these lines will make a useful contribution to our objective of achieving affordable rents and reducing benefit dependency. We will be giving further consideration to these issues in the Comprehensive Spending Review.
>
> I would therefore like the Corporation to set firm benchmarks for rents within the ADP bidding process, and for subsequent scheme appraisals, in order to deliver this target. The results of the Corporation's modelling suggest that it should be possible to achieve this constraint on rents whilst at the same time achieving, or even slightly exceeding, our current projection of the number of new units of social housing which will be delivered through the 1998/99 ADP.

This further cut in the grant rate was not welcomed by the housing association movement. It was noted that the new Government had met the previous Government's target of reducing the rate below 55% and, despite the Minister's assurances, the movement predicted that rent levels would continue to rise and that the cut would do little to ease tenants' benefit dependency.[20]

B. Local authorities

In theory local authorities are free to exercise a great deal of discretion when setting and reviewing their rent levels. Section 24(1) of the *1985 Housing Act* merely requires authorities to 'make such reasonable charges as they may determine for the tenancy or occupation of their houses. ' The *1989 Local Government and Housing Act* added subsections

[20] 'Shock over grant rate cut', *Inside Housing,* 15 August 1997

(3) and (4) to section 24 which provide that councils should have regard to the principle of proportionality when reaching rent fixing decisions. The local discretion afforded by section 24 must, however, be read subject to Part VI of the 1989 Act which introduced a new system of revenue subsidy for local housing authorities and which has had a significant impact on the way councils set their rent levels.

The 1989 Act 'ring fenced' council housing revenue accounts (HRAs)[21] so that it is no longer possible for authorities to subsidise HRAs by a transfer of money from their General Funds. The freedom to make rate or general fund contributions to the HRA had traditionally been the means by which low council rents were sustained. This practise attracted criticism in the Department of the Environment and Welsh Office White Paper, *Housing: The Government's Proposals*,[22] which described 'indiscriminate subsidies from the rates to hold down rents' as a 'waste of resources'. The 1989 Act also placed a duty on local authorities to prevent a debit balance on their HRAs; as one of the major sources of income to the account is rental income, rent levels set have necessarily reflected this duty.

Aside from rental income the other main source of HRA income is HRA subsidy which becomes payable when the notional HRA of an individual authority would otherwise be in deficit. Under the regime introduced by the 1989 Act the Department of the Environment issues annual guidelines for expenditure on the cost of managing and maintaining council housing stock and on the level of rent increase for each authority in order to construct a notional HRA. The subsidy entitlement that is then calculated is designed to meet the notional deficit irrespective of an authority's actual expenditure pattern.

The Department's guideline rent increases for each authority are designed to link the rent with the value of the property. The previous Government's aim was to encourage authorities to set rents that would come to reflect the pattern of the value of housing around the country, rather than a pattern based on historical circumstances or political choice. The formula for calculating the guidelines on management and maintenance spending is based on past expenditure patterns excluding spending on 'capitalised repairs', i.e. repairs financed from capital receipts, and including an allowance to reflect the cost of managing and maintaining different types of property.

The new financial regime did not necessarily imply a significant impact on rents and expenditure levels but much was to depend on the rent and expenditure assumptions made by the Department in calculating an authority's subsidy entitlement. Given the need to balance the HRA and the inability to transfer monies from the General Fund, authorities who believe that their notional management and maintenance allowances have been underestimated have

---

[21] Which govern the finances of council housing.
[22] 1987

had little choice but to raise rents above the Department's guideline increase. Alternatively, authorities wishing to hold down rent levels below the guideline increase have had to cut expenditure on the management and maintenance of their stock.

Another feature of the current HRA subsidy system is that authorities with a surplus on their HRAs receive reduced subsidy on the rent rebates given to their tenants. As a result, the rents of "better-off" council tenants not receiving rebates help to meet the cost of giving financial help to poorer tenants via housing benefit.[23]

C. Private sector

1. Protected/regulated tenancies

The majority of private sector tenants who have exclusive occupation of their homes and who took up their tenancies prior to 15 January 1989 (the date on which Part I of the 1988 *Housing Act* came into force) are usually referred to as 'regulated' or 'protected tenants'. The statute governing the rents and security of tenure of these tenants is the *1977 Rent Act.* Secure tenants of housing associations, i.e. those who entered into their tenancy agreements prior to 15 January 1989, are also covered by the rent setting provisions of the 1977 Act.

Regulated tenants are entitled to have a 'fair rent' set on their properties by the local rent officer. The rent officer is a statutorily appointed public official who is independent of central and local government. Rent officers are employed in local rent offices throughout the country. Each rent office has jurisdiction over an area that broadly corresponds to an area of local government.

In determining a fair rent the rent officer must take account of the provisions of s.70 of the *Rent Act 1977.* Factors which will influence the rent level include the age, character, locality and state of repair of the dwelling house and the quality and quantity of any furniture provided. Rent officers are obliged to assume that there is no scarcity of comparable rented accommodation in the locality for the purposes of setting a fair rent; this has traditionally meant that these rents have been held below market levels. The rent officer must also ignore the personal circumstances of the tenant(s).

Once a fair rent is registered by the rent officer it becomes the legal maximum that is chargeable for the tenancy and is reviewable every two years. Tenants and landlords have the right to appeal against a fair rent set by a rent officer to the local Rent Assessment Committee (RAC).

---

[23] Further information on this is available in a Library standard note by Wendy Wilson: *sps\note\housing\rentrebates.ww.doc*

These are bodies of independent people, some of whom have legal, surveying or other property or relevant expertise, and some of whom are laypersons who have been appointed by the Secretary of State or the Lord Chancellor. When a case is referred the RAC will reconsider the whole matter of the rent level again but may decide on a rent which higher than that originally set by the rent officer. There is no appeal against a RAC's decision except to the High Court on a point of law.

It is increasingly the case that landlords are appealing to RACs using the argument that the growth in the supply of private rented accommodation means that there is no scarcity and that fair rents should be compared, and set in line with, market rents.

In the case of *Spath Holme Ltd v Greater Manchester and Lancashire Rent Assessment Committee* (1995) the landlord successfully argued that, as the company was offering similar properties in the same block at much higher assured tenancy rents, those of regulated fair rent tenants should be allowed to rise to levels higher than allowed by the RAC. The Court of Appeal held that the tenancies were similar and that scarcity of rented accommodation was not a factor in this case.[24] The case established that rent officers should set fair rents by looking at market rents, including rents under assured tenancies, discounted for scarcity. Following this case there was concern that landlords, particularly in London, would use it as a basis to increase fair rent levels.[25] The previous government rejected calls to intervene to stop substantial increases in fair rent levels:[26]

On 9 October 1997 the Court of Appeal delivered what has been described as a 'landmark' judgement on the method of determining a fair rent and on the content of written reasons given by RACs. In *Curtis v London Rent Assessment Committee*[27] the landlord (Curtis) had taken the rent officer's determination of rent for two flats in a block to the local RAC. The rents registered of £3,900 and £3,640 were substantially lower than the £5,720 and £5,200 applied for, despite evidence that rents obtainable for flats let on assured tenancies in the same and similar blocks ranged between £5,720 and £6,240. The RAC accepted the landlord's comparables as evidence then reported that it had made 'appropriate deductions for differences commented upon…as well as a discount for the scarcity element', and that having done so, saw no need to alter the registrations. The RAC also said that it did not consider it appropriate to offer artificial calculations, detailed workings or hypothetical percentages, arguing that as an expert tribunal, they were entitled to rely on a broad, well-founded approach.[28]

---

24 see *Independent Law Report*, 28 August 1995
25 'Court bid to push up capital's fair rents', *Inside Housing*, 15 September 1995
26 HC Deb 16 October 1995 c.165W
27 [1997] EGCS 132
28 British Property Federation, *Residential News*, 7 November 1997

The landlord appealed to the High Court on a number of grounds but won the case on only a procedural point. He then took the case to the Court of Appeal because he maintained that the judge had wrongly rejected the substance of his appeal and that the RAC had failed to apply the principles of the Spath Holme judgement. The Court of Appeal ruled that the fact that the landlord's appeal to the lower court had been successful did not bar him from appealing to a higher court to clarify the law, since without the guidance he sought, even a differently constituted RAC might adopt a faulty approach.

On the substance of the appeal, the Court reaffirmed the principle established in the Spath Holme judgement that the starting point for a determination of a fair rent under section 70 of the *1977 Rent Act* could only be the market rent, adjusted for scarcity. In the Court's view the market in private rented housing had undergone profound changes since the *1988 Housing Act* and the best evidence in most cases would now be assured tenancy comparables since these were the natural successors to registered rents. Accordingly, the Court felt that there should be no reason to refer to registered rents at all in cases such as this and less reason to consider their soundness as market indicators.

The Court also ruled that where disputed adjustments had to be made when discounting scarcity, there was no rational way of giving effect to section 70 without some sort of arithmetical calculations, however few or approximate. In failing to give these calculations the RAC in this case was found to have fallen short of the standards required of decision making bodies. The Treasury Solicitor, who represented the London RAC, was expected to seek leave to appeal to the House of Lords for a final and definitive judgement on the case.[29]

As with private sector tenants, housing association secure tenants have experienced substantial rent increases in recent years. In addition to the factors outlined above, some housing associations have adopted a policy of bringing the rents of secure and assured tenants into line in order to remove the anomaly of having tenants living in the same, or very similar, properties being charged very different rent levels. Housing associations do have the flexibility to charge less than the full fair rent level; the circumstances in which this can be done are set out in Housing Corporation Circular 5/93, i.e:

a) where the increase set by the rent officer or the rent assessment committee is substantially above the corresponding rise in the average earnings index, then the association can phase the increase over a reasonable period of time, which should not exceed two years;
b) where fair rents are greater than the assured rents being set by the association under its agreed affordable rent policy then secure tenants can be charged the same rate as assured tenants in similar accommodation;

---

[29] ibid

c) where a tenant has appealed to a rent assessment committee for a rent reduction, and the committee has actually set an even higher rent, then the association can charge the tenants the rent originally set by the rent officer or charge rents similar to those being paid by other secure tenants in similar accommodation.

Some housing associations, e.g. the Joseph Rowntree Housing Trust, have withdrawn from using the rent officer service in their rent setting processes in reaction to the rate of increases that have been recommended.[30] The rent officer still sets a legal maximum rent for the properties concerned but the Trust has devised its own method of setting rents that ensures that the rents remain below the 'fair rent' level.

2. Assured and assured shorthold tenancies

The 1988 *Housing Act* introduced two distinct types of de-regulated tenancy. After the enactment of Part I of the 1988 Act (15.1.89) new private sector tenants could either be assured or assured shorthold tenants. If a landlord failed to follow the correct procedure for the creation of an assured shorthold tenancy they would generally, by default if not by intention, create an assured tenancy.[31] An assured tenancy allows the tenant to remain in the property unless a court grants the landlord possession under one of the grounds for possession specified in the Act. An assured shorthold tenancy gives the landlord an automatic right to regain possession of the property after the expiry of six months. The *1996 Housing Act* has reversed this position so that, since 28 February 1997, a tenancy of privately owned accommodation let on or after this date will be an assured shorthold tenancy unless the tenancy agreement or a separate notice says that it is not. Lettings of housing association properties since 15 January 1989 are on an assured tenancy basis.

The rent levels on assured and assured shorthold tenancies are freely negotiable between landlords and tenants. There is some provision for the referral of rent increases and unreasonably high rents to the local RAC, but there is no rent control in operation akin to that which applies to protected/regulated tenancies under the *1977 Rent Act.*

It was the Conservative Government's stated intention that the rents on deregulated private sector tenancies should increase. It was hoped that the improved rate of return that landlords could obtain, plus reduced security of tenure for tenants (particularly assured shorthold tenants), would attract potential landlords into private renting. The 1995 White Paper, *Our Future Homes,* attributed the growth in the sector since 1988 to the removal of controls over new

---

30 'Cumbersone system must be repealed', *Housing Today*, 2 April 1998

31 Assured and assured shorthold tenants must have exclusive occupation of their accommodation, ie someone who rents a room in their landlord's home will not be an assured or assured shorthold tenant.

private rented lettings;[32] it also noted: 'as the sector has expanded, and as average rents have risen as a result of deregulation, the cost of housing benefit has risen.'[33]

[32] p.21
[33] p.24

IV Action taken to limit rent increases

A. Housing associations

In its 1995 White Paper, *Our Future Homes,*[34] the previous Government noted that it had shifted the balance of housing subsidy by reducing subsidies to rents and relying more on housing benefit to provide help as rents increased. The Government stated that:[35]

> 'We are now approaching the limits of what can be achieved through higher rents. Around two thirds of social sector tenants now receive help with their rents through housing benefit. To increase rents much further could increase the cost to the taxpayer, because of the increased benefit bill and damage to work incentives.'

It was within this context that the Housing Corporation published proposals for a trial rent competition framework in July 1995.[36] Since 1996/97 bids for new development submitted by associations have been assessed on the level of their proposed rents in addition to factors such as housing need, quality and value for money. The aim of this 'competition' is to ensure that bidders putting forward lower rents, which result in lower housing benefit payments, are favoured in the allocation process.

In association with *Our Future Homes* the previous Government issued a series of consultation papers. *More Choice in the Social Rented Sector* set out the Department of the Environment's proposal to introduce inflation related rent controls for housing association assured tenancies based on the formula expressed as 'RPI+/-X'; the 'X' factor prescribing rental growth was to be set by the Government every five years. This proposal was met with a storm of protest. The NHF argued that the formula would threaten the ability of associations to raise private finance; the Nationwide, one of the largest lenders to the housing association movement, threatened to withdraw from the sector if the formula was implemented.[37] Lenders were concerned that the uncertainty surrounding the 'X' factor could prevent associations from meeting their debts by increasing rents. The idea of an across the board rent control formula was also criticised on the ground that it could reduce associations' assets by driving down valuations and forcing associations to put more properties into loan agreements. Head of Research at the Council of Mortgage Lenders (CML), Peter Williams, was of the view that housing benefit restrictions, the general requirements of business plans

---

34 Cm 2901

35 ibid p.27

36 *Competing for Grant*

37 'Nationwide threatens to end funding in protest at rent bidding', *Inside Housing,* 8 September 1995

and rent bidding pressure from the Housing Corporation would be enough to safeguard against excessive rent increases.[38]

In the event the proposed rent formula did not find its way into the *1996 Housing Act* but the Act does allow the Corporation to issue guidance on rents[39], impose conditions on landlords, require information from landlords and require the publication of performance indicators.[40] In effect it has given the Corporation powers to impose a contractual framework of rent regulation.

In October 1996 the Corporation published a discussion paper on the social housing standard for rents and service charges.[41] In this paper the Corporation proposed a 'twin-track' strategy for restraining association rents whereby associations submitting new schemes for Social Housing Grant after 1st April 1997 would have to abide by the rents proposed when bidding; subsequent rent increases would be limited to the RPI (including mortgage interest) plus 1 per cent. Breaches of this 'contract' would trigger an investigation and could result in future grants being blocked. In regard to existing stock, the Corporation proposed an 'accountability approach' where tenants would be informed by each RSL publishing its rent policies and average rent levels by local authority area. Accountability would be based on the expectation that rents on existing stock would remain sub-market and affordable and would not be subject to unnecessarily large increases. RSLs would be called upon to justify any rent and service charge increases significantly above the mean in each local authority area. For stock transferred to RSLs after 1 April 1997 the Corporation proposed that increases should not exceed RPI +1% unless it could be justified by changes in circumstances or their financial position.

These proposals were welcomed by the housing profession with some reservations. The NHF expressed concern over the absence of targets defining affordable housing and Steve Wilcox, Senior Research Fellow at the Centre for Housing Policy at the University of York, pointed out that the proposals did little to grapple with the fact that housing association rents were already at or above private rents in some areas of the country.[42] The CML was reassured by the fact that associations would be able to breach the rent limit where this could be justified.[43] Alternatively, some valuers and lenders warned the Corporation that the proposals would have an adverse impact on current and future valuations of housing owned by RSLs; Savills, the surveyors, predicted a 25% cut in Existing Use Valuations with consequent damaging effects on loans secured on this valuation basis.[44] As a result of these concerns the

38 'Rent controls will be a disaster, say lenders', *Inside Housing*, 15 September 1995
39 section 36(2)
40 section 36(3) of the 1996 Act provides that this guidance must first be approved by the Secretary of State
41 *Influencing rents*
42 'Twin track plan to tackle soaring rents', *Inside Housing*, 1 November 1996
43 'The price to pay', *Housing Today*, 31 October 1996
44 'Funders fear damaging Corporation rent proposals', *Social Housing*, January 1997

Corporation revised its proposals to provide that transfer associations[45] would be able to bring their rents up to levels that would cover their assets. Since April 1997, RSLs receiving capital grants for new development have been required to limit the increase in rents and service charges to RPI plus 1 per cent.

Average rent increases in the first quarter of 1997 were hailed as proof that the Corporation's rent control policies were working. Average rent for a new association property in the first quarter of 1997 was £59.37 compared with £58.89 for the same period in 1996.[46]

In August 1997 the new Minister for Housing, Hilary Armstrong, wrote in a letter to the Housing Corporation:[47]

> 'I am looking for a reduction in the average level of rents charged over a three-year period of about 4 per cent in real terms. Rents on new schemes have now reached a level where it is questionable whether they are affordable to those in low-paid employment without assistance from housing benefit.'

This was the first time that a target had been set by Government for cutting housing association rents. The announcement was made at the same time as the Government proposed a cut in the average grant rate in 1998/99 to 54% and housing commentators accused the Government of sending out an 'inconsistent' message on rents.[48]

In order to achieve this target the Corporation produced a set of benchmark rents that were based on 1996/97 CORE (continuous recordings) data alongside the Approved Development Programme bidding guidance for 1997/98.[49] The aim was to produce a new set of benchmarks to replace regional guideline rents that were designed to reflect local circumstances more accurately. The bidding guidance stated that housing associations would risk losing development funding if they charged rents above the benchmark levels; the Corporation advised that if associations could not bid at benchmark rents they should bid for more grant or not at all.

The NHF and individual housing associations made representations to the Corporation on the benchmark rents claiming that they contained confusing anomalies and could be unworkable

---

[45] These are associations that have taken over local authority stock following a large scale voluntary transfer (LSVT)

[46] 'Rent controls bite', *Inside Housing*, 25 July 1997

[47] DETR press notice ENV/321, 7 August 1997

[48] 'Rent target set as grant rate cut', *Housing Today*, 14 August 1997

[49] In August 1997.

in some cases given associations' existing rent policies. The NFH found that tenants in neighbouring local authorities could have ended up paying up to £15 more per week for the same size property. In response, the Corporation stressed that the benchmarks were 'not ceilings' and that associations could bid for schemes with higher rents if a convincing justification could be found.[50]

Under the new performance standards for RSLs, introduced on 1 April 1998, RSLs are expected to limit their overall rent increases to RPI plus 1 per cent.[51] This figure applies to the total rent envelope of an association's stock rather than to individual rents. It does not prevent an individual tenant's rent from rising by significantly more than that figure.

The current general requirement on RSLs in regard to rents and service charges is to:[52]

> 'Set their rents and Housing Benefit-eligible service charges to as to achieve sub-market levels whilst still meeting their legal financial and other commitments, covering their costs and making proper provision for future repairs. The rents and Housing Benefit-eligible service charges should be affordable to people in low-paid employment and RSLs should endeavour to minimise dependence on Housing Benefit for those who receive it.'

The efforts of the Housing Corporation in England can be compared with those of the Housing for Wales (Tai Cymru). In November 1993 the Welsh Federation of Housing Associations and Housing for Wales launched a twin strategy to curb rent rises. While lobbying the Government for extra grants, Welsh associations were urged to set a good example by freezing rents for a year; with a handful exceptions associations followed this course of action.

Housing for Wales started to take rents into account in the HAG allocation process before its English counterpart. In 1995/96 Housing for Wales fixed grant rates at the same average levels initially set by Ministers for England and focused competition between associations towards achieving lower rent levels. Associations submitting proposals for schemes with rent levels well above those proposed by other associations were either excluded or given a low priority in the HAG allocations. Critics of this approach thought that it was overly mechanistic and failed to take account of issues of quality.[53]

---

50 'Rent benchmarks not ceilings', *Housing Today*, 18 September 1997
51 Housing Corporation, *Performance Standards*, December 1997
52 ibid p.26
53 Steve Wilcox, *Unresolved Tensions: Grant, rent and benefit policies*

Rent bidding had the effect of limiting overall rent growth and reduced variations in rents among associations that had led to anomalies in some areas. In 1995 rents for new housing association assured lettings in England remained above those for relets and, at £56.50 per week had already climbed to nearly 20% of average male manual earnings. By contrast, in Wales housing association rent levels fell in 1995.[54]

In 1996 Housing for Wales decided to 'fine-tune' the system and replace rent bidding with benchmark rents. In 1997/98 housing associations were required to match benchmark rent levels in order to qualify for development, repairs and maintenance grants. Benchmark levels are negotiated annually with the aim of achieving below inflation rate increases via efficiency savings; they are set for each local authority area based on average rents. Concern was expressed over how the benchmark figures had been devised but all bar two associations agreed to comply with them. Housing for Wales dropped controversial plans to limit rent increases to RPI -1% following consultation.[55]

In February 1997 the Chief Executive of Housing for Wales, Adam Peat, predicted that average housing association rents, adjusted for inflation, would be 5% lower in 1997/98 and attributed this to the policy of rent benchmarking.[56]

Lenders in Wales are apparently relaxed about the current rent controls as associations have the option of dropping out of the regime if they do not wish to develop.[57] The success of Welsh associations in keeping rent levels down has been attributed to the fact that competition between them is based purely on rents whereas in England associations bid against each other on grant rates. The director of the Welsh Federation of Housing Associations has said that members have cut overheads, including management costs, to stay within the benchmarks; he also attributed their success to associations acting cohesively.[58]

Table 2 (page 7) shows that until 1993/94 there was little difference in the Welsh and English average assured rents and their rate of increase. Since 1994 the average Welsh housing association rent has levelled off whilst the English average has continued to rise. At September 1996 the Welsh average of £42.40 per week was 13% below the English average. Scotland has experienced a similar growth rate in average rents but from a much lower base.

---

[54] ibid
[55] 'New rent rules worry Welsh associations', *Inside Housing,* 8 November 1998
[56] 'Welsh association rents fall by 5 per cent', *Inside Housing,* 14 February 1997
[57] 'It's cheaper to live in Wales', *Inside Housing,* 7 March 1997
[58] ibid

In regard to increases experienced by secure tenants of housing associations (whose rents are set by the local rent officer) and discrepancies between 'fair' and assured rents, Nick Raynsford made the following statement earlier this year:[59]

> The corporation has also been encouraging RSLs to develop rent policies aimed at setting rents that reflect the size, nature and location of the property rather than the nature of the tenancy or the funding regime under which it was developed. That would suggest a gradual process of convergence between secure and assured rents. However, it could seem rather inequitable to allow individual fair rents in the social rented sector to rise unchecked, if those in the private sector were subject to a cap.
>
> We are therefore considering whether any proposal to limit fair rent increases for regulated tenants might also apply to secure tenants of RSLs, but within the rent control framework being developed by the Housing Corporation for all existing stock. RSLs would still be expected to develop rent policies which worked towards rent convergence, although that convergence might be slower if fair rent increases were limited. Clearly, we are trying to balance a number of issues here and we would not take any decisions about the way ahead without consulting all the interested parties first.

The Government issued a Consultation Paper on 21 May 1998 in which it proposes that all tenants (including secure tenants of RSLs), with a rent registered under the *Rent Agriculture Act 1976* or the *Rent Act 1977,* will have their rent increases limited by an Order made under the *Landlord and Tenant Act 1985*. The proposed limits are RPI plus 10% for the first re-registration after the Order comes into effect and RPI plus 5% for subsequent re-registrations. The limits will not apply if the rent had not previously been registered or a substantial increase in rent was due as a result of repairs or improvements by the landlord to the property.[60] The consultation period ends on 24 July 1998.

B. Local authorities

On 21 November 1995 the then Housing Minister, David Curry, announced the Government's intention to freeze the average guideline rent for local authorities in 1996/97, in real terms, at £34.70 per week; this gave a range of increases for individual local authorities of between 67p and £1.17 per week. A consultation paper was also issued setting out proposed arrangements to discourage authorities from increasing their rents by more than the Government's guideline increase.[61]

---

[59] HC Deb 26 January 1998 c.126
[60] HC Deb 21 May 1998 c.444W
[61] Deposited Paper 3/ 2369

The paper proposed that HRA subsidy would not be paid on any additional rent rebate expenditure resulting from authorities increasing their average actual rents by more than their guideline rent increases. The background to this was explained as follows:

> "Average actual rents have been increased by more than the Department's guideline in five out of the six years since the introduction of the HRA subsidy system in 1990/91. The Exchequer has had to meet the resultant large, unplanned, cost of the additional rent rebates arising from the increases. The Government is concerned that the existing subsidy arrangements - whereby the additional rent rebates arising from rent increases above guideline are subsidised at a rate of 100% at the margin - do not provide authorities with a sufficient incentive to control expenditure.
>
> The Government recognises that some of the increases in the past have been due to the transitional problems that authorities faced following the introduction of the HRA subsidy system. Now that the system has bedded down, the Government believes that it should be possible for authorities to provide council housing without recourse to further increases above guideline. Limiting subsidy on rent rebates will provide authorities with a proper incentive to finance improvements in service to tenants from efficiency savings rather than further rent increases above guideline."

On 22 December 1996, following consultation, the DoE (now the DETR) confirmed that it would be going ahead with the proposal. Guidance was produced on the formula for limiting subsidy and on the definition of average rent. The new rule operates in the following manner:

- there is no reduction in HRA subsidy on rent rebates where an authority increases its average rent by up to the guideline rent increase;
- HRA subsidy ceases to be paid on any additional rent rebate expenditure which results from an authority increasing its average rent by more than the guideline rent increase; and
- the **higher** of an authority's average actual rent and guideline rent for the year in question is used as a base for the comparisons. This is to ensure that those authorities with an average rent below guideline will continue to receive full subsidy on their rent rebate expenditure, subject to the usual deductions under the incentive area etc.

The DETR will consider requests for special determinations to dis-apply the rule in whole or in part where authorities can show that they face exceptional circumstances outside their control.

The local authority associations did not welcome this development. It was viewed as a substantial erosion of local autonomy; George Meehan of the London Housing Unit was reported to have said: "it makes a nonsense of consultation with tenants on the balance between rent and service levels. Any housing policy Mr Curry may have had has been supplanted by a housing benefit control policy."[62]

The local authority associations' response to the consultation paper claimed that the DoE had taken no account of inadequate management and maintenance allowances that had forced some councils to make up the shortfall from rent increases above the guideline level. It was pointed out that the average gap between rent increases and guidelines had actually been converging; only 3 per cent of authorities increased rents by more than £2.50 above guidelines in 1995/96 according to the AMA/ADC Housing Finance Survey.

The associations also argued that councils' HRAs already "unfairly contribute" more than £1 billion to rent rebate expenditure (see page 20). The new Government has maintained this 'capping' policy pending the Treasury's comprehensive spending review.

C. Private sector

The previous Government resisted calls for action to be taken to limit increases in registered rent levels:[63] There have been no attempts to re-introduce rent controls for assured and assured shorthold tenancies or to strengthen existing controls over registered rents; measures *have* been introduced to limit housing benefit expenditure on private sector rents.

Since January 1996 100 per cent housing benefit has only been payable on eligible rents that do not exceed the 'local reference rents'. These are set by rent officers to reflect the average market rents for properties of a specified size. Where the 'appropriate rent' for a particular 'above average' property is set by the rent officer at a higher level than the local reference rent then no benefit is payable on the difference between these two levels.[64]

From October 1996 single people under the age of 25 have only been eligible for housing benefit for rents based on the concept of a 'single room rent'; that is the average rent for a single room with shared facilities.

Since the introduction of these measures there has been a reduction in the number of private tenants in receipt of housing benefit as well as a far lower rate of increase in the average level

---

[62] 'Curry under fire as councils face a rent straightjacket', *Inside Housing*, 24 November 1995
[63] HC Deb 16 October 1995 c.165W
[64] Until October 1997 benefit was payable on 50% of the difference between these two levels.

of housing benefit paid to private tenants.[65] Recent research undertaken by the London Housing Unit in one London Borough found that one in two tenants facing a shortfall in their housing benefit had asked their landlords for a rent reduction; only one in four were able to negotiate the rent down to the level of their housing benefit and another one in four achieved a partial reduction. These findings seem to indicate that benefit restrictions could be resulting in tenants facing financial hardship rather than in landlords reducing their rent levels.[66]

Karen Buck raised the issue of increases in fair rents in a Debate on the Adjournment of the House on the 26th of January 1998.[67] The Minister for London and Construction, Nick Raynsford, gave the following response:[68]

> Regulated tenancies have generally been acquired in anticipation of substantial capital gains when the tenancies come to an end. These tenancies have always traded at a discount to vacant possession value. The discount may have reduced in recent years, but even now those properties trade at some 30 per cent. to 45 per cent. below vacant possession value. Moreover, the landlords bought those properties in the knowledge that the rents were subject to fair rent controls and that potential rental yields would be lower than those obtainable from assured shorthold tenancies. Therefore, we feel that there is a strong case for considering Government intervention to moderate rent increases for the small group of existing tenants in that position.
>
> What options are we considering? First, I must make it clear that we do not have it in mind to change either the existing system of fair rent determinations by rent officers and rent assessment committees, or the rent criteria in section 70 of the Rent Act 1977. That would require primary legislation and, in view of the many other pressures on parliamentary time, any opportunity for that would be likely to lie some way ahead.
>
> A more attractive option, which may be possible through secondary legislation, is the application of a maximum limit to the size of the rent increase which could be imposed by rent officers and rent assessment committees under the existing system. We have in mind linking rent increases to the retail prices index, as a well-established measure of affordability, by way of an "RPI plus X" formula. However, there are some tricky issues to be resolved. We would need to ensure that we got the right balance between the interests of tenants and the interests of landlords. Another issue is that we do not want to discourage landlords from carrying out necessary improvements to their property; but, equally, we must be sure that any mechanism which allows rent increases to reflect those improvements does not simply provide the landlord with a loophole for circumventing the new limit.
>
> There are difficult and detailed technical and legal issues which still need further study, but assuming that we can overcome these to our satisfaction, we shall issue a public consultation document setting out our proposals and seeking comments on the details. I cannot say precisely when that might be, but I can assure my hon. Friend that we are moving as rapidly as we can.

---

65 Wilcox & Sutherland, *Housing benefit, affordability and work incentives*, December 1997

66 LHU, *Minding the gap: shortfalls between private rents and housing benefit in one London Borough*, 1998

67 HC Deb 26 January 1998 cc 121-128

68 ibid

The Government's Consultation Paper, issued on 21 May 1998, proposes that all tenants with a rent registered under the *Rent Agriculture Act 1976* or the *Rent Act 1977* will have their rent increases limited by an Order made under the *Landlord and Tenant Act 1985*. As with secure tenants of RSLs, the proposed limits are RPI plus 10% for the first re-registration after the Order comes into effect and RPI plus 5% for subsequent re-registrations.

V The affordability debate

A. Defining affordability

A 1994 Cambridge University report (sponsored by the Halifax Building Society) noted that 'affordability has replaced need at the centre of the debate about the provision of adequate housing for all'.[69]

Government policy in the late 1980s and early 1990s was to target assistance towards those in the greatest need and to move towards a more market based system where prices (rent levels) reflected the cost of production. As described in detail in Part III of this paper, this meant a reduction in subsidies to providers, the deregulation of rent levels and finance markets and increased subsidies (housing benefit) for those who could not afford the resultant price rises. These policies have been attributed with giving rise to the question of whether people can obtain and retain suitable housing without running into difficulties in meeting their housing costs while still maintaining an adequate standard of living in terms of life necessities.[70]

The affordability of social housing rent levels has been identified as an important issue for the following reasons:[71]

- In the social sector it has become a central issue because of decreasing subsidies to suppliers, rent deregulation and moves towards market rents.
- For social landlords higher rents make them less attractive to low income working households as a result of the poverty trap. These pressures have been found to help to generate high concentrations of welfare benefit dependency and child density, particularly on large estates.
- For tenants, although those on housing benefit are protected from rent rises, they face an increasing poverty trap and have little income left over to deal with even small financial crises.
- In terms of lenders, affordability is important because only asset rich associations are likely to find it possible to continue to hold down rents for newer projects.

---

69 Halifax Building Society (Freeman & Whitehead), *Affordability: Definitions, Measures and Implications for Lenders*, 1994

70 ibid

71 ibid

Although various attempts have been made to define affordability within and across different housing tenures to date none of these attempts have been universally accepted and applied. Current debate surrounding this issue has largely, although not exclusively, been concerned with the affordability of housing association rents as it is this sector which, since 1988, has been the main provider of new social housing for rent. The Tenants' Guarantee has long enshrined the principle that housing association rents should be affordable to those in low paid employment; however, there is no agreement on what constitutes an affordable rent level.

Housing professionals who are in favour of rent reform view the development of an accepted definition of affordability as key element in this process; the National Housing Federation has argued that defining affordability outcomes of housing policy will enable:[72]

- the government to assess the balance of expenditure between subsidy and investment;
- the Housing Corporation as a regulator to assess the performance of registered social landlords;
- local authorities, as enablers, to achieve more effective partnerships;
- registered social landlords themselves - and local authorities - to concentrate on how best to use their resources to deliver affordable homes.

The National Federation of Housing Associations (now the National Housing Federation) lobbied against the *1988 Housing Act* having determined that a definition of affordability should be 20% of the median net income of new tenant households in work. This figure was used as it compared reasonably with interest payments by first-time buyers. The Federation's current definition is that: 'rents are affordable if the majority of working households taking up new tenancies are not caught in the poverty trap (because of dependency on housing benefit) or paying more than 25% of their income in rent'.[73]

The previous Government consistently refused to provide a definition of affordability:[74]

Mr Battle: To ask the Secretary of State for the Environment, if he will publish the affordability assumption used to determine grant rates to housing associations.

Sir George Young: Outturn rents are determined by housing associations. The Government do not publish the factors and assumptions implicit in the grant rate model or any general definition of affordability, since they do not wish to imply a view as to what constitutes an affordable rent in any particular case.

---

72 Wilcox & Sutherland, *Housing benefit, affordability and work incentives*, December 1997
73 This definition was adopted in 1993.
74 HC Deb 22 February 1993 c.421W

Sir George Young, the then Minister for Housing, gave evidence to the Environment Select Committee's inquiry into the Housing Corporation on the 21 April 1993 during which it became clear that, in calculating the effect of grant rate changes, the Government had assumed an affordability rate of 35% before housing benefit was applied. This was some 13% higher than that deemed acceptable by the Federation at that time. To date the new Government has also not published any assumptions on affordability.

Dr Christine Whitehead's research for the Halifax concluded that affordability means different things to different groups:[75]

> 'For *households* it is about having enough income to be able to purchase at least the minimum requirements for a reasonable standard of living. For *associations* it is about ensuring that the rent or mortgage can and will effectively be paid as well as about meeting their objectives of housing those in need. For *lenders* it is about protecting their income stream. For *government* is about how much subsidy has to be provided to ensure that the cost of adequate standards of housing is not so high that households cannot afford to buy the full range of necessary goods. Definitions of affordability must therefore take account not only of the cost of housing but of housing standards and the price of other necessities of life.'

B. Measuring affordability

Two basic measures of affordability are generally used when considering social sector rents and subsidies in the UK. The ratio measure is a relative measure that compares rent and eligible service charges to net income (after the deduction of tax and national insurance contributions) and housing benefit. The absolute measure involves measuring residual income, i.e. the sum left over after housing costs and the income support applicable amount have been deducted from net income and housing benefit.

The rent to income ratio does not distinguish between households on different income levels so that households may have the same ratio but may have very different levels of residual income. As noted above, the NHF currently suggests that gross rents, including service charges, should not be greater than 25% of net income for working households in housing association properties while the Housing Corporation appears to apply an implicit benchmark of 33-35% when negotiating suitable grant rates.

---

[75] Halifax Building Society (Freeman & Whitehead), *Affordability: Definitions, Measures and Implications for Lenders*, 1994

The Property Research Unit at Cambridge University has suggested that:[76]

> 'To reflect the underlying concept of affordability such measures must not only include a clear definition of rent and income, they must also specify over what range of income they are seen to be applicable, household circumstances and any variation in the costs of other goods and services, in order to assess whether or not the household can afford the relevant proportion of income for housing and still purchase other necessary goods. They must also clarify the quality of housing to which the ratio applies to ascertain whether what is purchased meets accepted standards.'

The residual income measure is embedded in the social security and housing benefit systems. Under this approach housing is deemed to be affordable as long as, after housing costs have been paid, the household has enough other income with which to purchase the necessities of life. This is, in principle, how the benefit system works: the whole rent is payable through benefit whenever a household's income falls below the income necessary to buy a suitable basket of goods deemed necessary for that household given its composition and any special circumstances. Above that level of income 65p of each additional £ is withdrawn until the full housing cost is paid by the tenant.

The residual income measure means that, as long as those eligible for benefit actually claim it, no household on benefit has an affordability problem (assuming that residual income is correctly defined to allow adequate standards of living to be achieved and that the costs of buying these goods and services is constant across households and areas) and households on benefit are protected from rent increases. However, because the income taper is steep (65p in every additional £1 earned above the applicable amount must be used to pay the rent as benefit is withdrawn) and because other benefits are withdrawn at the same time (e.g. council tax benefit), households may only keep a few pence in the £ of any increase in income. Moreover, the higher the rent level the larger a person's income must be before they receive any significant increase in spending power. The residual income measure allows its advocates to argue that all rented housing is affordable and that the benefit system exists to provide a proper safety net. An alternative view is that if a household qualifies for housing benefit, then by definition their rent is unaffordable.

Those who prefer the ratio measure have made the case for it to be applied to those just above the benefit level to ensure that the proportion of income spent on housing should remain reasonable without recourse to benefit.

[76] ibid

Cambridge's Property Research Unit concluded that:[77]

> 'Affordability needs to be monitored not only in terms of ratios, but also in terms of the residual incomes available to their tenants - both as part of the negotiations with Government about grant rates and by associations and lenders for management purposes.'

C. Affordability trends

In the *Halifax Affordability Report II*[78] Angus Freeman and Dr Christine Whitehead analysed the NFHA's CORE data for 1992-95 in terms of affordability. It was found that (in 1995) non-working lone parent families had the severest housing affordability problem followed closely by non-working single adult households. For households with one worker affordability measured by residual income decreased as their household size increased: single adult households with £53 per week had more than lone parent families on £42 per week who, in turn, had more than two parent families on £39 per week.

Using the rent to income ratio, non-working single adults were found to be spending the highest proportion of their net income (including housing benefit) on rent and service charges at 48%. The next highest ratio was 42% for non-working lone parent families. The lowest rent to income ratio was 23% for two parent families where both parents were working. Most household types with one worker had very similar rent to income ratios of around 30%.

Over the three years since the first *Halifax Affordability Report* was published (1992-95) the affordability situation was found to have worsened for non-working lone parent families, who had experienced an increase in their affordability ratio from 39% to 42% and a drop in their weekly residual income from £6 to £0. The affordability situation of non-working two adult households in two bedroom properties had also worsened; these groups accounted for 16.5% of all households obtaining assured new lets during this period.

Two parent families with both parents working were found to have the best affordability situation of all. Their rent to income ratio fell from 25% to 23% and their residual income increased from £61 to £108 during this period.

At a regional level the pattern of change in affordability was found to be 'mixed'. Improvements were confined to households in the South and Midlands while households in

---

77 ibid

78 *Affordability Revisited in English Housing Association Assured New Let Accommodation 1992-95,* 1995

the North-West, Yorkshire, Humberside and East Anglia experienced a worsening in their affordability situation. In the North, low income growth contributed to worsening affordability as housing association rents increased between 4% and 9% between 1993 and 1995 while income grew by only 1- 4%.

In *Housing Benefit, affordability and work incentives*, Steve Wilcox and Holly Sutherland noted that the average affordability ratios for new housing association tenants in employment (using the gross rent to income definition) have been consistently above the NHF guidelines for assured tenancy relets since 1991. For lettings of new dwellings only, the average ratio has been over 25% since the beginning of 1990. In both cases the average ratios have followed a rising trend over the years since the introduction of the new financial regime for associations; the ratio for all association lettings had risen to 29.5% by 1995/96 (CORE).[79]

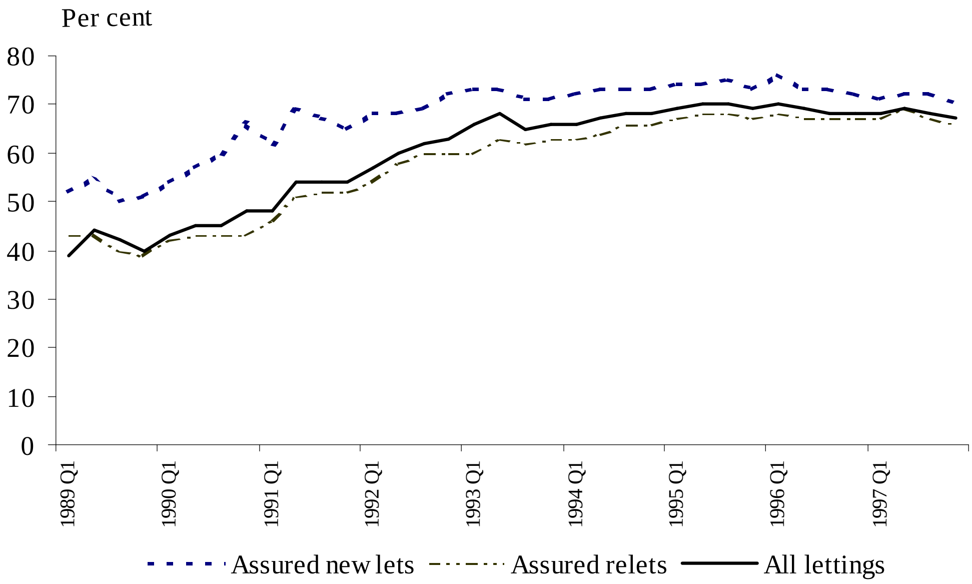
The NHF's CORE Lettings Bulletin for the final quarter of 1997 summarised its findings as follows:

- The annual increase in overall average rent was 3 per cent. This is the same rate of increase as seen in the July-September 1997 quarter, which was the lowest annual increase seen since CORE began.
- Relet rents for assured tenancies were 3.8 per cent higher than those of the year before - the lowest increase since CORE began.
- New let rents for assured tenancies increased by 1.5 per cent above those of the year before.
- Retail prices increased to 3.7 per cent above the previous year's level.
- Incomes of new tenants were 3 per cent higher on average than those of new tenants a year ago.

However, well over 50 per cent of working households (defined as one where the tenant or the tenant's partner, or both, are in work) were eligible for housing benefit or paying more than 25 per cent of their net income in rent at the time of letting:

[79] NHF, December 1997, para 3.8

Percentage of cases failing NHF affordability test



Regional Affordability - percentages of cases failing test Quarter 4 1997

Region	East	East Mid-lands	London	Mersey-side	North	North West	South East	South West	West Mid-lands	York & Humber -side	England
Fair relet	*	*	64%	*	*	*	*	*	*	*	**55%**
Assured new let	68%	59%	75%	70%	78%	73%	74%	72%	64%	70%	**70%**
Assured relet	66%	69%	70%	59%	61%	67%	67%	71%	67%	59%	**66%**
England	**67%**	**66%**	**71%**	**61%**	**63%**	**68%**	**69%**	**71%**	**65%**	**62%**	**67%**

Data in this table refer only to households with one or more persons in work
*denotes samples of fewer than 15 cases

VI Housing benefit, rent levels and work incentives

As explained in chapter III, recent years have seen a deliberate move away from bricks and mortar subsidies coupled with higher rents for social rented housing. These higher rent levels have been supported by increased housing benefit expenditure. The deregulation of private sector rents has meant an increase in real terms in housing benefit expenditure in all tenures. This increase in expenditure should be viewed in the context of savings achieved in bricks and mortar subsidies and the fact that a proportion of the costs of housing benefit payments to council tenants are met from local rent incomes, rather than by the Exchequer.

Table 7

Expenditure on Housing Benefit
Great Britain

		Total	Rent rebate	Rent Allowance Total	*Housing Association*	*Private*
£ million						
1988/89	outturn	**3,773**	2,688	1,071		
1989/90	outturn	**4,283**	2,905	1,365		
1990/91	outturn	**4,941**	3,367	1,769		
1991/92	outturn	**6,494**	4,006	2,426		
1992/93	outturn	**7,877**	4,593	3,284	*816*	*2,468*
1993/94	outturn	**9,209**	5,021	4,188	*1,069*	*3,119*
1994/95	outturn	**10,116**	5,242	4,874	*1,333*	*3,541*
1995/96	outturn	**10,944**	5,465	5,479	*1,613*	*3,866*
1996/97	outturn	**11,446**	5,621	5,825	*1,938*	*3,887*
1997/98	estimate	**11,563**	5,703	5,860	*2,213*	*3,647*
1998/99	forecast	**11,640**	5,533	6,107	*2,630*	*3,477*
£ million at 1996/97 prices						
1988/89	outturn	**5,343**	3,807	1,517		
1989/90	outturn	**5,669**	3,845	1,807		
1990/91	outturn	**6,056**	4,127	2,168		
1991/92	outturn	**7,482**	4,615	2,795		
1992/93	outturn	**8,709**	5,078	3,631	*902*	*2,729*
1993/94	outturn	**9,894**	5,395	4,500	*1,149*	*3,351*
1994/95	outturn	**10,708**	5,549	5,159	*1,411*	*3,748*
1995/96	outturn	**11,272**	5,629	5,643	*1,661*	*3,982*
1996/97	estimated	**11,446**	5,621	5,825	*1,938*	*3,887*
1997/98	forecast	**11,254**	5,550	5,703	*2,154*	*3,549*
1998/99	forecast	**10,999**	5,228	5,770	*2,485*	*3,286*

Sources: Social Security Departmental Report 1998, Cm 3913
DSS Analytical Services Division

Up until the early 1990s the DoE maintained a fairly relaxed attitude to high rent to earning ratios; this was partly based on the view that housing benefit would 'take the strain' of higher rent levels. Unemployed tenants in receipt of income support and income-based jobseeker's allowance can get 100% of their eligible rent met through housing benefit, subject to certain restrictions; for these tenants variations in rent levels have no impact on their disposable income. Wilcox and Sutherland note in *Housing benefit, affordability and work incentives:*[80]

> 'In the short term, higher rents reduce the disposable incomes of tenants with slightly higher incomes who are ineligible for benefit, or would have been had the rent been lower. In the longer term, however, those higher rents also extend the potential poverty trap for all households moving from unemployment into low paid work.'

Under the current housing benefit scheme tenants are permitted to earn a very low level of income above income support levels before entitlement to benefit is sharply reduced. The scheme is characterised by low levels of 'earning disregards', a sharp 'taper' rate at which benefit entitlement is withdrawn as net earnings rise[81] and the cumulative overlap of a number of benefit tapers (family credit, housing and council tax benefit). The table below illustrates the cumulative impact of the housing benefit taper rates in conjunction with tax and other means tested benefits.[82]

Cumulative deductions from each £1 of gross earnings

	Family	Single person or couple
Extra gross earnings	£1	£1
- Income tax @ 20%	20p	20p
- National insurance @ 10%	10p	10p
= Net earnings	70p	70p
- Family credit @ 70%	49p	-
= Income net of family credit	21p	70p
- Housing benefit @ 65%	14p	45.5p
- Council tax benefit @ 20%	4p	14p
= Net disposable income	3p	10.5p

The extent of the poverty trap is defined in terms of the income level at which benefit entitlement (or dependency) is extinguished; higher rent levels result in the poverty trap extending further up the income scale.

Although it is intended that the new working families tax credit[83] (WFTC) will be withdrawn at the rate of 55p for every extra £1 of income earned (as opposed to the 70% withdrawal of family credit), housing commentators have been quick to point out that, because of the

80 NHF, December 1997
81 Above income support levels claimants lose 65p of housing benefit for each extra £1 of income earned.
82 Wilcox & Sutherland, *Housing benefit, affordability and work incentives*, p.28
83 Announced in the March 1998 Budget.

operation of the housing and council tax benefit tapers, tenants on housing benefit who move into work could be left with a maximum of 15p for each extra £1 gained from WFTC.[84] In the absence of housing benefit reforms this effect is likely to wipe out the potential work incentive effect for working and non-working tenants in receipt of benefit.[85]

The people who live in social rented housing are more than twice as likely to be unemployed and otherwise economically inactive than families in other tenures. In the English housing association sector at the end of 1997 only 20 per cent of households had a head of household in full-time work.[86] Average incomes in the social rented sector in 1993 were 20% lower in real terms than in 1973.[87] As this paper has illustrated, these falling relative and absolute living standards of tenants in the social sector have not been matched by falling housing costs. Lower incomes, higher unemployment levels and higher rents for occupants of social rented housing have inevitably meant an increased role for housing benefit and a growth in the proportion of social renters who are dependent on it. Sixty eight per cent of housing association tenants in England were eligible for housing benefit in the last quarter of 1997.[88]

A great deal of research has been carried out into whether the tax and benefit system, in conjunction with high rents, creates barriers to employment for tenants of social housing. A 1996 report by the Institute for Fiscal Studies found that over 40% of men in the social sector in employment and nearly 70% of men out of employment faced very low financial returns to employment.[89] They defined this group as those who gained less than 40p for every pound earned because of reduced benefits and increased tax. The groups with the worst returns were men with children and those with an unwaged partner. The picture was similar for women; returns were found to be particularly low for lone parents.

Given the complexity of calculating entitlement to benefit it perhaps not surprising that research evidence also indicates that the poverty trap has 'only a limited direct impact on household decisions about taking up a low paid job'.[90] The body of research on household attitudes indicates that rent levels, rather than the potential availability of in work housing benefit, are currently the more significant consideration in terms of work incentives.[91] Wilcox and Sutherland conclude that 'this has important implications for housing policy decisions in setting the balance between the provision of bricks and mortar and personal subsidies.'[92]

---

84 'Still in the poverty trap', *Housing Today*, 19 March 1998
85 see Library Research Paper 98/45
86 NHF CORE Lettings Bulletin, October-December 1997
87 Institute for Fiscal Studies, *Living with the state: the incomes and work incentives of tenants in the social rented sector*, 1996
88 NHF CORE Lettings Bulletin, October-December 1997
89 Institute for Fiscal Studies, *Living with the state: the incomes and work incentives of tenants in the social rented sector*, 1996
90 Wilcox & Sutherland, *Housing benefit, affordability and work incentives*, p.15
91 ibid
92 ibid

VII Some options for reform

A. Rent reductions

A growing number of people in the housing profession believe that rent levels must be reduced if the Government's aim of reducing poverty and welfare dependency is to succeed. In an article for *Housing Today* Pete Challis, vice-chair of the London Government Association, argued that the current financial framework could not deliver sustainable communities:[93]

> 'The real incomes, after housing costs, of the bottom 10 per cent fell by 13 per cent between 1979 and 1993/94 while other deciles experienced real growth of between 4 per cent (second 10 per cent) and 65 per cent (top 10 per cent). As a result local economies have been decimated and communities do not have the resources to sustain many facilities at a community level.'

Bob Line, a housing consultant writing for *Housing Magazine*, has said:[94]

> 'The bottom line is that pretty well all ways of analysing rent levels show that rents now need to fall for them to become affordable in the current climate of low wages at the bottom end of the employment market. Differences in approach and detail should not be allowed to obscure this.'

The Institute for Fiscal Studies consider that lowering social housing rents has significant advantages over benefit reforms in terms of financial returns to employment for social housing tenants:[95]

> '…the cut in rent levels affects the greatest number of people [and] does have a positive effect on the depth of benefit dependency. [Under] the other …reforms…escaping the HB system becomes much more difficult.'

---

93 'A level playing field', 12 March 1998

94 'Bring rents down to unlock the poverty trap', September 1997

95 *Housing Benefit and Financial Returns to Employment for Tenants in the Social Sector*, Fiscal Studies, February 1997 Vol 18

1. Housing associations/RSLs

Although average housing association rent increases are slowing down,[96] it has been pointed out that the assumption that rents will rise by 1 per cent more than inflation each year means that after 25 years tenants will be paying rents that are, in real terms, 28 per cent higher.[97] The NHF has acknowledged that although the RPI + 1% formula limits rental growth, it cannot be equated with achieving affordability.[98] While some RSLs are still questioning whether they can live with RPI +1%, the debate on rent reductions is starting to be heard in RSL spheres.

A recent study by Christine Whitehead and Alan Holmans compared different approaches to the provision of supply subsidies, the most effective mix of supply and means tested subsidies and the overall impact on public expenditure of increased provision of social housing.[99] They concluded that: 'overall, an effective, sustainable social sector investment programme is probably best encouraged by maintaining grant rate (or equivalent) subsidy at around the 50 per cent level.' The study also found that if the grant rate was increased from 50% to 70% this would give rise to additional public expenditure of around £50 million but would allow rents to be reduced from £62 to £46 per week.[100] Translating these rent reductions into tenants' lives using data from the Family Resources Survey would, the LHU has noted, reduce the number of working tenants caught in the poverty trap from about half to less than three eighths.[101]

In December last year the Government was asked about the public expenditure implications of reducing housing association rent levels:[102]

> **Dr. Iddon**: To ask the Secretary of State for the Environment, Transport and the Regions if he will estimate the gross cost to public funds of a reduction in housing association rents of (a) 10 per cent., (b) nine per cent., (c) eight per cent., (d) seven per cent., (e) six per cent., (f) five per cent., (g) four per cent., (h) three per cent., (i) two per cent. and (j) one per cent.; and what would be the cost net of savings in (i) housing benefits and (ii) public expenditure linked to the RPI
>
> **Mr. Raynsford**: There are no powers under which the Government could impose a general reduction in housing association rents. The calculations below are on the hypothetical assumption that the cuts in rent could be achieved and that housing associations would be

---

96 By January 1998 new let rents were rising at a rate below RPI plus 1%, NHF, *Rents Briefing*, January 1998

97 'A level playing field', *Housing Today*, 12 March 1998

98 NHF, *Rents Briefing: can we live with RPI plus 1%*, January 1998

99 NHF, *Funding Affordable Social Housing*, December 1997

100 ibid para 31

101 LHU, *Rents and Affordability*, January 1998

102 HC Deb 4 December 1997 cc 283-4W

fully compensated for their loss of revenue. The estimated gross cost and the cost net of savings in Housing Benefit are as shown. The figures represent the annual costs calculated on the basis of average housing association rents in 1996-97. The Department does not have a model for calculating the RPI-related savings in public expenditure arising from reductions in housing association rents.

Reduction in rents (per cent)	**Cost of compensating HA revenue loss (£ million per annum)**	**Net cost after savings in Housing Benefit (£ million per annum)**
10	298	86
9	269	77
8	239	68
7	209	60
6	179	51
5	149	42
4	119	34
3	90	25
2	60	17
1	30	9

As with the figures on the cost of reducing local authority rents (see below), a number of housing commentators view this as an affordable means of tackling the poverty trap and work disincentives. The Director of Housing Services at Hammersmith and Fulham, Barry Simons, has calculated that, after taking account of inflation effects and rent allowances, the net cost of a 10 per cent reduction housing association rents would be £20-30 million over 30 years.[103]

Roof Magazine has commented that a 10 per cent cut could be achieved by a three-year freeze in rents, with at inflation at current levels, if a one off cut is seen as too dramatic.[104] The problem with this approach is that injections of private finance into housing association development have been built on rising rents, which are inevitably met by housing benefit. Rent reductions may have a detrimental effect on lender confidence and the value of transferred housing stock.[105]

Achieving rent reductions does have resource implications for RSLs. Where they need to use surpluses to deliver reductions it may affect their ability to maintain their stock through in the absence of the reinstatement of capital grant for stock reinvestment. The NHF lists the

[103] 'Coming down', *Housing Today*, 21 May 1998
[104] *Roof*, January/February 1998, p.11
[105] ibid

following constraints under which RSLs operate and which may mitigate against the achievement of rent reductions:[106]

- Stock reinvestment may require rent increases beyond the proposed limit;
- LSVT organisations have clear commitments to rent guarantees and business plan objectives, which underpin initial private finance;
- Private finance and loan covenants of RSLs may have implications for revenue affecting the RPI plus 1% limit;
- There are specific operational difficulties where fair rents are converted to assured tenancies.

According to the February 1997 edition of *Social Housing,* associations' success in keeping rent increases down in the previous two years was 'achieved through reduced profitability and internal funding from reserves with adverse consequences for the sector's financial ratios.'[107] The author of this article concluded:[108]

> 'The time may therefore be coming when a growing number of HAs have to consider whether their primary objective is to provide affordable rented accommodation or to subsidise the government's provision of new social housing.'

One of the ideas that has apparently been floated as a means of controlling RSL rent levels is that of introducing a 'local reference rent' (LRR) for social housing. LRRs were introduced in January 1996 as upper limits for private rents in an attempt to curb housing benefit expenditure; LRRs are intended to reflect average market rents within a locality and are used as a yardstick for assessing all housing benefit entitlements. Local authorities are currently not obliged to refer the housing benefit applications of RSL tenants to rent officers for a comparison of the rent charged with the LRR. However, Steve Wilcox has pointed out that in 1994/95 English authorities referred more than 2,600 housing association cases to the rent officer and in more than 550 cases the maximum rent fixed as eligible for housing benefit was set below the asking rent by an average of 21 per cent, or more than £25 per week.[109]

It is the case that in certain localities and regions, particularly in the North of England, housing association rents for lettings of new dwellings exceed the average level of rents in the private rented sector.[110] Steve Wilcox has argued for some time that associations with the

---

[106] NHF, *Rents Briefing: can we live with RPI plus 1%,* January 1998
[107] 'Below-inflation rent increases squeeze HAs' bottom line'
[108] ibid
[109] *Unresolved Tensions: Grant, rent and benefit policies,* 1996
[110] Joseph Rowntree Foundation, *Housing Finance Review 1997/98,* p.152

highest rents are exposed to the risk that rents will be restricted for housing benefit purposes.[111]

2. Local authorities

The Association of London Government (ALG) reportedly submitted a response to the Government's consultation on the Comprehensive Spending Review in which it was suggested that consideration should be given to options that reduce guideline rent levels.[112] The London Housing Unit (LHU) has looked at the effect of a reduction in council rents on HRA resources and concluded that if a reduction was coupled with a requirement on councils to reduce annual rents, this would have a neutral impact on councils' cash resources.[113] The reasoning behind this is that if the guideline rent goes down, the subsidy to a council's HRA should go up pound for pound.

Towards the end of last year the Government responded to a Parliamentary Question on the public expenditure implications of reducing local authority rents by various percentages:[114]

> **Mr. Raynsford**: A reduction in Guideline Rent in 1998-99 for Housing Revenue Account local authorities in England would have the following estimated effects:

Present value (discounting to 1996-97) of effects from 1998-99 to 2027/28
1996-97 prices discounting to 1996-97

Guideline Rent reduction in 1998-99 (per cent)	Loss of gross rental income (£ million)	Saving in rent rebates (£ million)	Saving in public expenditure linked to the RPI (£ million)	Net public expenditure cost (£ million)
11	6,402	4,816	1,476	110
12	6,984	5,244	1,610	130
13	7,565	5,675	1,744	146
14	8,147	6,104	1,878	165
15	8,729	6,527	2,012	190
16	9,311	6,954	2,146	211
17	9,893	7,379	2,280	234
18	10,475	7,799	2,415	261
19	11,057	8,222	2,549	286
20	11,639	8,643	2,683	313

> Figures in the table have been rounded to the nearest £1 million. The calculations are derived from LAMOD, the Department's model for estimating the public expenditure effects of a change in Guideline Rent policy for local authorities. The results from LAMOD are sensitive to assumptions which are kept under continuous review.

---

[111] ibid p.13
[112] London Housing Unit Paper, *Rents and Affordability*, January 1998
[113] ibid
[114] HC Deb 4 December 1998 c.284W

In response to an earlier Parliamentary Question Nick Raynsford estimated that a 10 per cent reduction in guideline rents in 1998/99 for HRA local authorities in England would have a net public expenditure cost of £100 million over 30 years; this would amount to 1.7p for every £1 of rent reduction.[115] Given the potential benefits that could arise from pursuing a policy of rent reductions many housing commentators view this cost as eminently affordable.

The London Housing Unit's paper notes that the DETR economists are of the opinion that the national average council rent (£41.11 per week in England) is currently 'at its public expenditure minimising position'.[116] Using LAMOD, the LHU has calculated that increasing the rent above the England average starts to produce a cost to the Treasury when the increase is between 10 and 15 per cent.[117] The average weekly council rent in London is £54.17, 32 per cent greater than the average for England. The LHU concludes that 'rents in London are already above the DETR's public expenditure minimising level. The current high level of London council rents in relation to other regions could lend itself to arguments for a separate consideration of a London-specific rent reduction option.' The LHU also emphasises that the DETR figures take no account of the public expenditure cost of any work disincentive effect of high rents.

The main arguments advanced in favour of council rent reductions are:[118]

- The promotion of the Welfare to Work ethos by the introduction of affordable rents;
- Lowering rents would be seen as improving the value for money of the housing service;
- Lower rents would enable the local regeneration of areas with concentrations of council housing. By helping to increase the proportion of tenants in employment it would improve tenants' standard of living and boost local businesses by increasing the spending power of local consumers;
- A reduction in the depth of the poverty trap to make employment a meaningful option for tenants currently dependent on benefit.

The main objections to a policy of council rent reductions are:

- Council rents are already low compared to rents in other sectors;
- Lower council rents would widen the gap between council and RSL rents;

---

115 HC Deb 27 October 1997 c.726W
116 *Rents and Affordability*, January 1998
117 see Appendix 1
118 LHU, *Rents and Affordability*, January 1998

- Lower rents will not increase the money available to councils;
- A larger gap between council and RSL rents could make nominations to RSLs more difficult and could inhibit geographical mobility.

These objections seem to indicate a need for joint discussions between councils and RSLs with a view to developing a coherent rent system. The Institute of Rental Officers and Rental Valuers recommended in 1997 that 'there should be a uniform valuation system for all tenures where public subsidy is, or has been, in any way involved'.[119] The Institute favours the adoption of a rental valuation system for all social housing.[120]

3. Private sector

There are no current proposals to re-introduce rent controls in respect of assured and assured shorthold tenancies.

The Government's consultation paper in which it is proposing that all tenants (including secure tenants of RSLs), with a rent registered under the *Rent Agriculture Act 1976* or the *Rent Act 1977*, will have their rent increases limited by an Order made under the *Landlord and Tenant Act 1985*,[121] has been roundly condemned by landlords and tenants' groups alike. The proposed limits are RPI plus 10% for the first re-registration after the Order comes into effect and RPI plus 5% for subsequent re-registrations.

The National Federation of Residential Landlords has described the proposed ceiling on fair rents as 'grotesquely unfair'.[122] Not surprisingly the interests of landlords and tenants are diametrically opposed on the question of rent levels. Landlords are of the view that fair rents have been held at an artificially low level since the 1970s and that the rate of return has led to poor maintenance records. It *is* widely accepted that rent controls, coupled with security of tenure, made private lettings a relatively poor investment in the 1970s and 80s and that this contributed to the decline of the sector. The position of the National Federation of Residential Landlords is set out in its 1996/97 Report:[123]

---

119 *The Benefit of Value*, May 1997
120 ibid
121 *Rents: Limiting Fair Rent Increases*, May 1998
122 NFRL press notice, 20 May 1998
123 *Responsible Residential Renting*

> 'Fair rents are the subject of a fundamentally flawed system as evidenced by great inconsistencies in rent levels and serious misinterpretations of the law by rent officers and rent assessment committees. From a low base, fair rents fell by over 40% against retail prices and by over 60% against house prices during the 1970s. Subsequent above inflation increases (quietly phased) were inevitable but understandably unpalatable to some regulated tenants who came to regard the low point of fair rents as the norm. In 1989, the then new director of the Rowntree Trust, Richard Best, had the rent of his £65,000 dwelling calculated on a 4% net return plus official management and maintenance allowances. The resultant figure of £67 per week was three times local fair rent levels. Today many fair rents are still well below the 'fair market rents' postulated by section 70 of the Rent Act and some rent officers and rent assessment committees are alleging that nine years after the deregulation of new lets, there is still substantial scarcity sufficient to justify the discounting of market rents by as much as 40%. Landlords have learned with dismay that just when the courts are very belatedly making correct judgements about the determination of fair rents, the Department of the Environment, Transport and the Regions are seriously considering the capping of increases of fair rents on two yearly review.'

On the other hand, tenant activists have criticised the proposals for setting the cap too high. The Camden Federation of Private Tenants has expressed disappointment over the cap on the grounds that it could allow increases above the market level and that it will not assist tenants who cannot afford their existing rents.[124]

B. Housing benefit

Wilcox and Sutherland concluded that research on the impact of housing costs on household decisions about labour market participation supported the case for restraining rents:[125]

> 'This would enable a far greater proportion of working tenants to 'leap the ditch of the poverty trap with one bound', and take up a modestly paid job without any need for means tested help with housing costs.'

They go on to note that, despite rent restraint, many households, particularly one parent families, will have very little prospect of obtaining jobs that will totally free them from benefit dependency:[126]

> 'Even if overall social sector rent levels are reduced by a move back towards greater levels of bricks and mortar subsidies, even with rents as low as £40 per week, for example, over 75 per cent of the working lone parent tenants taking up housing association tenancies would remain eligible for housing benefit (CORE, 1996/97).'

---

[124] 'Tenants bitter over rent levels', *Inside Housing*, 29 May 1998
[125] *Housing benefit, affordability and work incentives*, December 1997, para 7.1
[126] ibid para 7.3

It is within this context that there is believed to be a case for improving the work incentive characteristics of the current housing benefit scheme even if action is taken to restrain the level of social sector rents.

1. Amending the existing scheme

The traditional approach to amending the housing benefit system to improve work incentives is to argue for a reduction in the rate at which claimants lose benefit as their incomes rise (the 'tapers'). A reduction in the taper rate from 65% to 60% would cost an estimated £120 million annually; this represents 1% of the total annual cost of housing benefit.[127]

Owing to the combined effect of the housing and family credit tapers and income tax a reduction in the housing benefit taper alone would only have a limited impact on tenants' incomes. It is also recognised that tenants do not generally understand the operation of the taper and that adjustments to it may only have a limited effect on tenant perceptions of work incentives. For these reasons it is felt that it may be more effective to focus on increasing the earnings disregards in the calculation of housing benefit entitlement. It is estimated that it would cost £150 million to double the earnings disregard for a single person from £5 to £10, and to increase the earnings disregard for all other households by £10 per week.[128] However, increasing earning disregards alone would also not deal with the overlap of the family credit and housing benefit tapers.

2. Integrated housing credit scheme

Given the limitations of the existing system of housing benefit in terms of its complexity and the effect of overlapping tapers, consideration has been given to adopting an alternative structure of housing benefit. As the Chancellor has announced the intention to introduce a Working Families Tax Credit scheme, one possibility is the development of a scheme that would harmonise tax credits with a tenure neutral 'housing credit' scheme. Wilcox and Sutherland have written:[129]

> 'With tax and housing credit schemes harmonised it should still be possible to promote the message that working households qualifying for tax credit would get the same help with housing costs that they would if they were out of work and receiving income support. The harmonisation of the schemes would still remove the overlap of tax and benefit tapers, and

[127] ibid para 7.9
[128] ibid para 7.13
[129] ibid para 8.19

> make a greater contribution to easing the poverty trap than could be achieved by simply reducing the taper rates of any individual component of the poverty trap.'

It is suggested that this might cost about the same as the cost of integrating the family credit and housing benefit schemes, an estimated £750 million.[130]

It has been rumoured that the Chancellor is coming down in favour of the replacement of housing benefit with a flat-rate tax credit system.[131] The adoption of this system, whereby benefit credits would be issued to claimants via their pay, could reduce benefit fraud. Unemployed claimants would receive payments towards their rent through their basic benefits. A flat rate scheme has the support of those who believe that tenants should 'shop around' for cheaper housing and that there is a need to end the incentive for landlords to inflate their rent levels.

Housing campaigners are reportedly concerned that a tax credit system would be complex to administer and would create new poverty traps if the scheme is not closely linked with income support levels.[132] There is little support amongst landlords for a move away from a system under which tenants can get 100% of their rent paid as this would leave them collecting small amounts of rent from a large number of people.[133] A flat rate system would also present the problem of dealing with varying rent levels. Lenders are not enthusiastic about a change that would mean that part of RSLs' rental income would come from income support as this viewed as a less certain source of rental income than housing benefit.[134]

3. A cost gap housing allowance scheme

These schemes are designed to assist only those households with housing costs above basic levels; implicit in this approach is a level of social assistance that can meet the minimum levels of housing cost. Typically these schemes involve an allowance towards only a part of the rent above a defined minimum level.

These schemes usually involve far less severe income tapers than apply in the UK housing benefit scheme and therefore they have attractions from a work incentive point of view; lower tapers are possible because housing gap schemes provide a lower level of help with housing costs than the UK scheme. As these schemes provide only a proportion of assistance with

---

130 ibid para 8.20
131 'Brown: End the housing benefit scam', *Independent*, 25 May 1998
132 'Credit rates poorly', *Inside Housing*, 29 May 1998
133 'Benefit of the doubt', *Roof Magazine*, May/June 1998
134 ibid

rents beyond a certain level households are required to meet a proportion of their rent from their incomes. If a cost gap scheme was implemented in the UK there would need to be increased income support allowances for households with housing costs below the chosen minimum threshold. An attempt to introduce a 'nil cost' cost gap scheme in the UK would be likely to result in large numbers of households being left with a net disposable income below basic income support levels. Wilcox and Sutherland note:[135]

> 'The use of a single national threshold level for housing costs, across all tenures, differentiated only to reflect the size of each household, is an inherent characteristic of cost gap schemes. Given the marked diversity of rent levels. Both regionally and as between tenures such a scheme would inevitably have far more severe effects in London and the South of England. Low income households would be less able to secure accommodation within the private rented sector.'

4. Regional/local threshold schemes

This would involve setting regional or local threshold levels above which rents are either partially or entirely ineligible for benefit. Wilcox and Sutherland have suggested that local reference rents could be used to set the mid point of a range of rents partially eligible for benefit; they give an example where a local reference rent of £60 is set with a band of rents 33 per cent above and below that level which are 50 per cent eligible for benefit.[136]

This kind of scheme could result in limited expenditure savings or could be expenditure neutral depending on the proportion of rents eligible for benefit within the proportional rent band. Transparency could be achieved by setting reference rents and proportional rent bands for local authority areas rather than for 'localities', and by setting local proportional rent bands for households requiring different sizes of accommodation. Improved administration could be achieved by referring only those cases to rent officers where the property is in such poor condition or in such a low rent locality that the reasonable market rent for the property was below the lower limit of the proportional rent band.

In areas with a substantial diversity of private sector rent levels some localities within individual local authority areas would be likely to be beyond the price range of tenants in receipt of housing benefit under this scheme. This could result in some restrictions on the availability of private rented housing to low income households. A recent survey by the Association of Residential Letting Agents found that existing housing benefit restrictions had

---

[135] *Housing benefit, affordability and work incentives,* December 1997, para 4.12
[136] ibid para 10.12

led to an increase in the number of landlords who refuse to let to benefit claimants; 48% of respondents to the survey said they would not let to people on housing benefit.[137]

In terms of social sector rents, if housing benefit rent limits for private rents are set more broadly than at present, rent policy in the social sector would also need to take account of those restrictions.

The key advantages of this type of scheme over that of a cost gap scheme are seen by Wilcox and Sutherland as:[138]

- The possibility of setting threshold levels where 100 per cent of housing costs are eligible for benefit at higher levels without involving increased basic benefit costs for households with very low housing costs.

- The threshold levels both for 100 per cent benefit eligibility, and the bands of rent levels where rents are only proportionately eligible can be set locally rather than nationally and therefore operate more sensitively.

[137] 'Claimants face private squeeze', *Inside Housing*, 15 May 1998
[138] *Housing benefit, affordability and work incentives,* December 1997, para 10.18

Appendix I

Changes in rebates and in RPI-linked expenditure as a percentage of change in gross rental income:

	Change in 1998/99 Guideline Rent				
	-10%	-5%	+5%	+10%	+15%
Change in rebates as % of change in gross rental income	75.2%	75.7%	76.6%	76.9%	77.2%
Change in RPI-linked expenditure as % of change in gross rental income	23.1%	23.1%	23.12%	23.1%	23.1%
Total change	98.3%	98.8%	99.6%	99.9%	100.3%

LAMOD, DETR, October 1997

Glossary

ADP	Approved Development Programme
ALG	Association of London Government
CML	Council of Mortgage Lenders
DoE	Department of the Environment
DETR	Department of the Environment, Transport and the Regions
HAG	Housing Association Grant
HRA	Housing Revenue Account
LHU	London Housing Unit
LRR	Local Reference Rent
LSVT	Large Scale Voluntary Transfer
NFHA	National Federation of Housing Associations
NHF	National Housing Federation
RAC	Rent Assessment Committee
RSL	Registered Social Landlord
SHG	Social Housing Grant
WFTC	Working Families Tax Credit