Title: REDUCING THE RIGHT TO BUY QUALIFYING PERIOD FOR SOCIAL TENANTS **IA No:** DCLG 1314	Impact Assessment (IA)
Lead department or agency: Department for Communities and Local Government	**Date:** 31/01/2014
Other departments or agencies: Homes and Communities Agency	**Stage:** Final Stage
	Source of intervention: Domestic
	Type of measure: Primary legislation
	Contact for enquiries: Dan Howard 0303 444 2625
Summary: Intervention and Option	**RPC Opinion:**

Cost of Preferred (or more likely) Option				
Total Net Present Value	**Business Net Present Value**	**Net cost to business per year** (EANCB on 2009 prices)	**In scope of One-In, Two-Out?**	**Measure qualifies as**
£1,309m to £1,832m	-£9.49m***	£0.9m	Yes	NA

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

Until recently, Right to Buy sales had been in long term decline. They have been reinvigorated as a result of more generous maximum cash discounts from April 2012, and a further increase to these for tenants living in London Boroughs in March 2013. The Government is concerned, however, that tenants are being forced to wait an excessively long period before becoming eligible for the Right to Buy, which is contrary to the requirements in force when the policy first came into effect. Reducing the qualifying period for the right to buy will enable more social tenants to meet their home ownership aspirations sooner, support social mobility and will help create and sustain mixed communities. Housing need remains high and building replacement homes for affordable rent from the additional receipts will help us to meet this need. The replacement programme will help support the sector & support economic growth.

NB: Section 119 (qualifying period) of the Housing Act 1985 also applies to the Right to Acquire. The impact of these changes to the Right to Acquire on Housing Associations has been considered but has been found to be negligible, so will not be covered separately.

What are the policy objectives and the intended effects?

Reducing the qualifying period for the right to buy is intended to boost home ownership for social tenants. This will support social mobility policy objectives and help aspiration - around 80% of people aspire to homeownership. One for one replacement of additional sales with affordable rented units will prevent Right to Buy sales depleting the affordable housing stock and will ensure our ability to meet housing need is not impaired. It has been estimated that there are around 1.9 million households in housing need in England. Using the Right to Buy sale receipts to invest in house building will also stimulate construction activity and support the economic recovery without the need to increase central Government borrowing.

What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)

Only one option is considered: reducing the qualifying period from five to three years. The one for one replacement policy is not being altered from its current form.

The chosen approach (to reduce the qualifying period to three years) is in line with the original Right to Buy policy and helps to avoid conflict with two-year flexible tenancies.

Will the policy be reviewed? It will be reviewed. **If applicable, set review date:** March 2015

Does implementation go beyond minimum EU requirements?			N/A		
Are any of these organisations in scope? If Micros not exempted set out reason in Evidence Base.	**Micro** No	**< 20** No	**Small** Yes	**Medium** Yes	**Large** Yes
What is the CO_2 equivalent change in greenhouse gas emissions? (Million tonnes CO_2 equivalent)			**Traded:** Unknown	**Non-traded:** Unknown	

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

Signed by the responsible SELECT SIGNATORY: .... Date: ....

Summary: Analysis & Evidence

Policy Option

Description: Reducing the right to buy qualifying period for social tenants.

Chosen policy option: Reduce the qualifying period from five years to three years.

FULL ECONOMIC ASSESSMENT

Price Base Year 2012	PV Base Year 2012	Time Period Years 60	Net Benefit (Present Value (PV)) (£m)*		
			Low: +£1,309m	**High:** +£1,832m	**Best Estimate:** +£1,517m

COSTS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low				
High				
Best Estimate	NIL		NIL	**NIL**

Description and scale of key monetised costs by 'main affected groups'

None.

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

**Transfer costs (£120k per Right to Buy unit and £156k to £161k per replacement unit) are as follows.

For local authorities and housing associations: the lost rental income (due to losing a social unit as a result of Right to Buy purchase); the costs associated with replacement affordable rent unit in terms of maintenance, repairs, debt servicing, and other resource provision. For HM Treasury: the increase in housing benefit payments associated with the Right to Buy sale (losing a social housing unit)

BENEFITS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit* (Present Value)
Low				**£1,309m**
High				**£1,832m**
Best Estimate				**£1,517m**

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

The social benefit associated with improving household consumption of low income households (£997m for additional units over the first three financial years of the policy or £94,000 per unit - both Right to Buy unit and replacement unit combined). The economic benefit of increasing housing supply (£291m for units over the first three financial years or £28,000 per unit). Wider benefits of improved labour mobility, better health and education outcomes and reduced use of temporary accommodation, associated with replacement affordable rent units (£229m for additional units over the first three financial years or £22,000k per unit). See table 7 for further details.

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

**Transfer benefits (£146k per Right to Buy unit and £138k per replacement unit) are as follows.

For local authorities and housing associations: the savings associated with repair, management and debt servicing interest payments by selling a Right to Buy home, and the benefit of rental income from replacement affordable rent homes. For local authorities/HM Treasury: the Right to Buy sales receipt (hypothecated to one-for-one replacement funding and local authority / housing association debt compensation). For HM Treasury: Housing Benefit savings associated with Right to Buy unit and replacement affordable rent unit.

Key assumptions/sensitivities/risks | **Discount rate (%)** | 3.5%

*Economic and social benefits above are presented for additional Right to Buy sales (and the associated replacement units) which occur over the first three financial years only (2014/15-2016/17). This is not a reflection of the policy being time limited.

**The costs and benefits incurred by Government, local authorities and housing associations have been presented in Net Present Value terms per unit in the non-monetised section above, but these are excluded from the economic appraisal given that they represent transfers rather than net economic impacts.

***Business impacts have been calculated but not included in the Total Net Present Value.

BUSINESS ASSESSMENT

Direct impact on business (Equivalent Annual) £m:			In scope of OIOO?	Measure qualifies as
Costs: 0.9	**Benefits:**	**Net: -0.9**	Yes	NA

Contents

SECTION 1: CONTEXT

1. To help more people realise their aspiration of home ownership and sooner, and to increase investment in further affordable housing, the Government intends to reduce the amount of time a household is required to have been in social rented tenure before being able to exercise the right to buy. Government aims to ensure that every additional home sold under the Right to Buy is replaced nationally with a new home for affordable rent.

2. Under the Right to Buy legislation, council tenants (and tenants of housing associations who transferred from council landlords) have the right to buy their home at a discount[1]. The policy has been a great success – since its introduction in 1980, almost 2 million households have exercised this right and can enjoy the benefits of homeownership including greater independence, security of owning a valuable asset and the right to change their home as they wish. “The Right to Buy was one of the most successful housing policies… because the policy enabled many households to become owner-occupiers who would not otherwise have been able to do so… It has been a positive influence in maintaining mixed communities in spatial terms. It has also provided a cheaper access point into owner-occupation for lower income employed households helping to sustain mixed communities as these properties are transferred into the market[2].”

3. However, the previous Government reduced discounts and the take-up of right to buy fell to an all time low. Indeed, warning was given that cuts to the discount rate would affect take up: “The data suggests that those affected by the ceiling were somewhat more likely to withdraw from purchase. They were also more likely to face questions about the affordability of their purchase. Withdrawal was associated with the need to make larger average payments. These effects appear to be becoming more pronounced with time[3].”

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[1] Right to Buy is available to secure tenants of local authorities and non-charitable housing associations. Assured tenants of housing associations who were secure tenants and have been transferred with their homes as part of a stock transfer from a local authority to a housing association also have the Right to Buy - this is known as Preserved Right to Buy. Broadly the same terms apply to both schemes.

[2] ODPM, Lessons from the past, challenges for the future for housing policy, January 2005

[3] ODPM, The Impact of the 1999 Changes to the Right to Buy Discount, May 2003

Evidence Box: The Right to Buy over time

- On introduction in 1980, the discount was 33-50% (depending on length of tenancy) capped at £25,000. The qualification period was three years,
- In 1984 the Government introduced the 'cost floor rule' for homes which had been built or renovated since March 1984 where more than £5,000 had been spent on the property. The 'cost floor rule' provides that the discount cannot reduce the purchase price below a certain level. The discount range also changed to 32-60%. The qualification period was decreased to two years.
- In 1987, the cap was increased to £35,000, and a higher discount of 44-70% was established for flats. The date for the cost floor was also changed from March 1984 to March 1974
- In 1989, the cap increased from £35,000 to £50,000 and the cost floor rule changed to include buying the property and the effective time became eight years.
- In 1999, the Government reduced the maximum discount, by introducing regional caps - from £22,000 in the North East to £38,000 in London. The effective time for the cost floor was also changed to 10 years.
- In 2003, the maximum discount was cut to just £16,000 in 41 local authority areas in London and the South East.
- The Housing Act 2004 then increased the qualification period for Right to Buy from two years to five years of tenancy (this had the effect of changing the discount range for houses from 35-60% and 50-70% for flats, both subject to cash caps) for those taking up a tenancy from 2005 onwards.

4. As a result of these changes, the average Right to Buy discount, as a percentage of the sale price, fell significantly over the last 10 years; from a national average of 50% in 1998/99 to just 25% in 2010/11[4]. In London, the fall has been even more pronounced with the average discount falling from 53% in 1998/99 to 13% in 2010/11[5].

5. The Government remains determined to continue to invigorate the policy to give a new generation the opportunity of homeownership. As a result of raising the discount caps in April 2012 and at Budget 2013, the discounts have raised homeownership to affordable levels, boosting Right to Buy sales substantially. The money from these additional sales is being invested in paying down the existing housing debt and building new housing for affordable rent.

6. Currently, to qualify for the Right to Buy or the Preserved Right to Buy, tenants must have spent *five* years as public sector tenants. Once eligible, current discount rates are:

   - for houses: 35 per cent of the property's value plus 1 per cent for each year beyond the qualifying period up to a maximum of 60 per cent[6]
   - for flats: 50 per cent plus 2 per cent for each year beyond the qualifying period up to a maximum of 70 per cent

7. For both houses and flats, the maximum cash discount which can be received, regardless of the percentage discount entitlement, is £75,000 (£100,000 for tenants living in London Boroughs)[7].

8. One way to give more social tenants the opportunity to own their home and sooner is to reduce the qualifying period for the Right to Buy from five years to three years. The simplest way to do this would be

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[4] DCLG live table 643.
[5] DCLG live table 643.
[6] The Government has announced plans to increase the maximum discount for a house to 70% of its value. This change is expected in Spring 2014.
[7] The Government has announced plans to increase the maximum cash discount annually in line with the consumer price index (CPI) rate of inflation. This change is expected in Spring 2014.

to maintain the existing discounts beyond the five year qualifying period, whilst offering the starting discount rates in each of the preceding years as a flat rate within the new qualifying period. So with a three-year qualifying period, tenants must have spent three years as public sector tenants. Once eligible, the new discount rates would be:

- for houses: 35% per cent of the property's value *in the first two years and then* plus 1 per cent for each year beyond, up to a maximum of 60%
- for flats: 50% per cent of the property's value *in the first two years and then* plus 2 per cent for each year beyond, up to a maximum of 70%

9. The option that Ministers have chosen is to reduce the qualifying period from five years to three years. This option was chosen because it meets the policy objectives, in particular the potential to increase take up of Right to Buy and is considered, currently, that a three year qualification period represents a reasonable length of tenancy on which to accrue the Right to Buy. A three year qualifying period reverts the Right to Buy scheme back to the period when this important right was first introduced.

10. The Government remains committed to the aim that every additional home sold under Right to Buy is replaced by a new home nationally, and receipts from sales will be recycled towards the cost of replacement (and repayment of debt). As is currently the case, the receipt allowed to be used to fund replacement will only be a proportion of the cost of a new home. This is because most of the funding for new affordable rented homes comes from borrowing by the provider against the future rental income stream; and, in many cases, cross-subsidy from the landlord's own resources, including land.

11. As housing associations are independent organisations, we do not wish or intend to mandate what they do with any receipts they retain. In practice, any surplus receipts (after costs and compensation for lost rental income) retained by housing associations are likely to be used to support new build and other public benefits. Where receipts are shared with councils, it is our expectation that housing associations will work with them to develop replacement homes. For stock transfers that take place in the future we would expect housing associations to retain the whole receipt, and, in return for a lower payment for the stock (and hence higher level of support from Government for debt write-off), we would seek specific agreement on how surplus receipts will be used for new build.

SECTION 2: PROBLEM UNDER CONSIDERATION

Right to Buy

12. The Government wishes to help more people to realise their aspirations of home ownership and sooner. The Right to Buy programme has been immensely successful in helping to deliver this objective but before the reinvigoration in April 2012, sales had been in long term decline: Local Authority and Housing Association sectors combined sales amounted to fewer than 4,000 units in 2010/11. This is compared to a high in the early 1980s of over 160,000 sales per annum and a peak of over 80,000 sales per annum in the 2000s. Sales have fluctuated since the introduction of Right to Buy but the general trend has been downwards. This is likely to be a result of less generous discounts; increasing house prices; a general decline in the quality of the remaining stock as 'better' quality properties have been purchased; the changing socio-economic characteristics of social tenants; and, from 2007, adverse credit conditions.

13. However, as a result of the changes to Right to Buy in April 2012, Right to Buy sales increased substantially with Local Authority Right to Buy Sales reaching nearly 6,000 in 2012/13 – a doubling on the previous year. The Government would like to go further with continued increases in Right to Buy (and Preserved Right to Buy) sales in the coming years, allowing more social tenants to gain access to homeownership and sooner and thereby meet their homeownership aspirations. The scale and rate of the increase in sales will depend not only on the generosity of the discount policy, but also fundamentally on economic and financial (mortgage market) conditions.

Replacement

<u>Meeting need</u>

14. Historically, the Right to Buy policy has not involved the replacement of sales with new social or affordable homes. This has been a key criticism of the policy in the past, given the rising levels of housing need and demand.

15. Without one for one replacement of Right to Buy sales with affordable rented homes, the social and affordable housing stock has fallen. This is a problem because of the prevalence of housing need. It has been estimated that there are around 1.9m households in housing need in England.[8] Increasing the affordable housing supply remains an important way of meeting housing need and alleviating housing pressure, especially for the most vulnerable households, which is why we will continue to use the one for one replacement policy.

<u>Supporting economic growth</u>

16. Construction output and jobs have suffered during the recession, more than other sectors, with housing output declining by around 40% from the peak; net additions were around 121,000 in the latest year compared to over 200,000 in 2007. On the latest estimates from the Office for National Statistics, the sharp decline in construction accounted for a fifth of the 7.1% decline in GDP from peak to trough in the recession and house building is now at its lowest level since the 1920s. The use of the additional Right to Buy receipts will provide a stimulus to construction and the wider economy that does not involve additional central Government borrowing.

[8] http://www.communities.gov.uk/documents/housing/pdf/1776873.pdf

SECTION 3: RATIONALE FOR INTERVENTION

Right to Buy

17. In general, social tenants cannot afford to buy their homes at market prices. The Right to Buy discount, increases the financial incentive and improves affordability for social tenants to exercise their Right to Buy. By extending this to a larger pool of social housing tenants, it will enable more households to exercise their Right to Buy and sooner, which will boost homeownership, helping social tenants meet their aspirations. This returns the qualifying period for the Right to Buy to the length it was when the policy was first introduced, removing arbitrary barriers which were put in place by the previous administration.

18. The total stock of social sector housing today is approximately 4 million properties. In around 1.3 million of these, the head of the household is in work. Making reasonable assumptions around borrowing and transaction costs, we believe that nearly 250,000 of these households both have the Right to Buy and could afford to do so. Many of these households may also end up financially better off in the medium to long term given the acquisition of an asset and the implied low loan to value repayment mortgage which in many cases may be cheaper to service than paying social rents.

One for one replacement

Meeting need

19. Replacement with affordable rented homes builds on the funding model used in the 2011-15 Affordable Homes Programme, launched in July 2011 (which had the innovative ‘affordable rent’ model at its heart and is expected to produce up to 170,000 new affordable homes by 2015). This ensures that our ability to meet housing need is not impaired by the additional Right to Buy sales. The new homes that are built will add to the total stock of housing so that, combined with the previously announced Affordable Homes Programme, the affordable housing stock should rise over the Spending Review period (2011/12-2014/15).

20. These new homes will also help constrain Housing Benefit expenditure because the households being provided with the new affordable rent homes, some reliant on Housing Benefit, will have lower (affordable) rents than they would have to pay in the private market.

21. The use of the additional Right to Buy sales receipts to raise the capital to fund construction and help stimulate the wider economy does not involve additional central Government spending or borrowing which is imperative given the pressing need to reduce the budget deficit.

Supporting economic growth

22. During the recession, the UK economy contracted by 7.1% from peak to trough, according to the latest Office for National Statistics estimates, with the fall in construction output contributed around a fifth of this. Construction has been amongst the hardest hit sectors of the economy. It follows that restoring output to pre recessionary levels would support economic growth.

23. The housing construction associated with the one for one replacement policy will continue to help support economic recovery and growth in the near term. However, the number of homes that will be built over the current Spending Review will depend on the number of Right to Buy sales, and there will be a time lag before the sales receipt translates into a housing ‘start’. Given the current economic conditions,

it is much less likely that this building activity will displace other private sector building. Housing output is also more labour intensive than most other sectors of the economy, due to strong domestic labour supply chain effects.

SECTION 4: POLICY OBJECTIVE AND OPTION CONSIDERED

24. The overarching policy objectives for an higher level of Right to Buy sales and replacement combined are:

- to drive up Right to Buy take-up, thereby helping more people to realise their aspiration of home ownership;
- to ensure value to the government and a sufficient average sales receipt to be able to fund replacement homes for affordable rent;
- to protect the increase in overall affordable housing supply over the current Spending Review period to meet housing need
- to provide an investment stimulus to housing construction to support economic output and growth, without increasing central government borrowing.

25. We consider one option for extending the Right to Buy sale policy: Reduce the qualifying period from five to three years

26. The following pages consider this option, with an upfront explanation covering the approach and methodology taken.

27. The option that Ministers have chosen is to reduce the eligibility period from five years to three years. This option was chosen because it meets the policy objectives, in particular the potential to increase take up of Right to Buy. The qualifying period set when the policy was first introduced in 1980 was three years and so the proposed policy change reverts the policy back to its original intentions. The 30 year Net Present Value under this approach is positive, and the policy option results in significant net economic benefits.

SECTION 5: OPTION APPRAISAL AND METHODOLOGY

Take up

28. We estimated Right to Buy take up under the new Right to Buy policy using a module of the Department's Affordability Model. This was developed and built by leading housing economists at Reading University, with the latest development work to the model commissioned in June 2008 and concluded in summer 2010.

29. Within this model, Right to Buy sales, at a sub-national level, are estimated as a function of:

- Local authority housing stock
- Average Right to Buy discount percentage
- Mortgage interest rate
- House prices (both level and rate of change)

30. These were found to be the (statistically) significant variables and the model has an R-squared value of 0.68, which means the model explains roughly 70 per cent of the variation in Right to Buy sales. However, the model under-predicts the boom in sales up to 2003 and under-predicts the fall in sales following the credit crunch in 2008. Therefore, whilst the model performs reasonably well over time, it does not fully (or immediately) capture short term effects such as the influence of expected capital gains or credit restrictions.

31. Aside from average discount rates, we have selected a common set of assumptions for the other variables in the model. These are:

- Local authority housing stock. We assume the stock declines in line with Right to Buy sales.

- Mortgage rates. Based on Bank of England Inflation Report (implied forward rates).

- Regional House prices. Based on Office for Budget Responsibility projections.

32. The model predicts an initial increase in sales with an increased discount. This is a result of house prices and interest rates remaining initially low. However, rising interest rates and house prices eventually produce downward pressure on levels of sales.

33. Policy delivery will also have a bearing on future sales associated with increasing average discount rates and this is not captured in the modelling. For example, take-up will depend on factors such as publicity, guidance and assistance for prospective buyers, and wider support in relation to constraints such as buyer confidence and credit availability. Therefore given a particularly strong and well targeted programme of communications, for example, take up may be higher in the early years following a change in the discount rate than that predicted by the model.

34. Evidence from previous Right to Buy policy changes suggest that there was a degree of information failure and therefore provides evidence to suggest there may be room for measures to boost take up. A report assessing the impact of changes to the Right to Buy policy in February 1999[9] indicates that only one third of respondents were aware of the changes and only just over half of these respondents heard about the change before they applied.

35. The proposed reduction of the qualifying period for social tenants also applies to those who may obtain their Right to Acquire. The Right to Acquire (RTA) was introduced in the Housing Act 1996 to help

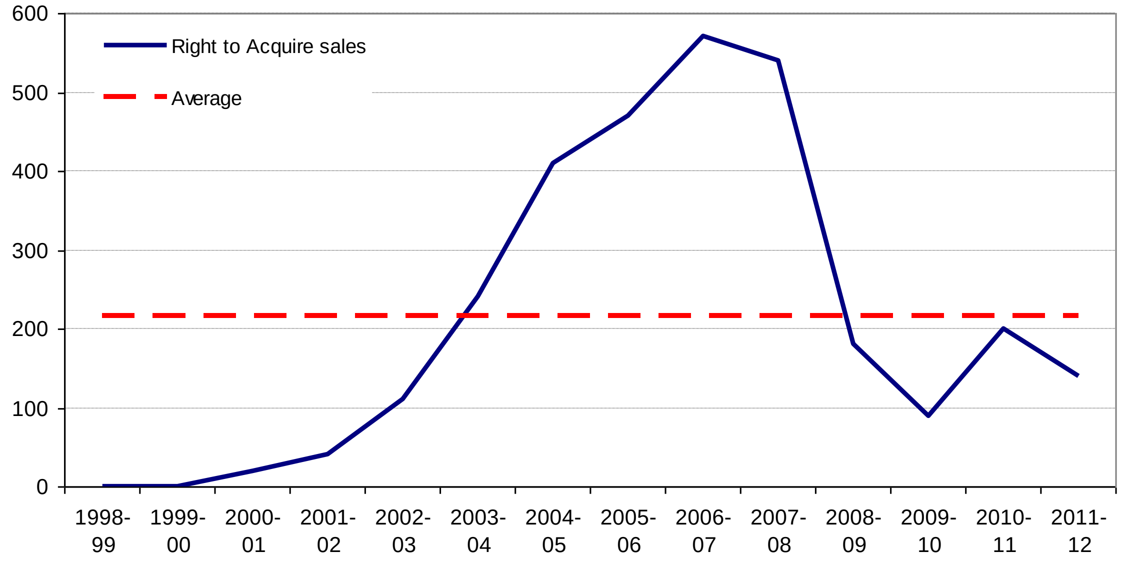
[9] http://www.communities.gov.uk/documents/housing/pdf/138199.pdf

eligible housing association tenants buy the property in which they live. The scheme only applies to properties built or acquired by housing associations, both charitable and non charitable, with public funds from 1 April 1997 onwards. Properties built before this date are exempt as it was not considered fair or reasonable to require housing associations to sell properties at a discount, which have largely been provided with private money and not funding from the public purse. Properties transferred from a local authority to a housing association after 1 April 1997 are also eligible. To qualify currently, housing association tenants must have spent five years as a public sector tenant and also live in a property that qualifies. Under the scheme, tenants are eligible for a discount ranging from £9,000 to £16,000 depending where their home is located. The Right to Acquire is offered on a different basis to the Right to Buy, including the level of discount, to reflect the different tenancy and type of landlord. The proposed change to the qualifying period for the Right to Buy from five to three years will also apply to the Right to Acquire. However, there are no proposals to extend the Right to Buy discount to housing associations. This is because, unlike local authorities, housing associations are private, independent not for profit, bodies often with charitable status. Extending the Right to Buy to housing associations would only be possible through central Government subsidy. In the current climate of fiscal pressures this is not considered an appropriate use of Government funding. In addition, if housing associations are obliged to consistently sell off their stock at substantially less than market value, they may find it difficult to borrow, which could impact adversely on their repair and maintenance programmes and affect the future provision of affordable housing.

36. The proposed change will therefore not change the discounts available to tenants under the Right to Acquire. Housing Association tenants with three years qualifying period will continue to be entitled to the discount set out in 'The Housing (Right to Acquire) (Discount) Order 2002'. Reducing the qualifying period for the Right to Acquire will simply enable those tenants who can afford it to meet their home ownership aspirations more quickly.

37. We have not included the impacts on Right to Acquire for a number of reasons. Firstly, and most importantly, is that the number of Right to Acquire sales have been very low since the introduction of the policy, as can be seen in the following chart. Another reason to suggest that the effect from Right to Acquire will be nominal is that the maximum discount available under Right to Acquire is £16,000, compared to £75,000 under Right to Buy (£100,000 in London).

Annual Right to Acquire sales



Cost-benefit analysis

38. Two approaches to cost benefit analysis are followed. One follows HM Treasury Green Book Appraisal methodology and considers the net economic impact of the policy in terms of a) the social benefit of improving household consumption of low income households, b) the economic benefit of increased housing supply and c) the economic benefit of increased construction. This gives rise to the best estimate, high and low Net Benefit figures provided in the summary section on page 2. Table 7 breaks these figures down into separate parts. The Green Book Appraisal is set out in Section 8. The other approach, which is set out below in paragraph 39 onwards, considers the net present value of the policy changes to the public sector (Government, Local Authorities and Housing Associations) and is an assessment of financial flows. The costs and benefits incurred by Government, local authorities and Registered Social Landlords, excluding administrative costs, are not included in the economic appraisal although they are included along with non-monetised impacts in the analysis of financial flows (e.g. Table 5). In accordance with the Green Book, they represent transfers from one part of society to another, for which no good or service is obtained in return, rather than net economic impacts.

Value (Net Present Value) to the public sector

39. Although the Right to Buy discount and one-for-one replacement are part of one policy (the second cannot happen without the first), we appraise them separately. This is because they are essentially two separate decisions: (i) to reduce the qualifying period for Right to Buy to increase sales, and (ii) to replace sales one for one with affordable rent homes using the proceeds - a continuation of the replacement policy.

40. For each policy, we compare the Net Present Value of the real terms costs and benefits over the assessment period, against a counterfactual of the status quo. The use of the status quo will not reflect the opportunity cost of being unable to pursue alternative policies in the future, e.g. instead of selling social homes under a Right to Buy policy, converting them to affordable rent homes.

41. We assess Net Present Value over both 30 and 60 years. 60 years could be considered a long period of time in appraisal terms but is consistent with some past practice. The advantage of a longer 60 year period is that the full value of the asset is captured in the Net Present Value analysis without needing to make an assessment of residual value, which can be subjective. It also more closely reflects the lifetime of homes. However, the advantage of a shorter 30 year period is that it minimises the so-called divergence problem, where small changes or differences in the initial values (including in our assumptions) can have a big and potentially spurious impact on the results, a problem that is more severe the longer the period. However, due to the subjective nature of the residual asset values, they are not included in the 30 year Net Present Values set out in this paper, but are set out alongside.

42. The figures presented are for a sale in the first year of the policy but, in reality, Net Present Values will differ according to the year of sale. There are a number of reasons for this:

    1. the cash cap is fixed in nominal terms so if house prices are generally rising with time, the effective generosity of the cash cap will be falling. So the Net Present Value will tend to be more positive for sales further into the future.

    2. macroeconomic variables (e.g. inflation), Local Authority rent, and Local Housing Allowance for rents increase at a different rate in the next few years compared with their increases in the longer run - this will affect the balance of benefits and costs depending on the year of sale

43. We consider only the net present value for the public sector of these policies. The public sector (or “government”) is taken to mean both central and local government combined.

44. The key Net Present Value assumptions are set out below.

Macroeconomic assumptions

Table 1: Macroeconomic Assumptions

	2013	2014	2015	Beyond
Retail Price Index	2.9%	3.1%	3.6%	3.2%
Consumer Price Index	2.1%	2.0%	2.0%	2.0%
GDP deflator	2.8%	2.5%	2.5%	2.7%
Debt interest	5.0%	5.0%	5.0%	5.0%

Policy assumptions

- Local Authority rent = Retail Price Index + 2.5% to 2015 to approximate Local Authority rent convergence criteria, Retail Price Index + 0.5% beyond
- Local Housing Allowance rent = Consumer Price Index 2013-16, Retail Price Index + 0.5% 2017 and beyond.

Local Housing Allowance inflation for 2012 is assumed to be 2% which reflects an announcement from the Department for Work and Pensions Ministers in December which confirmed that Local Housing Allowance rates will be frozen from April 2012 before Consumer Price Index uprating from 2013.

- Market rent = Retail Price Index + 0.5%
- Repairs Management and Maintenance = Retail Price Index to 2041, Retail Price Index +0.5% 2042-71

Table 2: Rent assumptions

	2013	2014	2015	Beyond
Local authority rent inflation	5.4%	5.6%	6.1%	3.7%
Local Housing Allowance rent inflation	2.1%	2.0%	2.0%	3.7%
Market rent inflation	3.7%	3.7%	3.7%	3.7%
Repairs, Maintenance and Management inflation	2.9%	3.1%	3.6%	3.2%

Key Housing Benefit assumptions

- Percentage of those exercising their Right to Buy who are on Housing Benefit = 10% (full housing benefit equivalent[10]). However, due to the continued uncertainty and the potential for the increase in the discount rates to increase this figure, sensitivity analysis is presented in Section 9.
- Social let term = 15 years (i.e. we assume that the Right to Buy purchaser would have otherwise left their property after 15 years).
- Percentage of social tenants on Housing Benefit = c.60% (full housing benefit equivalent[11]). This varies regionally.

[10] This is a simplifying assumption. We do not expect 10% of potential Right to Buy purchasers to be on full Housing Benefit, rather we expect that a larger number of tenants will be on partial Housing Benefit which amounts to an equivalent on 10% on full Housing Benefit. However, as mentioned above, there is a high degree of uncertainty associated with this assumption.

[11] Again, this is a simplifying assumption.

SECTION 6: RIGHT TO BUY

Preferred option: Reducing eligibility period from five years to three years

Additional Take-up

45. We estimated the impact on RtB sales of the April 2012 changes to increase the cash cap to £75,000 across the country using the Department's Affordability Model as described in Section 5 above. As a result of the policy, sales are forecast by the model to rise from around 7,000 RtB and PRtB sales to around 17,000. This was manifested through an increase in the effective discount rate from around 25% to around 44%. The additional sales as a result of this policy have been estimated using an off model adjustment applying a ratio of the total number of households eligible under the 5 year policy and the total number of households eligible under the new 3 year policy. These numbers are obtained from the English Housing Survey. This gives a ratio of 1:1.13.

Table 3: Take up under preferred policy option (Reducing eligibility from five to three years)

		2014/15	2015/16	2016/17
Baseline RtB sales	Lower	na	na	na
	Central	**17,250**	**23,000**	**26,500**
	Upper	na	na	na
Additional Right to Buy / Preserved Right to Buy sales	Lower	2,500	3,250	3,500
	Central	**2,750**	**3,500**	**4,250**
	Upper	3,250	4,250	5,000
Total Right to Buy / Preserved Right to Buy sales	Lower	18,000	23,250	25,250
	Central	**20,000**	**26,500**	**30,750**
	Upper	23,250	32,250	37,750

Average sale receipt and funding replacement

46. The average gross Right to Buy sale receipt is estimated at £72,175 in the first year of the policy. After compensation to the local authority of the debt position, the implied average net sale receipt is £55,500. Under our central assumptions we estimate that this would be sufficient for one for one replacement without the need for conversions within and beyond the current Spending Review period.

Value (Net Present Value) to the government

47. The table below presents the Net Present Value breakdown per home in the first year of the preferred policy option, versus the current Right to Buy policy, for England. The 30 year Net Present Value figure is positive at £38,075, and the 60 year Net Present Value figure remains positive at £5,975.

Table 4: Net Present Value of Right to Buy sale, England

Benefits		Present value	
		30 years*	60 years
- sale receipt maintaining existing discount ranges and with a £75k cash cap		£72,175	£72,175
- maintenance cost savings		£24,800	£36,500
- major repair cost savings		£18,800	£27,700

- management cost savings		£15,900	£23,400
- debt servicing interest savings		£7,400	£10,200
Benefits subtotal		***£139,075***	***£169,975***
Costs			
- loss of rental stream		-£95,000	-£144,100
- extra housing benefit costs		-£6,000	-£20,000
Costs subtotal		***-£101,000***	***-£164,100***
Net position		**£38,075**	**£5,975**

* The 30 year assessment excludes the potential residual value of the property. Residual values are incredibly subjective and difficult to calculate in an accurate fashion, particularly for non-market assets, therefore should be treated with caution. Using the estimated net rental income from year 31-60 as a proxy, we estimate that the residual value of the property could be in the region of £21k. Including the residual value would worsen the net position.

** Sale receipt is lower than in the Reinvigorating Right to Buy Impact Assessment (£72,500) to account for the increase of the cash cap in London to £100,000. The higher cash cap raises the effective discount rate which lowers the national average sale receipt.

Burdens on Local Authorities

48. We currently provide for a set administrative allowance of £2,850 in London and £1,300 elsewhere, per completed sale, which includes a 50% uplift to cover the cost of withdrawn applications. We do not propose to change this as we believe local authorities should be able to cover their costs of processing applications (and include a contribution towards the costs of aborted applications). This will also encourage efficient administration.

SECTION 7: PRESERVED RIGHT TO BUY IN THE HOUSING ASSOCIATION SECTOR

Tenants benefiting

49. Assured tenants of housing associations who were secure tenants of a local authority and have transferred with their homes as part of a stock transfer from the local authority to a housing association also have a right to buy – this is known as the Preserved Right to Buy. Eligibility, discount rates and caps applying to Right to Buy automatically apply to Preserved Right to Buy.

50. The number of tenants with Preserved Right to Buy is not known directly but, on the basis of a number of reasonable assumptions, we estimate that about 620,000 tenants in the housing association sector are eligible.

Allocation of receipts

51. Arrangements for distributing receipts from Preserved Right to Buy sales in the housing association sector are varied and depend on the local agreements made with transferring councils. In most cases, Preserved Right to Buy sale receipts are shared between the housing association and council but, for early transfers (pre 1991-92), housing associations generally retain the full receipt. Where receipts are shared, the portion retained by the association covers sales costs and compensates for lost rental income. This is important so that the sale has minimal impact on the association's business plan and it can continue to meet loan covenants.

52. Again, we do not have precise figures for the number of Preserved Right to Buy tenants in associations with sharing agreements but we have estimated the figure at around 530,000 – about 85% of the tenants eligible for Preserved Right to Buy.

Arrangements for replacement

53. As housing associations are independent organisations, we do not wish or intend to mandate what associations do with any receipts they retain. In practice, any surplus receipts (after costs and compensation for lost rental income) retained by associations are likely to be recycled to support new build and other public benefits. We estimate that around 70% of tenants (440,000) with Preserved Right to Buy are in associations with development programmes participating in the 2011-15 Affordable Homes Programme.

54. For stock transfers that take place in the future we would expect housing associations to retain the whole receipt, and, in return for a lower payment for the stock (and hence higher level of support from Government for debt write-off), we would seek specific agreement on how surplus receipts will be used for new build. Transfer landlords would alternatively be able to pass surplus receipts to a developing provider to use for new build or surrender surplus receipts centrally.

Burdens on Housing Associations – One In Two Out

55. There are three possible areas of impact upon housing associations:

- cost of one for one replacement of housing purchased under the Right to Buy;
- costs of administering sales; and
- possible impact upon their business due to loss of assets and therefore borrowing capacity.

56. Housing associations are independent organisations and we cannot therefore mandate the use of any receipts from Right to Buy sales that they retain, including for one for one replacement. However, in

practice, any surplus receipts (after costs and compensation for lost rental income) retained by associations are likely to be recycled to support new build and other public benefits.

57. We expect take-up of the Right to Buy and Preserved Right to Buy to be higher than current levels, because of our proposals to decrease the qualifying period from five years to three years, and that the costs of administering sales (successful and withdrawn) will therefore rise correspondingly.

58. Under our original Right to Buy proposal, we expected take-up of Right to Buy to be substantially higher than current levels, and therefore the costs of administering sales (successful and withdrawn) would rise correspondingly. Councils could deduct the administration and transaction costs of successful sales from Right to Buy receipts but there is no allowance for costs relating to applications under Right to Buy which fall through and do not result in a sale.

59. The Reinvigorating Right to Buy and one for one replacement consultation document of December 2011[12] published estimated average administration costs per sale based on data supplied by local authorities through the annual audit forms. Starting from 2008/09 this gave a three-year average of £3,107 for London and 1,888 for the rest of England. This also gave transaction costs of £2,360 for London and £1,070 elsewhere based on the 40th percentile of administration costs with a 25% uplift to take account of withdrawn applications. As a result of responses to the consultation it was decided to increase the uplift from 25% to 50% leading to the administration and transaction cost estimates of £2,850 in London and £1,300 elsewhere. We propose to continue providing for set administrative costs of £2,850 in London and £1,300 elsewhere, which includes a 50% uplift to cover the cost of withdrawn applications. We have received no negative feedback from local authorities on these provisions for administration costs which were based on historic administration costs over a 3 year period. This will mean authorities should be able to cover their costs of processing applications (and include a contribution towards the costs of aborted applications) but will also encourage efficient administration.

60. This estimate agrees with work carried out by the HCA looking at the impact of PRtB on housing associations. This work assumed average administration costs to housing associations of £2,000 per sale, a figure that reflects the average administrative fees set out in a sample of 14 sharing agreements which the HCA has had access to. The duties and requirements on housing associations to process Preserved Right to Buy applications under the Housing Act 1985 are the same as the duties and requirements on local authorities to process Right to Buy applications. The change in the qualifying period from five years to three years does not change these duties nor does it affect the costs associated with administering applications. Stock transfer agreements are private commercial contracts between local authorities and housing associations. The costs associated with administering sales (successful and withdrawn applications) in their transfer agreements will have been based on those experienced by the local authority prior to the stock transfer taking place. Whilst we accept that abortive Preserved Right to Buy applications may rise, so will the overall receipts from increased applications, and these should therefore be sufficient to cover the administration costs. We would expect housing associations to take account of the change from five years to three in their business planning, and the impact of this change should be manageable under their existing arrangements. In discussions with housing associations about the proposed change, administration costs were not raised as an area of concern.

61. Assuming that housing associations face the same administration costs the administrative costs that are used for local authorities in paragraph 48 of £2,850 in London and £1,300 for the rest of the country give an estimated total cost of administering sales as £10.7 million over a ten-year period from 2014/15. These figures are based on estimates of approximately 1,200 additional Preserved Right to Buy sales in London and approximately 5,600 additional Preserved Right to Buy sales for the rest of the country. This is derived from the following additional PRtB sales as a result of the eligibility policy

[12] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/8420/2053578.pdf

Table 5: Additional Housing Association Sales and Administration Costs 2014/15 to 2023/24

	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24
Additional HA sales (PRtB)										
London	114	155	181	183	160	121	99	84	73	64
Rest of country	507	669	773	786	705	560	473	415	374	341
England	621	824	953	969	865	681	571	499	446	405
Additional HA admin costs (£m)*										
London	0.3	0.4	0.5	0.5	0.5	0.3	0.3	0.2	0.2	0.2
Rest of country	0.7	0.9	1.0	1.0	0.9	0.7	0.6	0.5	0.5	0.4
England	1.0	1.3	1.5	1.5	1.4	1.1	0.9	0.8	0.7	0.6

* Applying admin costs of £2,850 in London and £1,300 outside London. This gives an Equivalent Annual Net Cost to Business of £0.9m

62. We then distribute this £10.7 million on an annual basis to arrive at an Equivalent Annual Net Cost to Business of £0.9m. We estimate projected PRtB sales very simply as a figure equal to 30% of local authority RtB sales. Therefore we model local authority RtB sales using the department's affordability model as described in the previous section 5. We then estimate PRtB sales by applying the 30% uplift to the modelled RtB sales. This uplift was estimated on the basis of historical outturn data which show a ten-year average uplift of 23%, whilst recognising the higher outturn figures in recent years i.e. 35% in 2010/11 and 42% in 2011/12.

Table 6: RtB sales, PRtB sales and PRtB sales as % of RtB sales[13]

Year	Local Authority RtB sales	Housing Association PRtB sales	PRtB sales as a % of RtB sales
2003/04	69,577	14,525	21%
2004/05	49,983	8,665	17%
2005/06	26,654	6,356	24%
2006/07	17,684	4,835	27%
2007/08	12,043	3,150	26%
2008/09	2,869	996	35%
2009/10	2,375	804	34%
2010/11	2,758	956	35%
2011/12	2,638	1,106	42%
2012/13	5,940	2,458	41%
10 year average	19,252	4,385	23%

[13] Figures have been reproduced from DCLG live table 671

63. Where associations retain all receipts from sales, we believe overall receipts will be sufficient to cover administration and transaction costs as well as any outstanding debt on properties sold. An illustrative example is provided in the following table which is of a similar form to table 4 but covers both the sale and the replacement unit. However, as associations may not replace after two years we have also provided the cumulative net position without replacement.

Table 7: Net position from Preserved Right to Buy sale and replacement unit, current prices

		2014/15	2015/16	2016/17	2017/18	2018/19
BENEFITS from:						
Preserved Right to Buy sale	Sales receipt	£72,175	£0	£0	£0	£0
	Maintenance savings	£1,224	£1,237	£1,253	£1,260	£1,266
	Repairs savings	£927	£937	£949	£954	£959
	Debt servicing interest savings	£382	£382	£382	£382	£382
Replacement	Affordable rental stream	£0	£0	£6,665	£6,731	£6,799
Sub-total		*£74,707*	*£2,556*	*£9,249*	*£9,326*	*£9,405*
COSTS from:						
Preserved Right to Buy sale	Loss of social rental stream	£4,162	£4,312	£4,390	£4,434	£4,478
	Administrative costs	£2,000	£0	£0	£0	£0
Replacement	Maintenance costs	£0	£0	£1,253	£1,260	£1,266
	Repairs costs	£0	£0	£949	£954	£959
	Debt servicing interest costs	£0	£0	£382	£382	£382
	Grant	£0	£0	£48,672	£0	£0
	Provider resource	£0	£0	£18,387	£0	£0
Sub-total		*£6,162*	*£4,312*	*£74,033*	*£7,029*	*£7,084*
IN-YEAR NET POSITION (with replacement)		*£68,545*	*-£1,756*	*-£64,784*	*£2,298*	*£2,321*
CUMULATIVE NET POSITION (with replacement)		*£68,545*	*£66,788*	*£2,004*	*£4,302*	*£6,623*
IN-YEAR NET POSITION (without replacement)		*£68,545*	*-£1,756*	*-£1,806*	*-£1,839*	*-£1,872*
CUMULATIVE NET POSITION (without replacement)		*£68,545*	*£66,788*	*£64,983*	*£63,144*	*£61,272*

64. Where associations share receipts with councils, under the terms of a sharing agreement, they can deduct an agreed allowance to cover sales costs from receipts and this will continue to be the case. Again estimates based on regional averages for costs, the Net Present Value of lost rental income and projected receipts show that receipts should more than cover administration costs and the Net Present Value of lost rental income. Sharing agreements differ across different stock transfers, but there has been very little concern in the sector about the impact of sales on their ability to raise debt or meet loan covenants.

Small and micro-business assessment

65. We have carried out an assessment and consulted the Homes and Communities Agency, the Regulator of housing associations. In 2014 the HCA set out the outcomes (standards) that housing associations are expected to achieve and the specific expectations of the HCA as the regulator[14]. All of the standards apply to all registered housing associations regardless of their size. This is a risk based and proportionate approach to regulation which seeks to minimise the burdens on housing assocations. A small business is defined as up to 49 FTE employees and micro-business is defined as up to 10 employees. The HCA no longer collects information on the number of employees per housing association. However we have sought to carry out an assessment using the 2011 Regulatory Statistical Return which collected such information from associations alongside information published by the HCA on stock transfers since 1997 which may be eligible for PRtB. Taking this approach we have been able to identify employee data for 126 associations out of 300 where the data indicates a stock transfer has occurred at some point since 1997. This analysis identified four associations which may be affected as a small business (in the HCA's opinion it is highly unlikely that any associations will fall into the definition of a micro-business).

66. Of these four housing associations we estimate that three fall into the HCA's definition of a larger association on the basis that they manage in excess of 1,000 dwellings. For these, like other associations the HCA will carry out a risk assessment process involving an assessment of the association's financial strength, size, cash requirements and sector risk exposures. This is based on data provided by the associations. The output from this initial assessment is then moderated to take account of further information available to the regulator, such as any emerging issues or shifts in the strategic direction of the association. This will form the basis of a strategy for regulatory engagement.

67. The remaining one housing association appears to meet both the RPC definition of a small business and the HCA's definition of a smaller association. The regulatory approach for smaller associations means in general that they should expect to have a reduced level of engagement. The regulatory arrangements for smaller associations include review by the regulator of audited annual accounts. Direct regulatory engagement is by exception and usually only in response to specific problems. In these circumstances reactive engagement will be similar to that for larger housing associations and may take different forms including initial conversations to establish quickly whether further follow-up is necessary or could include the regular receipt of additional monitoring information to allow the regulator to assess how well the presenting issue has been addressed.

68. Under Schedule 5 to the Housing Act 1985 the right to buy does not apply in specific circumstances. These are where (a) the landlord is a charitable housing association or housing trust, (b) the landlord is a co-operative housing association or almshouse, and (c) the landlord is a housing association which has never received grant. Analysis of the HCAs Regulatory Data Return (now replaced by the Statistical Data Return) suggests that as at 31 March 2011 1,197 out of 1,577 housing associations, or 76%, who returned an RSR were charitable in status and therefore Right to Buy is not applicable for these associations. The one housing association that meets the RPC definition of a small business and the HCA's definition of a smaller association operates on a charitable basis (under the model charitable rules of the National Housing Federation) and therefore the right to buy does not apply. The analysis also indicates that the sorts of tenants with PRtB are concentrated in larger (i.e. those managing more than 10,000 units) and more established landlords. This is partly due to the fact that tenancies which are eligible for PRtB tend to be older and therefore concentrated in landlords which have grown over a number of years through mergers etc.

[14] Regulating the Standards, 2014

69. Given the full exemptions which are already in place for housing associations including smaller housing associations, the availability of dedicated support for smaller associations through the HCA's regulatory function and our analysis of the available evidence which suggests that tenants with PRtB are likely to be concentrated in larger associations, we do not propose any additional actions to mitigate the possible burdens on smaller housing associations. Our expectation is that receipts from Preserved Right to Buy sales should be used to help fund new homes for affordable rent and we would encourage housing associations to work in partnership with local authorities, and use other sources of cross-subsidy, to help achieve this. Stock transfer agreements are private commercial contracts between local authorities and housing associations, and, if they have concerns, we would urge associations to discuss their agreement with their transfer authority.

Impact on Housing Association capacity

70. Under a sharing agreement a housing association would typically keep the receipt calculated as the Net Present Value of the lost rental income on the home based on their original business plan (i.e. the attributable debt). This plan will have been drawn up at the point of transfer.

71. The debt profile in the business plan will generally be forecast to rise in the early years, as additional debt is taken on to pay for improvements. The level of debt will fall once past the point of peak debt as it is repaid, eventually falling below the starting debt position.

72. Where additional debt has been taken on for a home subsequently sold through Preserved Right to Buy, this will be reflected by an increase in the share of the receipt that the housing association retains. This will be most common where the stock transfer or improvement work takes place in the early years (say in the first 5 years). On the other hand, once debt begins to be repaid, the latest debt position will be less than the initial attributable debt (and receipt).

73. A further complication is that the business plans made by the housing associations themselves will be updated at least annually. These will take a revised, latest, view of the debt servicing capacity of the homes transferred to them. This debt servicing capacity is affected by future net rental stream which will typically grow and may be used to service new debt to fund affordable housing supply and other community benefits. After a 20 year period this could be significantly more than the initial debt position at the point of transfer, which is important for the more leveraged Housing Associations that are utilising that capacity more heavily.

74. According to the Homes and Communities Agency[15], around 18% of the Preserved Right to Buy stock was transferred more than 15 years ago, half (54%) was transferred to local authorities within the last 10 years and nearly a quarter (23%) within the last 5 years.

75. Taken all these effects together, the usual profile is for debt to rise in the early years but to diminish over a 30 year period. It would be possible under Preserved Right to Buy sales for the Housing Association's share of the sale receipt on Preserved Right to Buy sales to be less than the debt-servicing capacity they will have assumed in their latest business plan therefore reducing their overall capacity. However, as noted above, there has been very little concern in the sector about the impact of sales on their ability to raise debt or meet loan covenants.

76. The Homes and Communities Agency has estimated that the average debt capacity for housing associations is around £19,000 per home under stock transfers and for the majority it is between £10,000 and £30,000.

[15] Formerly known as the Tenant Service Authority

SECTION 8: ECONOMIC AND SOCIAL IMPACTS

Distributional benefit

77. The HM Treasury Green Book suggests that policy appraisal should take into account the income levels of the beneficiaries of the policy. This is because, according to the theory of "diminishing marginal utility of consumption", an individual's well-being will vary according to his or her income, with policies aimed at lower income individuals having a greater impact than policies aimed at higher income households. Distributional analysis essentially allows us to account for the economic benefits of making national household income more evenly distributed.

78. In theory, allowing social tenants to purchase a house under the Right to Buy policy has associated distributional benefits in that social tenants are on average less well off than the average household. Although it is difficult to collect accurate information about income and we do not hold such information about purchasers under the Right to Buy, analysis of 2010-11 English Housing Survey data suggests that on average the gross household annual income of households with eligibility to exercise RtB is similar to the gross household income of social renters in general at around £17,000. The table below compares the equivalised income[16] distribution of average social tenants compared to the national median average. By combining the information on median equivalised incomes (by decile) and the distribution of social tenants (by these deciles), we can calculate the net distributional benefit of transferring £1 from the median household to a social tenant (or Right to Buy) household in each decile.

Box 1: Income deciles of social tenants

Decile:	**1**	**2**	**3**	**4**	**5**	**6**	**7**	**8**	**9**	**10**
Before housing costs (median income £402pw)										
Proportion of SRS in decile	13%	19%	18%	17%	11%	9%	7%	4%	2%	1%
Decile median income	145	224	275	322	374	431	500	588	730	1,082
Net impact of £1 transfer from median	1.77	0.79	0.46	0.25	0.08	-0.07	-0.20	-0.32	-0.45	-0.63
After housing costs (median income £347pw)										
Proportion of SRS in decile	18%	21%	19%	13%	9%	7%	6%	3%	1%	1%
Decile median income	76	168	220	268	320	375	443	527	653	984
Net impact of £1 transfer from median	3.54	1.07	0.58	0.29	0.08	-0.07	-0.22	-0.34	-0.47	-0.65

Source: Family Resources Survey

79. The distributional benefit of Right to Buy is calculated by applying this distributional weighting to the implicit subsidy associated with the Right to Buy unit. This subsidy is taken as the difference between the 30 year Net Present Value of the 30 year social rents on the one hand, and the 30 year Net Present Value of the net costs associated with purchasing the property on the other (i.e. ongoing costs, such as

[16] Equivalised income is a measure of income that takes into account household size and consumption.

mortgage payments and maintenance, associated with the property which are partly offset by the "value" of the asset at year 30).

80. There are also distributional benefits that accrue to households renting the new affordable housing, because they are saving on rent by not having to rent private rented sector homes[17]. This means that they can increase their consumption of other goods and services. This increase in consumption represents a distributional benefit given that affordable rent housing is, in general, allocated to lower income households.

Economic benefits (replacement)

Additional housing supply

81. The economic benefit of additional housing supply (due to the one-for-one replacement) can be captured through 'land value uplifts'. The land value uplift is the difference in land value between residential and non-residential use which proxies the benefit of building additional units in different locations which also captures the variance of the net value of new developments by location and will be greater in areas where additional housing is most needed. This benefit should in theory capture consumers' willingness to pay for housing services adjusted for the cost of using land for residential use.

82. The average potential uplift in each sub-national area is estimated using January 2009 Valuation Office Agency data which contains land values for both residential and non-residential usage. These values are assumed to grow in line with house price inflation.

83. However, not all replacement units will translate into additional housing supply. Some replacement units will be truly additional; but some replacement units will simply displace private supply. The 'additionality' of affordable housing is likely to change over time depending on local factors and current market conditions.

84. A central assumption of 50% additionality is used. Given the current economic climate this is likely to be a conservative estimate; affordable housing is most likely to be additional:
    i. in economic downturns when house building activity is generally suppressed;
    ii. when development is on infill sites and makes such sites more viable and levers in private development;
    iii. when funding brings forward supply;
    iv. when there are planning restrictions which mean that local authorities favour social housing;
    v. in conditions of low credit availability therefore creating funding difficulties for developers.

Improved labour mobility

[17] Assuming no Housing Benefit.

85. In the economy, housing plays a key role in supporting an efficient labour market. It does this enabling labour to move to where it is needed (labour mobility) and ensuring incentives to work are not distorted. In the case of the UK, demand for labour relative to its supply is greatest in the south and south east.

86. The CBI London Business Survey (December 2012) reported that although London is a good place to do business, unless some of the main weaknesses including housing are addressed, London stands to lose its attraction and competitiveness in the global market place[18]. The implication is that wages in London were either higher, or vacancies were not filled, as a result of the housing shortage in the Capital, risking the competitiveness of firms in those regions.

87. Research by Solutions[19] estimates that building 20% more homes in the wider south east by 2030, relative to the current trend increase, and closest to the areas of high demand would reduce the costs of doing business there by over £3bn a year, as a result of reduced wage demand pressure. There are around 22 million households nationally and a 20% increase would imply a further 4.4 million. We have pro-rated this figure and adjusted it to account for the regional disparity between the research and the location of affordable housing development, to derive a per unit benefit figure.

Better education outcomes

88. In relation to linkages between housing an education, ECOTEC[20] assessed the critical impacts that poor quality, overcrowded, and temporary accommodation can have on individuals' educational attainment (as well as health and well-being, and likelihood of criminality). The report estimates "£14.8billion pounds in lost earnings forecast for this generation in poor housing". We use this figure to estimate the adverse impact that overcrowded housing conditions have on education, taking account of the extent to which overcrowding is alleviated by the additional housing supply through one for one replacement.

Better health outcomes

89. Overcrowding has well-documented links with poor health and is most severe for families living in temporary accommodation. Overcrowding leads to an increase in infectious diseases among children and the probability of domestic accidents rises due to a lack of available space to live and play. Overcrowding is also associated with a range of social and emotional problems in children.

90. Research carried out by Ambrose et al, 1996[21] considered the health costs associated with poor housing by comparing both an existing and refurbished housing estate in two different areas. The estimated costs to the NHS for illnesses associated with poor housing ranged from £170 to £1,200 per annum. In

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[18] http://www.cbi.org.uk/media/1892095/cbi_kpmg_london_business_survey_dec2012.pdf
[19] http://www.suburbansolutions.ac.uk/findings.htm p8.
[20] http://www.salford.gov.uk/corestrategy/iw/JC-JC13-Social-impact-of-poor-housing.pdf
[21] http://www.brighton.ac.uk/sass/research/publications/pa52/Laugh_Too_Much.pdf

assessing the benefits to improved housing quality we take the average of these two costs and attribute a benefit per unit.

<u>Reduced use of temporary accommodation</u>

91. We assume that around 10% of the new affordable homes under one for one replacement will go to households that would otherwise not have formed; including to concealed and homeless households (who would otherwise be in temporary accommodation). Temporary accommodation costs around £3,120 a year (London) and £2,340 a year (outside London) in management costs. The implied average annual cost nationally is around £2,500 and over double that of management costs for social rented / affordable rented housing.

Summary economic and social impacts

92. The per unit impacts are consistent with those used in the Business Cases for the 2015/16 Spending Round, as the new policy does not fundamentally change these. The per unit impacts are then given as follows:

Table 8: Summary of results: per unit social and economic benefits under the preferred policy option – (60 year Net Present Values):

Right to Buy unit	
Distributional benefits	£52,000
Replacement unit	
Distributional benefits	£44,000
Economic benefits of increased housing supply	£28,000
Improved labour mobility	£8,000
Better education outcomes	£7,000
Better health outcomes	£5,000
Reduced used of temporary accommodation	£2,000
Subtotal (no conversions)	*£94,000*
Right to Buy unit and replacement combined	
Net social / economic impact (no conversions)	*£146,000*

93. The following results are presented as 60 year Net Present Values for additional take up expected over the first three financial years from when the policy commences (2014/15 to 2016/17) under the preferred policy option.

Table 9: Summary of results: social and economic benefits of additional units over next three financial years under the preferred policy option – (Reducing the qualifying period from five years to three years):

60 year Net Present Value	**lower**	**central**	**upper**
Right to Buy unit			
Distributional benefits	£466m	**£540m**	£653m
Replacement unit			
Distributional benefits	£394m	**£457m**	£552m
Economic benefits of increased housing supply	£251m	**£291m**	£351m
Improved labour mobility	£72m	**£83m**	£100m
Better education outcomes	£63m	**£73m**	£88m
Better health outcomes	£45m	**£52m**	£63m
Reduced use of temporary accommodation	£18m	**£21m**	£25m
Subtotal (no conversions)	*£843m*	***£977m***	*£1,179*
Net social / economic impact (no conversions)	*£1,309m*	***£1,517m***	*£1,832m*

SECTION 9: IMPACT ON HOUSING BENEFIT

94. This section considers the Housing Benefit implications of the policy changes in more detail. These impacts were included in the public sector Net Present Value analysis described earlier in this document, however here they are explained further with additional sensitivity analysis around key assumptions. 'Housing Benefit' should be taken to be referring to the housing element of Universal Credit or Pension Credit.

95. The following describes the potential 'flows' of Housing Benefit costs and benefits as a results of a Right to Buy sale and subsequent replacement with an Affordable Rent unit.

Housing Benefit impacts associated with the Right to Buy unit:

96. <u>Housing Benefit saving:</u> A Housing Benefit saving will occur for households who exercise their Right to Buy, and are currently claiming Housing Benefit (because they may receive some assistance from family). Housing Benefit savings are calculated assuming that the equivalent of 10% of Right to Buy purchasers are on the equivalent of full Housing Benefit[22] (however sensitivity analysis around this figure is presented). The Housing Benefit saving is calculated using the average Local Authority social rent level over 15 years, (the average length of tenancy in the social sector) therefore assuming that the Right to Buy purchaser would have otherwise remained in the property for 15 years (again, sensitivity analysis around this figure is presented).

97. <u>Housing Benefit cost:</u> A Housing Benefit cost will be incurred as a result of a Right to Buy purchase in terms of the loss of the social unit in the future compared to a counterfactual where the unit would have otherwise become available for a new social let. We assume that in the counterfactual, the tenant would have otherwise moved on after 15 years, therefore freeing up the unit for another household for social rent. We calculate the Housing Benefit cost by the difference between Local Housing Allowance in the private sector and Local Authority social rent using assumptions about Housing Benefit coverage. Therefore, the counterfactual assumes the unit would have been re-let as a social unit rather than an affordable rent unit.

Housing Benefit impact associated with the replacement unit:

98. <u>Housing Benefit saving:</u> If a Right to Buy unit is replaced by a new affordable unit, there is a Housing Benefit saving resulting from the new unit. The Housing Benefit saving arises due to the fact that tenants previously on Local Housing Allowance in the private sector can move to the new <u>affordable</u> unit at lower cost to government. This saving is calculated based on the difference between Local Housing Allowance and affordable rent combined with Housing Benefit coverage assumptions.

99. We estimate the Housing Benefit impacts making a number of assumptions on both rent levels and Housing Benefit coverage (i.e. the proportion of households on Housing Benefit and how much of their rent is covered by Housing Benefit). Crucially, however, we are extremely likely to see Housing Benefit

[22] As noted in section 5, there is a high degree of uncertainty associated with this assumption. Therefore readers should also refer to the sensitivity analysis around this assumption which is presented in tables 19 and 20.

savings over the three year period from when the policy commences – we estimate around £7m with additional savings from replacement units that may be delayed due to the lag between the Right to Buy receipt coming in and the affordable rent unit being built (assumed a one year lag).

100. The reason why the housing benefit impact is positive (i.e. a saving) in the short term and becomes increasingly negative (i.e. a cost) in the longer term is because the initial housing benefit savings (as a result of the small number of RTB purchasers that were claiming housing benefit before exercising their right to buy and the savings associated with the replacement affordable rent units) are outweighed by housing benefit costs associated with losing a social unit through the RTB purchase in the longer run.

101. It should be noted that this analysis excludes further Housing Benefit implications which may arise as a result of:

- some households who over time would have drifted on to Housing Benefit in the social sector, so a potential extra Housing Benefit saving; and
- some Right to Buy households who may drift onto Support for Mortgage Interest, so a potential extra cost.

Table 10: Housing Benefit impacts per unit (positive = saving)

	Central assumptions		
	Net Present Value over 3 year period	30 year Net Present Value	60 year Net Present Value
Right to Buy unit	+£1,200	-£6,000	-£20,000
Replacement unit	+£900	+£2,900	+£3,900
Right to Buy unit & replacement unit combined	+£2,100	-£3,100	-£16,100

Table 11: Housing Benefit impacts per unit, sensitivity analysis (positive = saving)

	Net Present Value over 3 year period	30 year Net Present Value	60 year Net Present Value
Right to Buy unit			
The Housing Benefit propensity of Right to Buy purchasers: 5% to 25%	+£600 to +£3,000	-£8,600 to £2,000	-£22,600 to -£12,100
The average length of tenancy: 10 to 20 years	+£1,200 to +£1,200	-£12,300 to -£400	-£26,300 to -£14,400
Replacement unit			
No conversions	+£900	+£2,900	+£3,900
Right to Buy unit and replacement unit combined			
Range: low to high (worst case to best case)	+£1,500 to +£3,900	-£11,300 to +£12,500	-£24,300 to -£500

Table 12: Housing Benefit expenditure impact associated with additional sales over 2014/15 to 2016/17 under the preferred policy option – (Reducing qualifying period from five years to three years) (positive = saving)

	Central assumptions	
	Spending over 2014/15-2016/17 (cash)	Spending over 30 years (Net Present Value)
Right to Buy unit	**+£1,200,000** (+£0 to +£3,100,000)*	-£6,200,000
Replacement unit	**+£5,600,000** (delayed)**	+£18,100,000
Right to Buy unit & replacement unit combined	**+£6,800,000** (+£5,600,000 to +£8,700,000)*	-£24,300,000

*Range presented based on 0% to 25% of Right to Buy purchasers on Housing Benefit. The central assumption is 10%.

** Savings are calculated on the basis that one for one replacement is achieved within the Spending Review period. These savings would be reduced/eliminated if this was not achieved.

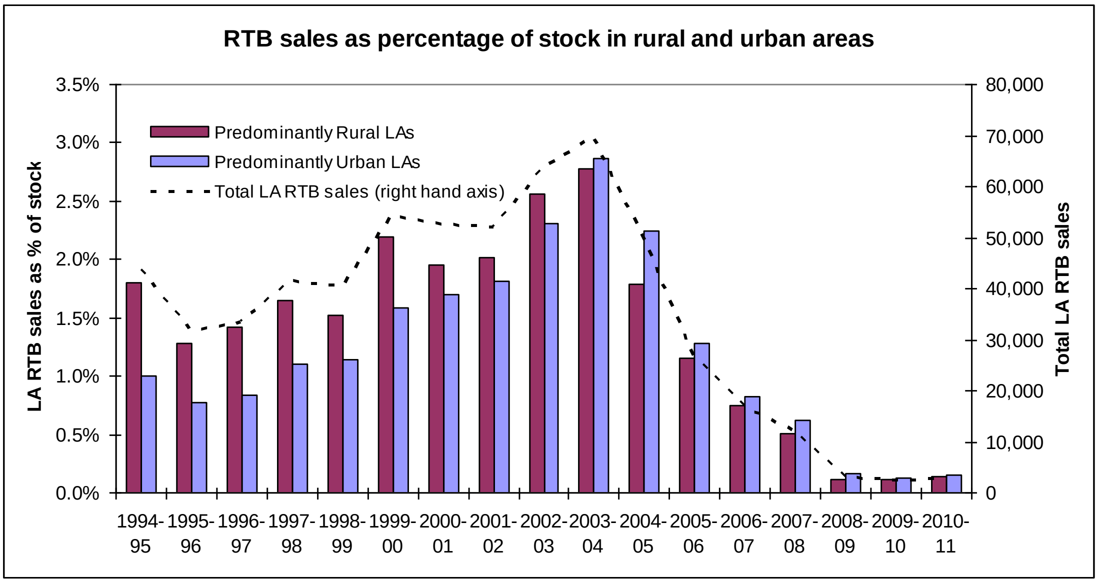
Rural Proofing

102. Over the years, concern has been expressed over the impact of Right to Buy on rural areas where the original stock of council houses was small and high house prices make owner occupation inaccessible for many local people. A number of measures (under section 157 of the Housing Act 1985) now ensure that properties sold under Right to Buy in rural areas remain in the ownership of local people. For example, where homes are sold under Right to Buy in National Parks, Areas of Outstanding Natural Beauty or areas designated as rural by the Secretary of State, social landlords can impose restrictions on their resale. The restrictions are either:

- that the property can only be resold to someone who has been living or working locally for at least 3 years; or
- as with for all Right to Buy resales, if the owner wishes to resell within 10 years of the Right to Buy sale, they must first offer the property to the original social landlord.

103. In the early years of the policy, the proportion of Right to Buy sales in rural areas[23] exceeded that in predominantly urban areas but since 2002-03 this has reversed (see graph).

Right to Buy sales as percentage of stock in rural and urban areas



104. We will continue to monitor the impact of Right to Buy in rural areas and keep under review whether existing safeguards are sufficient, whilst not being excessive.

[23] Rural districts with at least 80% or 50% of their population in rural settlements and larger market towns

SUMMARY AND IMPLEMENTATION PLAN

105. Based on the analysis of the evidence, Ministers have chosen to maintain the existing discount ranges and cash caps but decreases the eligibility threshold from five years to three years. This returns the eligibility threshold back to its original length, when the policy was first introduced and extends the Right to Buy, Preserved Right to Buy to approximately 275,000 tenants as well as a significant number of Right to Acquire tenants although these are far less likely to take up the offer. This will enable increased homeownership among social tenants, but at the same time ensure sufficient sales receipts to enable one for one replacement of every additional Right to Buy unit that is sold. There is no change to the existing approach to one for one replacement, which is based on Localist principles, but with safeguards to ensure value for money and to protect the scheme's viability.

106. The change to the eligibility threshold requires an amendment to Section 119 of the Housing Act 1985. This will require primary legislation, which we intend to implement via the Deregulation Bill and will be subject to the parliamentary timetable. We will continue to engage closely with councils, Registered Providers and representative bodies to explain the changes to them.

107. There will not be any change to the discount rates or the cash caps available on houses and flats, therefore no further action in this area is required.

108. The aim is to bring the lower eligibility threshold into force as soon as possible after the Deregulation Bill becomes an Act and this will be done via a commencement order. We plan to make tenants aware of the changes to the discounts through a number of communication channels at an appropriate point, depending on the Bill's passage through Parliament. Our communications plan will also cover arrangements for ensuring that lenders and landlords are prepared for the likely increase in Right to Buy, Preserved Right to Buy and Right to Acquire applications.