Briefing Paper

Sale of High Value Council Homes

June 2015

Council Housing in South London

Introduction

Probably the most contentious and high profile housing proposal in the Conservative manifesto is that to extend the Right to buy to tenants in Housing Associations. It is described as follows:

"We will extend the Right to buy to tenants in Housing Associations to enable more people to buy a home of their own. It is unfair that they should miss out on a right enjoyed by tenants in local authority homes. We will fund the replacement of properties sold under the extended Right to buy by requiring local authorities to manage their housing assets more efficiently, with the most expensive properties sold off and replaced as they fall vacant. We will also create a Brownfield Fund to unlock homes on brownfield land for additional housing."

The Conservatives have promised to introduce the policy within the first 100 days of a new government.

Response of the Sector to extending the Right to buy

This proposal has aroused some criticism from many who work in the sector. For example, Ken Lee, Chair of the Housing Panel at the Chartered Institute of Public Finance & Accountancy wrote a critique of the policy in 'Public Finance' as follows:

"Offering housing association tenants homes at a knockdown price while forcing councils to sell their most valuable stock makes no business sense

"One of the most eye catching pledges floated by the Conservatives during the election campaign concerned the right of housing association tenants to buy their properties. Alongside this measure, local authorities would be required to sell their most valuable housing stock.

"We are often told that if only local government managed its assets better, there would be less of a housing problem. Ministers chastise councils for not getting rid of the more valuable assets on their Housing Revenue Accounts so that the released money can be reinvested.

"Closer examination of the proposals suggests that central government could give the shedload of cash made available to registered providers of social housing as compensation for them, in turn, selling their assets at a knockdown price to tenants. It would also enable setting up of a fund to bring abandoned brownfield sites back into use for house building.

"I do not know which business school the creators of this idea went to, but experience tells me that usually these very valuable properties are the ones that are located in the more desirable areas, tend to cost the least to maintain – and bring in the highest rents.

"So, in business terms, getting shot of these properties is totally wrong. Keeping them enables councils to meet housing need in their areas.

"Local authorities paid central government billions of pounds to take full control of their Housing Revenue Accounts. Subsequently, a host of negative actions taken by government have impacted on the housing revenue account – welfare reform, Right to buy changes, rent guidelines and so forth. Each time, local government has tried to find a way to keep on delivering. If anyone knows how to run their housing revenue accounts it is councils.

"All the lessons from the past indicate that the latest plans to sell off council housing stock are fraught with danger. In fact, many would put today's housing crisis at the door of Right to Buy.

"Experience suggests it is a popular policy in the short term – especially with those who gain a financial fillip from the discounts – and initially, because the sold properties were better maintained, some areas did benefit. In the longer term it has led to less social housing being available; more private rented stock, as original buyers sell on; poorer maintained properties (you can now drive down the street and spot the non-housing revenue account ones because of their poor state); and, in many cases, poorer management standards that have increased problems on estates.

"This also resulted in higher overall public expenditure, due to benefits funding ever-increasing rents in the unregulated private rental market.

"Extending Right to buy to registered providers is also poor asset management for a sector that has been urged to 'sweat its assets' and borrow on the strength of the asset base. What problems are they going to face if they reduce it? Will their funders be happy? And what will the impact be on the opportunity to borrow in the future to provide more housing?

"None of these proposals promote good business practice.

"Any good business reinvests income to ensure a future revenue stream. The HRA can provide much needed social housing if only the absurd borrowing cap is removed. Giving these decisions back to local authorities makes far more sense than imposing a sales regime that does not reflect local circumstances.

"Councils are cautious about the way they invest, in keeping with the prudential code, and respond to local needs if they are left to get on with the job. Rather than coming up with tired policy suggestions that will only cause longer term problems, why not let local authorities build the much-needed housing? That is one promise that everyone could usefully keep."

Since the election, Moody's, which provides credit ratings to 43 housing associations, warned that the impact of a Right to buy extension – if introduced – would be 'mixed'. It said the impact would depend on how many tenants took up the policy and if housing associations were compensated for the discount. Jeanne Harrison, one of their analysts, told 'Inside Housing' that:

"Right to buy sales give housing associations short-term cash flow upside, but could also erode their long-term rental income streams and potentially impair both their balance sheets and future borrowing capacity, if it hampers replacement of housing stock."

The agency listed housing associations alongside life insurers, banks and renewable energy developers as the sectors that may see increased risk as a result of the Conservative victory.

It became clear during the election campaign that Conservative politicians resented housing and housing finance professionals criticising their proposals and attempting to prevent tenants of housing associations being given the same rights that council tenants have enjoyed since 1980.

I would not advise the housing sector to become confrontational with the government on this or any other issue, but I think that the government and the sector should bear the following issues in mind:

- Right to buy is generally recognised to have some advantages in that it helps people into home ownership and helps to create mixed tenure estates.
- However, I think there is a strong argument that right to buy should not be allowed to result in a reduction in the number of social homes (homes sold should be replaced) and this argument was accepted by the coalition government and is still accepted by the present government.
- The discounts represent a public subsidy and therefore should there not be an evaluation of the benefits that they bring against their costs and a comparison of this cost-benefit analysis with the costs and benefits of other public investment in housing?
- Housing Associations are not owned by the state so I think that the proposal that they should be forced to sell their assets raises civil liberties issues as well as financial issues. In what circumstances should the state be able to take control of privately owned assets?
- This proposal raises questions about the legal status of housing associations. Is this part of a process of 'nationalising' housing associations? If so, their loans would become part of the public borrowing and the basis on which they are financed would be called into question.
- If these proposals are justified on the grounds that the government supports housing associations financially through housing benefit, could or should the same argument be applied to private landlords?

AWICS Ltd., Unit 3, Shire Hall, The Sands, Appleby in Westmorland, Cumbria. CA16 6XN.
Tel: 017683-52165. Mob: 07502-142658. Twitter @AdrianWaite. E-Mail: adrian.waite@awics.co.uk. Web: www.awics.co.uk

Managing Director: Adrian Waite MA CPFA CIHM FInstLM
Registered office as above. Company Number: 3713554. VAT Registration Number: 721 9669 13.

- If, as Natalie Elphicke (the joint-author of a report commissioned recently by the government) claims, the compensation that would be given to housing associations would exceed their losses on disposal this could address many of the financial concerns of housing associations. However, we would need to be sure about how this would affect properties that are used as security for loans. If an association sold a property that was used as security for a loan, could the bank recall or re-price the loan? There is also the question of maintaining effective asset management on an estate where homes are being sold.
- The proposal that local authorities should sell high value council houses when they become vacant has disadvantages. High value properties usually have high rents and low management and maintenance costs and from a business point of view are not the properties that a council should consider disposing of. Properties that are in low demand and that have high management and maintenance costs are probably the ones that councils should be disposing of. The policy would also lead to a reduction in the number of social homes in high value areas forcing social tenants to leave places like Central London and this may be considered to be a social dis-benefit.
- I am not convinced that local authorities would be able to generate sufficient usable capital receipts from the sale of high value properties to compensate the housing associations fully for selling homes at a discount. Would the receipt from selling a high value council house be sufficient to repay debt, compensate a housing association for a right to buy sale and then pay for building two new homes to replace the one sold by the local authority and the one sold by the housing association? I suspect not. Even if it was, would this be the best way to use the receipts given the shortage of resources for building social and affordable homes.

Sale of High Value Council Homes

Councils will be forced to sell about 5% of their most valuable housing once it becomes vacant and build more affordable, cheaper properties with the proceeds. The government argues that this will mean the number of affordable homes will double for each home sold, thereby increasing the national housing supply.

The government says that the remaining funds raised from the sale of valuable council stock will go towards freeing up brownfield land for development. Right-to-build plans, which will also be in the housing bill, would give people the right to be allocated land with planning permission to self-build or commission a home to be built for them.

Housing Minister Brandon Lewis said:

"It is right that as high value council homes become empty they should be sold to fund new affordable housebuilding in the same area. The proposals in the Queen's Speech will do that and more, extending Right to Buy level discounts to over a million housing association tenants, with the homes sold replaced on a one-for-one basis. This is part of our wider efforts to help anyone who works hard and wants to own their own home achieve their dream."

The idea of selling high value council homes was outlined in a report by the right-wing policy group 'Policy Exchange' in 2012 in a report entitled 'Ending expensive social tenancies'. This report argued that selling expensive social housing as it becomes vacant could create the largest social house building programme since the 1970s. It was estimated that the sales would raise £4.5billion annually that could be used to build 80,000-170,000 new social homes a year and reduce the housing waiting list by between 250,000 to 600,000 households in five years.

The report concluded that ending expensive social housing:

- Would generate growth and jobs. This reform should allow 80,000-170,000 new homes every year. This would create 160,000-340,000 jobs a year in the construction industry.
- Is extremely popular with all sections of society. 73% of people including social tenants think that people should not be given council houses worth more than the average property in a local authority. By 2:1 voters agree people should not be given council houses in expensive areas.
- Has no real effect on employment. More expensive areas do have slightly higher employment rates but these differences are very small. Since people commute to work – either by public transport or car – the only effect of moving tenants is reducing time spent travelling and travel costs. This is not a major driver of employment
- Would raises tenants' standard of living. The majority of social tenants are either totally or largely reliant on benefits. Someone living on benefits in an expensive part of London will pay a 10-15% premium compared to someone living in a cheaper area.
- Would reduce the housing waiting list by between 250,000 to 600,000 households in five years. The overwhelming majority of people waiting for a council house will benefit from these reforms.

The report said:

"When an expensive social property becomes vacant, it can go to a single fortunate household, or be sold to fund the building of multiple less expensive properties… The public oppose expensive social housing and want more homes… 20% of social housing is expensive and its value is £159billion."

The report calculated that the turnover and sale of 3.5% of the expensive social housing stock would sell off 28,500 expensive properties yearly and raise £5.5billion for new housing construction. Writing off an average debt of £35,000 would still leave £4.5billion a year to spend on new homes. This annual total is equal to the current four year (affordable housing programme) total from 2011 to 2015.

It was argued that expensive social housing has a much larger rental subsidy than normal properties as only 30% of the rent is set by the property's value. The Policy Exchange considers that a sensible estimate is that a property with a weekly £100 market rent has a weekly social rent of £65 (£35 subsidy) but one with a weekly £300 market rent has a social rent of around £104 (£196 subsidy).

The report also argues that right to buy for expensive properties means large government losses and that large discounts are poor value. They calculate that raising £5.5billion on a 66% discount would mean £16.5billion in sales and £11billion in discounts lost to government.

The recommendation was to define a high value council home in relation to average values in each region. A two-bedroom council home would therefore be considered to be high value if its value exceeded the following regional thresholds:

- London - £400,000
- Southeast - £250,000
- East - £220,000
- Southwest - £200,000
- Midlands - £145,000
- Northwest / Yorkshire - £130,000
- Northeast - £125,000

This policy will clearly have an impact on housing revenue account business plans. Firstly, there would be the effects on capital: The level of additional capital receipts would be highly unpredictable and potentially large – and complex processes would have to be introduced to re-distribute them and to allocate proportions of them to repay debt and build new homes. Secondly, there would be the effects on revenue: Reduced income from high value properties that had been relied upon in business plans and the self-financing settlement.

Response of the Sector to the sale of high value council homes

The Association of Retained Council Housing and the National Federation of Arms' Length Management Organisations have described the proposed sell-off of council properties to fund the right to buy as 'unfair' for local authorities as it goes against the principles of the self-financing regime introduced by the coalition government in 2012. John Bibby, Head of Housing at Lincoln City Council told the 'Local Government Chronicle' that:

"There are a lot of implications for council business plans, which were all based on the assumption that there would be continued income from these properties over thirty years. The impact varies between local authorities and depends on what thresholds are set for sales.

"There are considerable uncertainties as to whether the compulsory sale of higher value council housing as it becomes vacant will raise sufficient monies to fund the cost of Right to buy discounts.

"The present system of council housing finance was based on a one off payment to or from each individual council based on the value of their housing stock – including both high and lower value housing in their stock.

"The vast majority of councils whose housing debt was lower than the valuation of their housing stock borrowed to pay the difference to the government at the time and this additional borrowing was funded by the predicted future revenue income stream from the rents on those properties.

"If councils are now to be forced to sell off their higher value stock and handover the receipts to central government to fund right to buy discounts to housing association tenants then council tenants will in effect be paying twice.

"Councils will also lose the higher rental income from any vacant properties sold and this could adversely affect the financial sustainability of councils' housing business plans and their ability to properly maintain and improve the remaining lower value housing stock.

"Everyone recognises and applauds the desire to help first time buyers onto the housing ladder but this is a very high cost policy which will benefit only a relatively small number of better off housing association tenants who can afford the right to buy.

"There are serious questions about whether this policy represents value for money at a time of austerity and there are considerable uncertainties as to whether the compulsory sale of higher value council housing as it becomes vacant will raise sufficient monies to fund the cost of right to buy discounts for housing association tenants and compensate housing associations for the loss of their assets, let alone fund the replacement of sold properties on a one for one basis as well as providing a new Brownfield Regeneration Fund for house builders."

Eamon McGoldrick, National Federation of Arms' Length Management Organisations Managing Director, added:

"Arms' Length Management Organisations like councils are also very concerned about the potential loss of high value stock. For example, even if the promised one for one replacement homes can be provided in the areas where housing association and council housing is sold, these new homes will take two to three years to plan and build.

"In the meantime council waiting lists will get longer and homelessness is likely to increase, leading to additional costs to councils and council taxpayers in securing temporary accommodation through the private rented sector.

"This policy will cost billions of pounds over the life of this parliament and is predicated on selling revenue earning public assets which, at a time of continued austerity, will jeopardise the housing business plans of local authorities and Arms' Length Management Organisations.

"There is a risk that this policy will inevitably lead to a depletion of affordable rented accommodation, at least in the short term, and the Association for Retained Council Housing and the National Federation of Arms' Length Management Organisations look forward to receiving further details of how this proposal will work in practice."

A report by the Local Government Association, due to be published in June 2015, will call for councils to be allowed to set their own discounts.

It is predicted by many in the sector that the high value homes that are sold will be mainly bought by buy-to-let landlords thus increasing the size of the private rented sector rather than the owner-occupied sector. If this was to occur it would also be likely to cause an increase in housing benefit expenditure if the private tenants were eligible for housing benefit. Alternatively, homes could be sold to investors who could leave them uninhabited.

Local authorities and critics of the policy will doubtless attempt to amend the legislation and try to secure protection for certain cases. For example, rural villages where the social stock is below a certain proportion of the total, homes that have been adapted and those built in the last decade. There could also be an argument for a ceiling on sales on particular estates to ensure that whole areas don't lose their social housing. Attempts may be made to change the formula for designating the high-value stock so that boroughs like Westminster don't lose every new letting.

There may be possibilities for legal challenge. How will councils decide if they have two conflicting statutory duties but can't comply with both? How does the new obligation square with homelessness duties, for example? Does the obligation to rehouse over-ride the sales policy?

Impact in London

One implication of the policy is that any new homes that will be built will be in low value areas. This raises the prospect that the monies raised by councils selling stock in high value areas could lead to replacement homes in cheaper areas served by different authorities. Boris Johnson, Mayor of London, has identified this as a potential issue and has told the London Assembly that it would be 'the height of insanity' if money raised from selling stock leaves London. However, the Policy Exchange has argued that the use of a regional definition of a high value council home would prevent the need to build replacement homes outside of the region in which the high value homes were sold.

A number of councils are also understood to be looking into the possibility of moving high value homes into separate companies to exempt them from sales.

In May 2015, four Labour-led London Councils published research showing that 3,500 homes would be sold off over five years. The report's findings show:

- Around 3,500 homes can be expected to be sold across Camden, Haringey and Islington in the first five years of the new policy.
- Selling off empty properties is not likely to be enough to pay for the right to buy discounts, to compensate housing associations for loss of asset, to build replacement homes and also contribute to a brownfield fund.
- Even if the government's proposal for replacing homes works, there would be an estimated time lag of at least two years from the sale of homes to replacement ones being built. The report uses Department for Communities & Local Government data to estimate that this would result in 579 families with children and 385 homeless households being unable to get a council tenancy in the first two years.
- Many families unable to get a council tenancy would face the prospect of remaining in overcrowded homes, whilst households who are under-occupying would likely remain in their home for longer before downsizing.
- Homeless households would have to enter or remain in temporary accommodation. This is likely to have an effect on the private rented sector and on other council services in outer London boroughs as inner London boroughs rent homes for use as temporary accommodation outside of their own boroughs.

Councillor James Murray, Islington Council's executive member for housing, said:

"With Londoners already facing a huge housing crisis, this report shows that forcing councils to sell homes in high-value areas is likely to have a destructive impact right across the capital.

"Thousands of council homes would have to be sold, particularly in inner London boroughs, and the report underlines that there would be a big question mark over the government's promise that the homes would be replaced. We'll see a fall in the number of council lettings, which in turn will push up private rents even further, particularly in outer London boroughs.

"This report seems to confirm what we feared – that the Government's policy is wrong for London, both socially and economically, and will make our grave housing crisis even worse."

Haringey Council Leader, Councillor Claire Kober said:

"This counterproductive policy would choke the supply of new homes across London at the very time our city is battling a chronic housing shortage.

"Forcing councils and housing associations to sell off the few affordable homes that remain in areas where prices are skyrocketing will only serve to exacerbate – not resolve – the housing crisis.

"The government's tight restrictions on reinvesting money from sales under the current right to buy scheme mean only one house has been built for every ten sold, so it's unfeasible that extending the same policy will lead to a sudden rise in house building.

"The research shows that, far from helping families onto the housing ladder, this policy would leave the simple right to an affordable home further out of reach for many in London."

Councillor Sarah Hayward, leader of Camden Council said:

"This research seems to support our belief that the government simply doesn't believe people on lower incomes should be able to live in London.

"This policy will change the social mix of London for ever, yet our economy relies on people of all income brackets being able to support the businesses here. Forcing councils to sell will kill off investment, stalling house building and mean that London's communities will no longer be mixed and vibrant."

Enfield Council's Cabinet Member for Housing and Housing Regeneration, Councillor Ahmet Oykener, said:

"We would want the government to ease borrowing restrictions on councils so they can fund house building and allow Councils to build more houses."

It has also been estimated that in the London boroughs with the highest property values, such as Westminster, the policy will result in ALL council homes that become vacant being sold rather than re-let. In Westminster 400 homes become vacant in a typical year. The implications of this for the homelessness services in these boroughs would be significant.

Lord Kerslake, now Chair of Peabody Housing Association and former permanent secretary at the Department for Communities and Local Government used his maiden speech in the House of Lords to highlight the implications of the policy for London. He said that central London boroughs including Wandsworth, Westminster and Kensington & Chelsea would lose two-thirds of their stock over time and that it would be impossible to replace them. He added:

"There is a good case for local authorities being able selectively to sell off some of their high-value properties to reinvest. However, a top-down, one-size-fits-all approach is contrary to the spirit of greater devolution and will bring with it unintended consequences.

"There are also real doubts in my mind as to whether the receipts from the sale of high-value local authority properties can simultaneously cover the cost of the discount, the re-provision of new affordable homes and a contribution to the brownfield regeneration fund. At the very least this should be subject to a full independent financial review. What is clear, though, is that there would be a substantial flow of funds out of London, potentially of the order of £5 billion, to other parts of the country to make the numbers balance. The level of sales in London could reach 5,000 a year, which would be almost impossible for the London boroughs to match with new-build affordable homes—a fact borne out by the current experience of the one-for-one policy. This loss of affordable homes and redistribution of funds out of London at a time when its housing needs are so acute seems to be completely counterproductive."

The figures were based on Lord Kerslake's own research – but he declined to expand further on where he had sourced the numbers.

In the same debate Lord Best said:

"The whole process of selling some social housing and building elsewhere will have grave consequences. With councils having to sell in the best areas and having to build in cheaper places, a divisive segregation results, separating the better-off and the less affluent, in contradiction to the universally preferred alternative of mixed communities. As the London mayor has pointed out, replacing the homes sold in London with homes built outside will deny London the key workers on which this city depends, while affordable homes sold off in rural communities will often be quite impossible to replace.

"Moreover, what happens if selling good council housing as it falls vacant fails to raise all the funds to cover the cost of the new discounts, let alone pay for the councils to replace the homes they sell off?"

Potential Financial Arrangements

The government has yet to announce the details of how it proposes to manage the financial aspects of the scheme. However, it is possible to speculate about what the arrangements may be.

Housing Associations will be obliged to sell their homes at a discount and the government has said that they will be compensated. Presumably they will receive a sum equal to the discount that they have provided (or the difference between the discount that was given and that which would have been given under the right to acquire) plus maybe a sum to cover their administrative expenses. It could be expected that the government will take the view that if the Housing Association receives compensation at this level then it will have effectively received market value for the sale of the home and should therefore have sufficient resources to replace it.

Local authorities will be obliged to sell their high value homes when they become vacant. Presumably the government will provide guidance regarding how vacant homes should be valued and in practice there may be some scope for dispute around whether specific homes are sufficiently valuable for them to be sold. The government expects that the proceeds of these sales will exceed the sums that will be required to compensate the housing associations and presumably the proceeds will be divided into three:

- The Council will retain sufficient of the receipt to repay debt associated with the home that has been sold and their administrative expenses.
- The Department for Communities & Local Government will receive sufficient to compensate the housing associations for the discounts on the right to buy sales.
- The balance will be used to fund replacement homes in lower value areas.

There will obviously be a problem if receipts are not sufficient to cover the first two calls on them.

It will be interesting to see how the government will propose to manage the third call on the receipts. One option would be to estimate what proportion of receipts will be needed to compensate the housing associations and to require councils to pay a fixed proportion of their receipts (after deducting sufficient to repay debt and meet administrative expenses) to the government. This would enable councils to retain their share of the receipts locally and to spend them locally either on new council homes or on supporting development by housing associations. It could be expected that the rules regarding these receipts would be similar to those that apply to the reinvigorated right to buy scheme, including a requirement that the receipt could only be used to fund 30% of the cost of any new development.

This approach would have the disadvantage, from the government’s point of view, that it would not guarantee that sufficient resources would be provided to compensate the housing associations, and would not ensure that resources were targeted at the places where the cost of new homes would be lowest. However, the government has said that it would allow local authorities to retain some receipts to invest in new housing locally.

An alternative would be for the government to take all the receipts (apart from the Council’s share to cover debt and administration) and then to distribute any surplus receipts, effectively as Social Housing Grant.

Presumably this policy will effectively bar councils from building new homes in high value areas unless they are intended for sale as in any event they would be obliged to put them up for sale immediately!

Conclusions

The proposal to extend the right to buy to housing association tenants and to fund this through the sale of high value council homes raises the following questions:

- Will the sale of high value homes lead to 'social cleansing' of high value areas?
- Will the sale proceeds be sufficient to repay debt and compensate housing associations for lost assets?
- Will housing associations have the financial capacity to replace high value homes and homes sold under right to buy?
- Will sufficient sites be available for replacement homes especially in rural areas?

Adrian Waite
June 2015

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