LOCAL GOVERNMENT ASSOCIATION

Sustainability of Right to Buy

Summary Report - FINAL DRAFT
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savills

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Foreword

The Local Government Association (LGA) has long argued that a resurgence in house building by councils must be at the centre of a renewed effort to deliver additional homes that individuals, communities and economies need now and into the future[1],

While Right to Buy has helped thousands of families into home-ownership, the rules governing the scheme and the Housing Revenue Account have not enabled councils to replace those homes which are desperately needed in so many parts of the country.

The LGA continues to argue for councils to have maximum flexibilities to build, for instance the freedom to borrow against its housing assets, to retain 100 per cent of receipts generated from all sales, and to set rules – such as discounts – locally in line with local pressures.

In light of this the LGA has asked Savills to undertake an analysis to understand how existing policy is limiting the potential for each local authority to build, and how possible adjustments to the system can enable the sector to deliver more effectively overall.

[1] *Building our Homes, Communities and Future, Local Government Association, 2016*

Executive Summary: Summary of key findings

Headlines

In order to maximise the reinvestment potential under Right to Buy Retention Agreements (so-called "141 agreements"), and therefore to maximise the supply of new affordable homes under this programme:

Continued operation of Housing Revenue Account (HRA) debt caps have the potential to all-but eliminate local reinvestment of 141 receipts in 5 years. The forthcoming HRA Borrowing Programme should extend debt caps based on the deliverability of supply only according to established value for money factors within the Affordable Homes Programme (AHP); linking extensions of the debt cap to existing borrowing headroom risks limiting the reinvestment potential of 141 receipts.

Retention agreements and the borrowing programme are likely to need to pay attention to increased build and land costs as the availability of free land reduces. This may require increased grant rates and changes in the 30:70 matching principle within 141 agreements.

Linked to this, authorities should have the flexibility to negotiate retention agreements at funding mix rates which best suit their ability to maximise reinvestment in new supply. For a significant proportion of authorities, this might mean a move away from the 30:70 matching principle towards 40:60 and up to 50:50.

An approach to the selective limiting of discount rates in some authorities and certain regions could materially increase the potential for reinvestment in new supply.

Retention Agreements should allow greater flexibility to reinvest receipts over a period longer than 3 years to reduce the risks that receipts will not be used to provide new supply. Retention Agreements should also at least allow for the reinvestment into wider definitions of affordable housing.

Summary

1. This paper has sought to analyse the various features and factors affecting local authorities' ability to reinvest Right to Buy receipts within Retention Agreements (so-called 141 receipts agreements) signed with Government since 2012.

Trends and forecasting

2. Following a peak in sales between 2015 and 2017, there is evidence that volumes are beginning to reduce or level off in most authorities across the country. This is particularly true in London; however many authorities in the northern regions continue to see increases.

3. Forecast sales and receipts suggest that, given unrestricted access to matched funding alongside 141 receipts, there is the capability to deliver a replacement rate nationally of around 1.3 to 1 (representing c16,000 supply against c12,200 sales annually).

4. However, this masks a radically different picture at the regional and local level where reinvestment potential is primarily focused in London and the wider south and east; receipts are insufficient to deliver anything near to 1 for 1 replacements in all five northern and midlands regions.

Impact of the Debt Cap

5. Authorities are not unrestricted in finding resources to match receipts. The operation of the HRA debt cap restricts the reinvestment potential for local authorities and this restriction increases over time.

6. If authorities borrow to their cap, this reduces reinvestment potential to 1.07 to 1 as of now (13,037 supply compared to 12,224 sales). This reduces to 0.18 to 1 in 5 years as the constraint of the debt cap applies progressively to more and more authorities. Replacements would be as low as 2,000 compared to sales of 12,000 in 5 years' time. This highlights the importance of allowing extensions to the debt cap in order to maximise reinvestment into the supply of new homes. Only 54 (of 164) authorities would be able to sustain any kind of 141 replacement programme in 5 years' time without debt cap restrictions being lifted.

7. In practice, authorities may not borrow fully up to their cap given a commitment to long term business planning. If borrowing is limited to 90% of cap, this reduces the replacement rate to just 57% of sales as of now and all but eliminates the capability for replacement in 5 years' time. This in turn highlights that the extension of borrowing caps shortly to be consulted upon should be development-based and not linked to the existing borrowing position.

8. Assuming the availability of borrowing to cap, and without changes to any other factors within the agreements, our forecast suggests the potential to provide for c39,000 new affordable homes over a 5-year period, a net *loss* of c22,000 social homes over that time. 52% of the total 141 receipts arising over that period (£1.5billion) would be sent to central Government.

9. The lifting of debt caps must therefore be a pre-requisite to achieving a One for One programme at the national level. The programme for lifting borrowing headroom announced in the Budget and shortly to be consulted will be seen as a welcome opportunity for many authorities to achieve a bigger replacement programme. Restricting this programme to those close to cap might risk under-playing the potential for authorities in general to join the borrowing programme. It is likely that replacement rates under the 141 agreements will be higher should there be no restriction in the ability of authorities to bid for additional headroom.

10. Raising debt caps does not provide for a One for One replacement profile in the five northern and midlands regions without other changes to the basis for the agreements.

Cost and land pressures

11. There are pressures arising from increasing build costs and the increasing need to access land from outside the HRA. Decreasing availability of free land and increasing pressures on build costs have the potential to significantly affect the ability of authorities to maintain 141 replacement programmes at current levels in the future perhaps reducing reinvestment rates by as much as one third. This could impact the London region in particular, with a very large reduction in replacement rates given a requirement to provide for land costs. The Government will need to work with authorities to assess the impact in detail at a local level and the forthcoming borrowing programme should be sufficiently flexible in its allocations to address these pressures.

Flexibility in the application of the 30:70 funding mix

12. Changing costs of development also have the potential to require higher grant levels within the Affordable Homes Programme and the allocation for new social rented units is likely to have to reflect these cost pressures. Given the relationship between grant assumptions and 141 RTB programme assumptions, these pressures might suggest a need for higher grant rates and therefore a move away from the 30:70 matching principle as a national factor.

13. In this context, there is also strong evidence that varying the 30:70 funding mix/matching principle to 40:60 or 50:50 on a flexible, authority-by-authority basis, has the potential to increase replacement supply by 10%. The number of authorities that could benefit from a change to either 40:60 or 50:50 is estimated to be 61 over a 5-year period, around 40% of all authorities. Of these 48 are in the London and wider south/east regions reflecting the greater capacity to reinvest and there is no trend which would suggest anything other than authority-by-authority flexibility is the optimal way to maximise reinvestment.

14. There is evidence to suggest that a flexible approach to the reinvestment of receipts deducted from the 141 receipts calculation could also enhance replacement programmes, by between up to 9% depending on the approach taken to removing restrictions on borrowing.

Varying discount rates to maximise reinvestment

15. There is substantial evidence that a selective reduction in the rates of discounts offered to households, whilst leading to a reduction in sales volumes, could lead to an increase in gross receipts - as the reduction in sales is more than offset by a higher average sales price.

16. By way of illustration, we estimate that by reducing discounts in the five northern and midlands regions by a flat £20,000 applying to all sales in all authorities, could lead to an increase in reinvestment supply of 640 per annum (over 3,000 additional homes over a 5-year period); the reduction in sales volumes could potentially be 1,800 per annum (9,000+ over 5 years) leading to a net greater social/affordable housing stock of 12,000 homes over a 5-year period.

Other key factors

17. Twelve authorities were asked to engage on a series of set issues within this analysis. The key findings are summarised below.

18. A majority of authorities have deployed staff to carry out detailed checks on eligibility and around half of authorities have utilised fraud team officers in dealing with false applications. Some authorities have introduced extensive additions to standard forms requiring further information to be provided around funding and eligibility to act as a deterrent for spurious applications.

19. Most authorities have been able to sustain reinvestment via 141 agreements without paying any monies to Government but many reported that there were increasing pressures which might mean that money could be paid over in the near future without changes to the rules.

20. The rule which states that there is only 3 years in which to reinvest receipts, calculated on a quarter-by-quarter basis was reported universally as an issue for authorities. Most felt that 5 years was a more realistic timeframe.

21. The 30:70 funding mix works for some authorities. Others reported that a move to 40:60 and 50:50 would allow for more flexibility in the application of the receipts, particularly if this was able to vary between years, or the 30% element was able to be input up-front.

22. The debt cap was the single biggest factor affecting the consideration of a move away from 30:70. However, some authorities reported that a move away from 30:70 was likely to be necessary in viability terms as the costs of development were increasing.

23. Authorities are reporting that their land and other resources are being used up within the HRA, and that they will need to enter the market to purchase land in the future.

24. Several authorities have subsidiary companies and/or ALMOs in place to supplement the delivery of housing in their area. Many of these highlighted that it would be helpful to be able to deploy 141 receipts into these companies, which in turn could offer increased value for money in terms of increased supply numbers.

25. There is unanimity on the point that 141 receipts should be able to be utilised for a full range of affordable housing products in line with those supported by Homes England programmes.

26. Engagements with local Registered Providers to take up allocations have generally had low interest.

1. Methodology

Introduction

1.1 This analysis has been commissioned by the Local Government Association in early 2018 to investigate the issues, factors and features affecting the sustainability of the replacement of Right to Buy (RTB) sales through the Government's Retention Agreements with local authorities which were introduced following the reinvigoration of the Right to Buy in April 2012.

1.2 These agreements are commonly known as "141 Agreements" as they are based on the principle that authorities are able to invest a proportion of additional Right to Buy receipts for reinvestment into the provision of new affordable housing in order to achieve, at a national level, a One for One replacement of old stock with new.

1.3 In order for the Government to achieve value for money for the public purse, the 141 Agreements carry with them a substantial number of caveats and conditions, many of which have been identified by local authorities as inhibiting the reinvestment of receipts, and therefore inhibiting the replacement supply of affordable housing. Taken together with the operation of the Limit of Indebtedness (Debt Cap) for the Housing Revenue Account, the operation of the agreements is often felt to unduly constrain replacement supply.

1.4 This analysis has therefore been commissioned to test the features and factors within the agreements in order to determine whether, if any of them were to be varied or offered more flexibly, this might facilitate the delivery of an enhanced programme of replacement supply.

1.5 The work has therefore been addressed in three main parts:

1. Developing a national "Baseline Replacement" model, built from the individual local authority level (164 authorities), which estimates future sales, gross and net sales receipts and potential replacement rates based on the application of the factors and constraints as they operate under the current policy; this model is then able to be varied to test the potential impact on replacement rates as a result of varying the factors and constraints within the policy, principally the limiting factor that is the Debt Cap, the Funding Mix (the fact that 141 receipts are only able to be a maximum of 30% of development costs), and the impact of potential trends in development costs.

2. Developing a national analysis, built from the local authority level, which estimates the potential impact of varying discounts from the current policy, applying at an individual authority level, in order to test the hypothesis that in some cases, though lower discounts may lead to fewer sales, the actual net receipt to authorities might increase thereby enabling greater replacement supply and increased achievement of "One for One" replacements.

3. A qualitative analysis based on the engagement of 12 individual authorities identified to exemplify a representative group of experiences since the reinvigoration policy was

introduced in 2012, in order to offer insight to the potential impact of varying policies and measures across the country.

1.6 The outputs from the analysis are summarised within this paper. It should be noted that this analysis is focused on addressing potential flexibilities within the operation of the Right to Buy and the associated RTB Retention Agreements as they currently operate and has not been commissioned to question the application of the RTB policy itself, nor the right of the Government to retain a proportion of receipts for reinvestment at a national level. Both of these issues are felt to be subject to live policy debate between local authorities and Government, however they are outside the scope of this paper.

1.7 Thanks go to all those who have participated in the generation of material for this analysis.

Methodology

1.8 The initial year for the analysis is 2017.18 from which the model is launched to test future replacement rates over a 5-year period. A 5-year period is sufficient to test all of the hypotheses around changing each of the factors.

1.9 At the time of writing (April 2018), the final sales volumes and receipts levels for local authorities for the 2017.18 financial year are not yet available; we have therefore utilised an extrapolation of live tables in-year (three quarters are available - but there are a number of authorities for which data is missing or incomplete). Where the live data is incomplete, assumptions have otherwise been made based on the average of sales 2014-2017.

1.10 Sales values have been modelled on a range of bases:

- 2016.17 levels increased by the average of inflation in prices in the previous 3 years – average values have grown 25% over the 3 years from 2014 to 2017 and it feels unlikely that this growth will continue and there is evidence within 2017.18 that this growth has slowed.
- 2016.17 levels increased by house price inflation as this limits real growth in average sales prices.
- 2017.18 live data to date - where available, two or three quarters of actual data with actual sales price averages have been applied to the forecast.

1.11 In the absence of live data for 2017.18 and where volumes and prices vary significantly from previous years, we have applied a limited subjective judgment to the basis for the 5-year forecast of volumes and average prices.

1.12 Subject to the basis for the forecast, these volumes and values combine to a gross receipt forecast for 2017.18 from which is then deducted the various allowances for administration, debt, Local Authority unpooled share, Government Share, and buy-back allowance in order to arrive at an estimated forecast of 141 receipts for 2017.18[2].

[2] *Administration, debt repayment, LA and Government shares are included in the 2012 self-financing settlement and have been rolled forward to 2017.18 to estimate these deductions in the forecast*

1.13 The estimated forecast of 141 receipts highlights that there are a small number of authorities for which there are forecast to be no 141 receipts (three) and very small amounts (a further 10-15).

1.14 Build costs have been applied at a regional level (varying from £100,000-£140,000 / unit for total build cost only - but excluding land) and these have been supplemented with land value estimates, also based at a regional level[3]. The land value estimate is felt to be important as many authorities are reporting that HRA land is close to being used up and that they will need to purchase land in order to sustain supply.

1.15 The estimates of 141 receipts are then "grossed up" by the relevant factor from the Funding Mix (Matching Factor - currently 30%/70%) in order to test the potential for replacements at the relevant build cost rate.

1.16 There are three forecast replacement rates modelled for 2017.18:

- Assuming no limit on borrowing or the availability of other funds to form the 70% matching element
- The availability of borrowing only up to 100% of Debt Cap
- The availability of borrowing only up to a % of debt cap (in order to maintain a sensible risk buffer in the HRA) – each of these three approaches delivers a number of potential replacements, which is either a gain or loss on the RTB sales made.

1.17 Whilst local authorities have been able to draw on reserves and other resources to form the 70% element of funding, the use of HRA borrowing headroom only in the model is felt to be a good proxy for how these resources are used up over the forthcoming 5-year period; for example at the national level c£550-600m of 141 receipts requires £1.4billion of other resources (i.e. in this example borrowing) to form a full programme; this is barely 2-3 years of borrowing headroom nationally and at the local authority level the picture is very mixed.

1.18 The Baseline Replacement model is then projected forward for 5 years, using the volumes and receipts in real terms from 2017.18, principally to test the rate at which authorities would use up their borrowing headroom in forming programmes, as would be expected some authorities will have sufficient headroom to provide for the 70% element for many years, others do not have the headroom to match for one year.

1.19 It is recognised that local authorities are able to provide resources additional to borrowing in order to provide for the 70% "matching element". These include: revenue and reserves, other capital resources from (for example) s106 commuted sums, other capital receipts and also those amounts deductable from gross receipts (principally the administration and debt repayment elements) prior to determining the level of 141 receipts applicable.

[3] *We considered whether land value data might be obtainable at the individual local authority level, and whilst there is some evidence gained, this tends to be skewed by the operation of the market and small samples in certain areas; we have therefore retained an estimate of land values for affordable housing at the regional level.*

1.20 We have analysed HRA outturn statistics from 2015-2017 in order to test whether there is a realistic and meaningful potential stream of ongoing revenue resources to support replacement programmes. Our conclusion is that, whilst some authorities do have considerable reserves, the number is limited and, given that revenue reserves are only useable once, the impact on the overall forecast would be immaterial.

1.21 Conversely, we have applied a variation to the main forecast to test the impact of whether the application of the "deducted amounts" to the programme could add to supply - this is a potentially material output and is covered below. We have NOT carried out any modelling of the impact of being able to utilise the Local Authority Share as we consider that most authorities will utilise these resources to help support their mainstream capital programmes; similarly we have NOT modelled any change in the use of retention of the Government Share as this would be a national cost to Government - which was the principle established by HM Treasury in 2012.

1.22 All factors are then able to be varied in order to test the operation of various policy and other levers on replacement supply and investment over a 5-year period. We have also presented outputs at the regional level in order to exemplify and highlight the differential experiences around the country. Our modelling is available to the Local Government Association in order to respond to any queries that individual authorities may have on the basis of the detailed modelling applied to each. However, we consider the differential in regional experience to be significant and worthy of highlighting throughout within this paper.

1.23 In respect of the modelling of varying discount levels, we have applied the following methodology:

1. The discount levels applying in 2016.17 have been varied in order to increase potential selling prices for homes.
2. Income distribution at the local authority level has been cross-referenced with an affordability factor to represent the potential for purchase at different income levels given different sales prices (arising from varying the level of discount) - the core affordability factor is 5 (i.e. we expect sales prices up to five times income to be affordable to a %age of the local authority population.
3. The ability for more of the local authority population to achieve a purchase is then moderated by a factor employed to represent the fact that some of the stock will not be able to be sold (for example sheltered housing).
4. The outcome is an estimate of the number of sales reduced as a result of reducing discounts - applied against the 2016.17 sales rates at the authority level.
5. The reduced sales volumes are then applied to the increased sales price in order to estimate the change in receipts as a result of varying discounts, and therefore the increased or reduced capacity of the authority to replace supply.
6. Finally, we have applied the increased potential for replacements for those authorities where there is a forecast increase - this models the change in gain/loss of replacements compared to sales from changed discount rates.

1.24 Three approaches to varying discounts have been tested: a flat cash reduction across all authorities, a uniform %age reduction across all authorities, and a regional-based maximum discount.

1.25 It is recognised that Government policy is to encourage home ownership and that any reduction in sales volumes affects the achievement of that objective. This highlights therefore that there is potentially a balance to be struck within Government policy between the need to maximise the supply of housing (including affordable housing) and the ability of more households to access the Right to Buy through increased discounts.

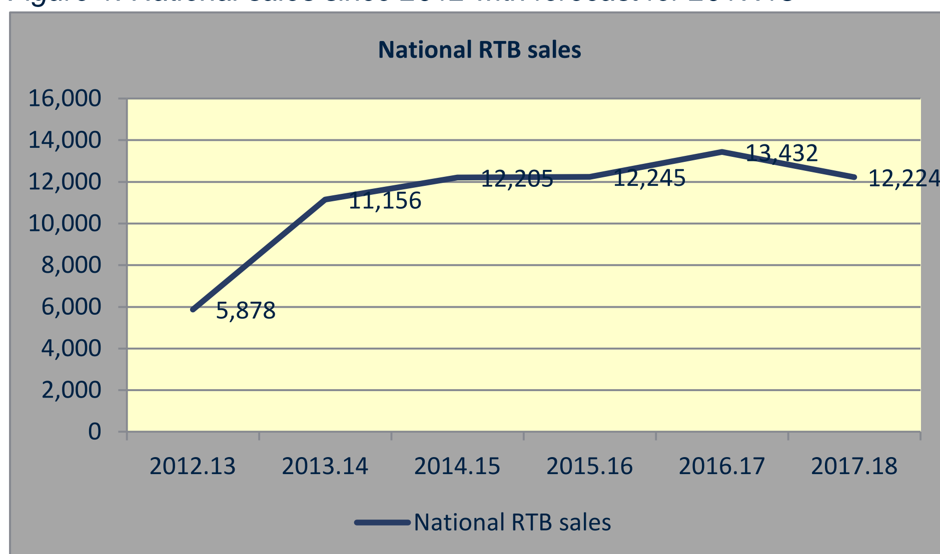
1.26 We have not sought to lock into the national model the impact of possible changes to the "3 year rule" for replacement prior to return of receipts. There are too many variables at the individual authority level, not least the prevailing position within agreements as at 2017.18. However, this has emerged as a major issue in our qualitative engagement and is highlighted below. It is acknowledged that the presentation of annual replacements is a proxy for an actual programme, which will be made up of receipts and expenditure over several years.

2. Baseline Replacement Model: Summary Outputs

Summary

2.1 The chart below shows the trend in sales since the reinvigoration of the RTB policy in 2012. In the year immediately prior to the extension of discounts which formed the basis of the reinvigoration policy (2011.12), sales were at very low levels historically - less than 3,000 per annum. Discounts had been restricted to much lower maximums and volumes were also affected by the financial crash and subsequent trends within the housing market generally.

Figure 1: National sales since 2012 with forecast for 2017.18

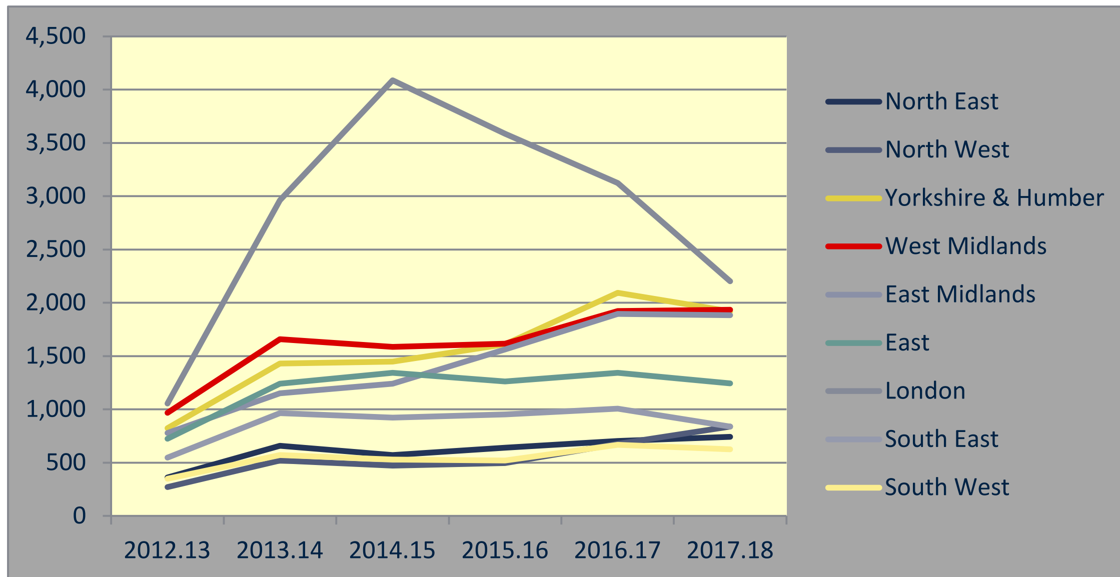


2.2 The national picture shows one of an increase in sales following 2012, with a period of 2-3 years taken for sales to reach a reasonably steady state, followed by further increases in volumes to 2016.17. Recently however, sales have begun to decline in many areas, particularly in those authorities where there had been high levels of sales in the 2014-2016 period.

2.3 However, the national position set out above masks a highly variable picture at the regional level. This is exemplified in the chart below.

2.4 At a regional level, sales volumes are expected to either be maintained or increase in 2017.18 in the northern and midlands regions. Sales volumes within the wider south and east are forecast to decline. However, sales volumes in London have reduced quite significantly during the first two/three quarters of 2017.18 when compared to the previous 2 years. The change in activity in London is really quite marked and a key driver for the generation of sales and receipts levels nationally. Authorities engaged during the course of this work suggest that sales may have peaked as a result of rising values in London where increases in discount rates do not match the price increases, perhaps also coupled with a tightening up on application procedures at many authorities.

Figure 2: Regional sales trends 2012 - forecast 2017.18



Baseline sales, receipts and 141 receipts forecast

2.5 The forecast level of sales, receipts and estimate of 141 receipts retained within the Retention Agreements is set out in the table below.

Figure 3: Forecast sales, gross and 141 receipts 2017.18 by region

	Sales	%age stock	Average values	**Gross receipts**	All allow'ces	**141 receipts***	%age of total
			£	**£'000's**	£'000's	**£'000's**	
ENGLAND	**12,224**	**0.77%**	**85,099**	**1,040,253**	**-454,597**	**585,656**	100.00%
North East	**741**	0.81%	42,916	**31,801**	-24,029	**7,772**	1.33%
North West	**837**	1.04%	44,824	**37,518**	-27,344	**10,174**	1.74%
Yorkshire & Humber	**1,919**	0.83%	45,626	**87,556**	-53,913	**33,643**	5.74%
West Midlands	**1,933**	0.95%	50,213	**97,062**	-57,306	**39,756**	6.79%
East Midlands	**1,883**	1.07%	51,141	**96,298**	-48,658	**47,640**	8.13%
East	**1,245**	0.75%	115,602	**143,924**	-52,788	**91,136**	15.56%
London	**2,202**	0.56%	177,811	**391,539**	-128,658	**262,881**	44.89%
South East	**839**	0.54%	124,626	**104,561**	-41,250	**63,311**	10.81%
South West	**625**	0.66%	79,990	**49,994**	-20,651	**29,343**	5.01%

** The modelling suggests there are 3 authorities (of 164) that would have insufficient receipts for a 141 Agreement*

2.6 The table shows that:

- The forecast level of sales is 12,224 for 2016.17 representing 0.77% of the total HRA stock, generating £1.040bn of sales receipts (after discounts).

- After deduction of allowances for administration, debt repayment (totalling £158m between them), wider Local Authority and Government shares (totalling £298m between them), the net receipts which could form part of a 141 replacement programme are forecast to be £586m.
- The regional experience varies significantly. Forecast 141 receipts are quite limited in some regions, compared to the level of sales. Less than 10% of the 141 receipts arise in the three northern regions, compared to c30% of the sales; over 75% of 141 receipts are focused in London and wider south and east.

2.7 141 receipts are applied to a prospective programme in which they represent the maximum allowed 30% of development costs - with the other 70% in the Baseline Replacement model coming from HRA borrowing. The application of borrowing is assumed to be an effective proxy for the application of "matched" funding. In practice, local authorities are able to apply other sources of funding such as receipts or s106 contributions - however it is assumed that these are also finite, or at least limited over time.

2.8 Our initial headline forecast exemplifies the capacity of 141 receipts to enable the replacement of supply of affordable housing, given no restriction on borrowing or other sources of funding for the 70% element. This is then varied to allow for the constraints of the Debt Cap on limiting borrowing to provide the 70% matched element.

2.9 The unrestricted replacement potential, by region, is shown in the table below.

Figure 4: Forecast and potential replacements given unrestricted access to 70% match funding

2017.18	141 receipts	Other funding	Progrmm total	Replace-ments	Sales	**Gain/loss**
	£'000's	£'000's	£'000's			**£'000's**
ENGLAND	**585,656**	**1,366,532**	**1,952,188**	**16,069**	**12,224**	**3,845**
North East	7,772	18,136	25,908	259	741	**-482**
North West	10,174	23,739	33,913	338	837	**-499**
Yorkshire & Humber	33,643	78,500	112,143	1,122	1,919	**-797**
West Midlands	39,756	92,765	132,521	1,326	1,933	**-607**
East Midlands	47,640	111,160	158,800	1,588	1,883	**-295**
East	91,136	212,651	303,787	2,531	1,245	**1,286**
London	262,881	613,390	876,271	6,260	2,202	**4,058**
South East	63,311	147,725	211,036	1,758	839	**919**
South West	29,343	68,466	97,809	887	625	**262**

2.10 The table highlights the following main outputs:

- At a national level, the generation of 12,224 sales and 141 receipts of £586m could deliver a programme of £1.95bn of replacement stock, representing an estimate of just over 16,000 units (16,069 - a net gain of 3,845) assuming all other things are equal. The replacement profile nationally would be 1.31 to 1.

- However, this national net position masks a highly variable position at the regional level in which not one of the five northern and midlands regions are able to achieve a "One for One" replacement programme.

2.11 Not included within the table but behind the headline regional figures, the number of authorities where there is the potential to gain stock (i.e. better than One for One) is 102 (out of 164), of which 91 are in the London and wider south/east regions.

2.12 Whilst it is understood that the policy of "One for One" is intended to operate at the national level, the net loss of affordable housing within large parts of the country is a potentially significant consequence of the operation of the agreements, particularly given the demand for affordable housing across the country generally. This might be of interest to those authorities affected where the implied outcome of the operation of the agreements as they currently stand is that the proportion of affordable housing is shifted from the north and midlands to London and the South.

2.13 If sales trends continue into the future as they have from 2016 to 2018, this process of regional difference may be somewhat ameliorated given that sales volumes are reducing in London and the wider south/east with maintaining or increasing levels in the north and midlands; however this has the potential to exacerbate supply and demand issues across the country, as northern and midlands authorities continue to see their stock reduced with no current route to fully replacing that supply.

Effect of the Debt Cap

2.14 As is well understood, access to alternative resources to make up the 70% matching element is far from unrestricted. The table below shows the impact on the 2017.18 replacement potential if the 70% element is assumed to be solely from borrowing (see above) and this borrowing is restricted by the debt cap.

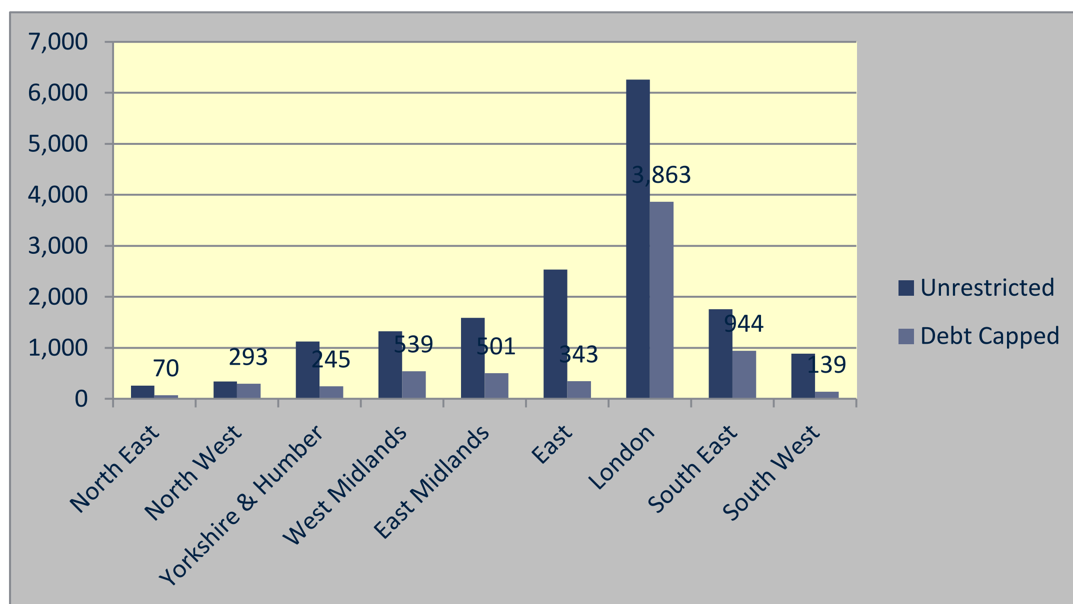
Figure 5: Forecast and potential replacements restricted by borrowing for the 70% element

2017.18	Progr. total	Replace-ments	Gain/loss	141 recs used	Receipts paid over
	£'000's			£'000's	£'000's
ENGLAND	**1,585,327**	**13,037**	**813**	**475,598**	**110,058**
North East	20,771	208	-533	6,231	1,541
North West	33,913	338	-499	10,174	0
Yorkshire & Humber	79,962	800	-1,119	23,988	9,655
West Midlands	115,107	1,152	-781	34,532	5,224
East Midlands	135,503	1,355	-528	40,651	6,989
East	224,286	1,869	624	67,286	23,850
London	731,341	5,223	3,021	219,402	43,479
South East	169,866	1,416	577	50,960	12,351
South West	74,579	676	51	22,374	6,969

2.15 The table shows that:

- The potential replacement programme is reduced to £1.59bn (from £1.95bn) as a result of the operation of the Debt Cap and restriction affecting some authorities in borrowing to match the 141 receipts.
- The forecast number of replacement units is reduced to 13,037 (from 16,069). The majority of the reduction in potential replacements is focused into those regions with the largest potential unrestricted capacity to replace (i.e. London and the wider south/east). This is highlighted in the chart below (which sets out the replacement volumes restricted by the Debt Cap for 2017.18 - applying one year only.
- Under the prevailing borrowing restriction, the estimate of receipts paid over to Government unspent is £110m.

Figure 6: Change in replacement potential as a result of the HRA Debt Cap - year 1 only



2.16 We have then varied the level at which authorities may reasonably be expected to borrow within their Debt Cap to provide the 70% "matched" funding. Research undertaken by Savills on behalf of the council housing trade bodies and CIPFA in 2017[4] highlighted that it is not best practice in the context of effective long-term business planning to assume that borrowing is maximised to 100% of debt facility at any one time - as this reduces the opportunity to address risks within the business plan.

2.17 We have therefore applied a theoretical limitation to borrowing below the cap of 10% and 20% to show how this might impact on the ability to provide for replacements. The outputs are set out in below:

[4] *http://www.arch-housing.org.uk/news/latest-news/"raising-the-roof"-an-analysis-of-hra-borrowing-headroom.aspx*

- If borrowing is restricted to 10% below Debt Cap, the impact on the potential replacement programme is to reduce it from £1.59bn to £0.87m, reducing replacements from 13,037 to 6,937 - which is a net loss annually against sales of 5,287. Only the London and South East regions would have a positive "gain/loss" net replacement.

- Further, if borrowing is restricted to 20% below Debt Cap (which some might consider a prudent buffer in a business plan - and would be best practice for housing associations), the impact on the potential replacement programme is to reduce it from £1.59bn to £0.43m, reducing replacements from 13,037 to 3,201 - which is a net loss annually against sales of 9,023. Only in London would there be the potential for a positive "gain/loss" net replacement.

2.18 This highlights that any potential consideration of the relaxation of the Debt Cap within the forthcoming HRA Borrowing Programme should not be accompanied by an expectation of prevailing borrowing headroom - as many authorities will be understandably cautious about maximising their borrowing in the context of their business plans.

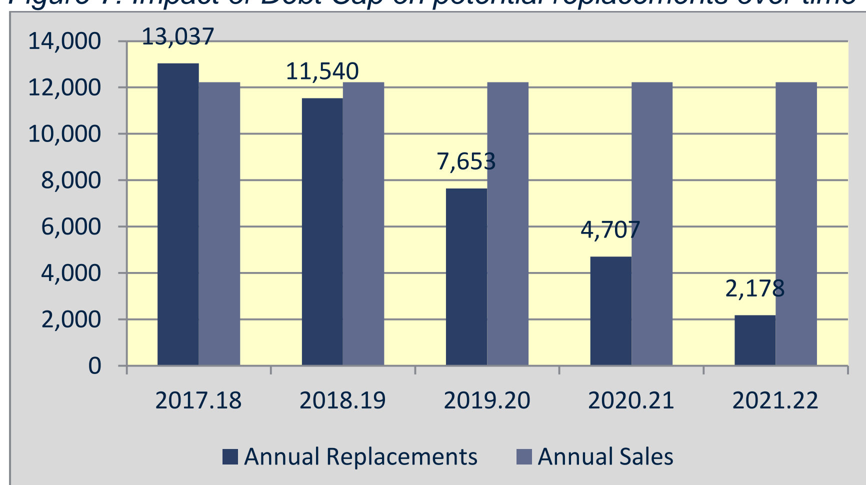
Effect of the Debt Cap - over time

2.19 The Debt Cap is fixed over time. If the same Debt Cap applies to the forecast 5-year period within the model, this will restrict future programmes for replacement beyond 2017.18 as borrowing headroom is used up. Notwithstanding the point made above around there not being a requirement to borrow up to cap, we have modelled the impact of the Debt Cap on the basis that authorities are able to deploy resources up to the Cap to try to match the 70% element.

2.20 The outputs are based on the continuation in real terms of sales volumes and receipts for the next 5 years with no further upwards or downwards trends in sales. The outputs are set out below. They show a relatively stark picture of the rate at which borrowing headroom "runs out" over time.

2.21 The chart below shows the forecast over 5 years inclusive of the estimates made for 2017.18.

Figure 7: Impact of Debt Cap on potential replacements over time



2.22 The table below further shows the impact on the potential of authorities to sustain a replacement programme if debt caps remain unchanged.

Figure 8: Number of authorities able to sustain 141 replacement programme - 5 years

Year	2017.18	2018.19	2019.20	2020.21	2021.22
Authorities with a programme	152 *	126	100	76	54

* *Note that two authorities are estimated to be 1 unit only, the remaining 12 authorities have no programme*

The table highlights that less than a third of authorities would be able to sustain a programme of replacements through the 141 agreements in 5 years' time.

2.23 The 5-year impact of the continued restriction via the operation of the Debt Cap is set out in the table below.

Figure 9: Five year totals of 141 receipts, replacement potential and net gain/loss of units

5 year totals	141 recpt	Borrow	Program	Paid over	Potential	Gain/loss
	£'000's	£'000's	£'000's	£'000's	Repl'mnts	5 years
ENGLAND	**1,417,960**	**3,308,573**	**4,726,533**	**1,510,320**	**39,115**	**-22,005**
North East	20,113	46,931	67,044	18,747	671	-3,034
North West	45,255	105,596	150,852	5,615	1,503	-2,682
Yorkshire & Humber	84,469	197,095	281,564	83,746	2,818	-6,777
West Midlands	121,801	284,202	406,003	76,979	4,064	-5,601
East Midlands	121,968	284,591	406,559	116,232	4,066	-5,349
East	145,664	339,883	485,547	310,016	4,047	-2,178
London	650,468	1,517,759	2,168,227	663,937	15,487	4,477
South East	179,180	418,087	597,267	137,375	4,979	784
South West	49,041	114,429	163,470	97,674	1,480	-1,645

2.24 The table shows that the forecast replacement potential is just over 39,000 against sales volumes of over 61,000 across a 5-year period and that more than half of the potential 141 receipts arising would need to be given to Government as matching funding would not be able to be found from borrowing for these receipts (£1.51bn sent to Government compared to £1.42bn retained and spent locally).

2.25 Only in the South East and London regions are replacements at greater than one for one over the 5-year period.

Summary

2.26 At the national level, it is clear from the foregoing that if the Government and local authorities are committed to a One for One Replacement Programme at a national level and debt caps continue at their current rate, alternative resources to match the 141 receipts would need to be found (and

it is unclear what these might be given the prevailing policy towards authorities not being able to accompany the use of 141 receipts with grant from Homes England).

2.27 The lifting of Debt Caps must therefore be a pre-requisite to achieving a One for One programme at the national level. The programme for lifting borrowing headroom announced in the Budget and shortly to be consulted upon may be seen as a welcome opportunity for many authorities to achieve a bigger replacement programme. Our analysis highlights that restricting this programme to those close to Debt Cap might risk under-playing the potential for authorities in general to join the borrowing programme. Put another way, it is likely that replacement rates under the 141 agreements will be higher should there be no restriction in the ability of authorities to bid for additional headroom.

2.28 There are a range of issues to arise from the regional analysis of the position, including the inability for northern and midlands authorities to replace stock lost through the Right to Buy using any reasonable combination of assumptions based on the current arrangements in place for 141 agreements. Raising debt caps does not provide for anywhere near a One for One replacement profile in these regions.

2.29 In turn, this might underpin a view whereby policy could be driven in different regions offered different approaches to the arrangements in place for agreements. This is explored in more detail in the next section.

3. Varying key factors within the Baseline Model

3.1 This section analyses the possible impact of varying different factors within the 141 agreements and tests whether by varying these factors, there might be the opportunity to increase replacement potential and therefore the supply of affordable housing.

Varying development costs

3.2 The Baseline Replacement model makes assumptions of build costs at a regional level, and nil land costs. This is felt to be appropriate for the baseline test given that the overwhelming majority of new developments to provide replacement stock are likely to be undertaken on existing council land, in particular within the HRA.

3.3 However, many authorities are reporting increased build costs and that they are running out of "free" land and that they may need to enter the land market in order to sustain 141 replacement programmes. We have therefore modelled an impact on replacement potential arising from higher build costs and/or the inclusion of land costs (for affordable housing). The outputs are set out in the tables below.

Figure 10: Modelling varying build costs

	Build £/unit - LOW/BASELINE	Build £/unit -HIGH *	Land / plot £
East	120,000	140,000	30,000
East Midlands	100,000	120,000	20,000
London	140,000	175,000	60,000
North East	100,000	100,000 *	10,000
North West	100,000	100,000 *	15,000
South East	120,000	150,000	40,000
South West	110,000	130,000	25,000
West Midlands	100,000	120,000	20,000
Yorkshire & Humber	100,000	100,000 *	15,000

* *North region costs are unaffected by a change in assumption given recent trends*

Figure 11: Gross impact of higher build costs and land costs on 5 year replacements

	5 year total	Differ-ence	%age
Baseline replacements	**39,115**		
Higher build costs	**32,861**	-6,254	-16%
Including land costs	**30,163**	-8,952	-23%
Higher build costs with land	**26,455**	**-12,660**	**-32%**

Figure 12: Regional impact of increased costs and land on replacements 5 years

	High Build + Land	Baseline	Difference	%age
North East	608	671	-63	-10%
North West	1,312	1,503	-191	-15%
Yorkshire & Humber	2,446	2,818	-372	-15%
West Midlands	2,905	4,064	-1,159	-40%
East Midlands	2,908	4,066	-1,158	-40%
East	2,853	4,047	-1,194	-42%
London	9,227	15,487	-6,260	-68%
South East	3,140	4,979	-1,839	-59%
South West	1,056	1,480	-424	-40%

3.4 The tables show that, at a national level, the potential for reduction in programmes is around 16% from higher build costs across the south and midlands, and when land costs are also included, this reduction in potential is as much as one third nationally. This level of replacement would mean less than "One for Two" compared to sales volumes over the 5-year period.

3.5 As would be expected, at a regional level, the changes in assumptions have much more potential impact, with the London region in particular subject to the potential for a very large reduction in replacement rates from a requirement to provide for land costs. At this level, there would be a net loss of units in the London region (i.e. less than One for One replacement).

3.6 The foregoing analysis suggests that increasing build costs and the increasing scarcity of free land within councils has the potential to significantly impact on the capability of 141 programmes to replace at a rate of One for One. As free land runs out, the current policy will come under increasing pressure, and is likely to necessitate the incorporation of additional resources including further extension of borrowing caps in order to sustain the achievement of One for One replacements.

Varying the Funding Mix (30%/70% Matching arrangements)

3.7 Many authorities have suggested that the restriction of the use of 141 receipts to a maximum of 30% of the development cost of a programme is constraining their ability to invest receipts alongside borrowing and other resources in order to achieve replacements.

3.8 In order to test this view, we have modelled the impact of varying the 30:70 matching arrangement to 40:60 and 50:50 whilst maintaining all other factors. The outputs are set out below.

3.9 The table below shows the *national impact* of varying the matching mix - as if the change/variation applied to all authorities.

Figure 13: National impact of varying 30:70; 40:60 and 50:50 funding mixes

	30:70	40:60	50:50
Baseline replacements	39,115	37,649	34,879
Increase/decrease		-1,466	-4,236

3.10 The table shows that the current 30%/70% approach is likely to provide for the most replacement units at a national level. This is somewhat to be expected given that, for those authorities with sufficient headroom to sustain a programme for several years, the 30%/70% approach is able to generate a higher programme level than the variations (for example, for every £1m of 141 receipts, unrestricted borrowing could generate a programme of £3.3m at 30:70 and £2.5m at 40:60).

3.11 However, the picture is radically different if applied at the individual authority level. Some authorities will have limited headroom that will be able to be sustained for longer and therefore a longer programme, if the matching requirement is changed to 40:60 or 50:50. We have tested this at the authority level and identified those authorities with greater potential from either of these two variations, then made an assessment of which approach offers the best opportunity to maximise replacement units if each authority could select the best approach for itself. The outputs are set out in the table below.

Figure 14: Impact of varying 30:70; 40:60 and 50:50 funding mixes at individual LA level

5 year totals	**Replacement potential**				**No authorities best suited**		
	30-70	**40-60**	**50-50**	**Max**	**30-70**	**40-60**	**50-50**
North East	671	640	582	752	1	1	2
North West	1,503	1,270	1,020	1,503	9	0	0
Yorkshire & Humber	2,818	2,540	2,289	2,968	8	1	1
West Midlands	4,064	3,203	2,852	4,064	12	0	0
East Midlands	4,066	3,791	3,826	4,737	16	2	6
East	4,047	4,508	4,551	5,005	9	3	12
London	15,487	15,417	14,191	16,657	14	5	9
South East	4,979	4,629	4,055	5,317	15	3	9
South West	1,480	1,651	1,513	1,852	5	3	4
England	**39,115**	**37,649**	**34,879**	**42,855**	**89**	**18**	**43**

3.12 The table shows that by variably applying the different funding mix/matching principles at the individual authority level and allowing each authority to select the approach which maximises potential replacement delivery, this could increase 5-year supply by up to 10% (all other factors being equal). The number of authorities estimated to benefit from moving to 40:60 is 18 (c12%) of all authorities) and from a move to 50:50 is 43 (around one quarter of all authorities).

3.13 This analysis supports an approach which is based on individual flexibility negotiated between authorities and Government in the operation of their 141 agreements. Around 40% of those

authorities with potential programmes would be able to deliver more supply for the same sales and receipts if given flexibility to move away from the 30%:70% funding mix.

3.14 Whilst there is no obvious pattern at the individual authority level as to which authorities are better placed to adopt greater flexibility, particularly given that levels of borrowing headroom are almost entirely a result of historical decisions, there *is* an apparent focus in those authorities which might benefit from flexibility in the London and wider south/east regions. This might simply be because these regions have the greatest potential for supply from a higher level of receipts than the northern and midlands regions. There is no trend which would suggest anything other than authority-by-authority flexibility is the optimal way to maximise reinvestment.

3.15 If borrowing levels are able to be less restricted (or removed), this would affect the outputs above. In an environment where borrowing is unrestricted by a cap, the level of matched funding required should then be seen primarily in the context of deemed grant support. For example, we would expect that an authority where there are (say) 40% of developed costs required for grant support in order to make for a sustainable investment programme for social rented housing, that this would be mirrored in any bid for additional borrowing headroom.

3.16 Our analysis highlights the potential for flexibility in the matched funding arrangements when borrowing and other funding restrictions continue to apply, and highlights that an open and flexible approach to setting borrowing levels and funding matching %ages at the local authority level is likely to provide the best opportunity to maximise replacement supply under 141 Agreements.

Varying the availability of other resources

3.17 It is acknowledged elsewhere within this analysis that revenue and reserves resources are likely to remain as restricted as other capital sources in the context of other pressures within HRAs. For example, reserves are only able to be utilised once.

3.18 However, there is one potential source of resource that could assist in furthering the potential for replacement within 141 agreements: that represented by the Administration and Debt-Repayment allocations within the calculation of the 141 receipt amount. In effect, these amounts are deducted from gross receipts prior to determining the level of 141 receipts (for the 30%:70% matching principle) but in theory they could be available for spending on capital programmes.

3.19 The amounts that are deducted in the Baseline Replacement model for the 2017.18 year are estimated at £158m. Over time, the generation of these resources allows debt to be reduced thereby increasing headroom for programmes in the future. Were these to be added to the programme funding sources, therefore, this could add the potential to increase programmes by up to 7,000 units over 5 years.

3.20 If other sources such as borrowing are similarly unrestricted, this would be an increase over 5 years of 9% - increasing the national replacement potential from 1.3 to 1 becoming 1.4 to 1. However, given that other resources are not currently unrestricted, the capacity for these

deductions to add to the programme is limited by the debt cap - i.e. these resources are unable to form the 70% element without borrowing - and this remains restricted by the cap.

3.21 This is highlighted as a variation for the potential to achieve higher replacement programmes - individual authorities would need to take specific decisions to act in this way as there is no compulsion to do so.

Summary

3.22 The variation of key factors at the national and local level suggests the following high level conclusions:

- The decreasing availability of free land and increasing pressures on build costs have the potential to significantly affect the ability of authorities to maintain 141 replacement programmes at current levels in the future. The Government should work with authorities to assess the impact in detail at a local level and the forthcoming HRA Borrowing Programme needs to be sufficiently flexible in its allocations to address these pressures.

- Changing costs of development also have the potential to require higher grant levels within the Affordable Homes Programme and the allocation for new social rented units is likely to have to reflect these cost pressures. Given the relationship between grant assumptions and 141 RTB programme assumptions, these pressures would suggest a case for higher grant rates and therefore a move away from the 30:70 matching principle.

- There is strong evidence from this analysis that varying the 30:70 principle to 40:60 or 50:50 on a flexible, authority-by-authority basis, has the potential to increase replacement supply by 10%.

- There is evidence to suggest that a flexible approach to the reinvestment of receipts deducted from the 141 receipts calculation could also enhance replacement programmes, by up to 9% depending on the approach taken to removing restrictions on borrowing.

4. Varying discount rates and the impact on replacement supply

4.1 Part of the brief for this analysis included working up a model of how sales rates and levels of receipt might vary if it were possible to change the maximum discounts available under the Right to Buy across the country. The analysis tests the hypothesis that reducing discount rates in some circumstances at some authorities might have the impact of reducing sales volumes but lead to a net increase in receipts - thereby enabling greater addition to replacement supply. We are aware from this analysis that authorities in the north and midlands are selling homes (particularly flats) at such low values that there is a view that were the price to increase, this might not affect sales potential.

4.2 In order to carry out this test, we have developed a Discounts Model which allows a forecast impact on sales volumes to be modelled based on the variation of discounts in a specific set of circumstances (see the methodology above).

4.3 The model allows discounts to be varied (reduced or increased) by a fixed £ amount nationally applying to every authority, a fixed national %age variation applying to every authority, and a regional-based approach similar to that in place currently which distinguishes between maximum discounts in London and the rest of England (but extended to vary by all regions).

4.4 The outcome of the modelling is set out below. At the outset, it is emphasised that the outputs appear to offer substantial evidence to suggest that selective reduction in discount rates would actually lead to greater net receipts and therefore a larger replacement programme.

4.5 The table below shows the potential impact if discounts are reduced by a flat rate £20,000 per sales across the board.

Figure 15: Impact of reducing maximum discount rates by £20,000 across all authorities

2017.18	Reduc-tion in sales	Reduc-tion in receipts NET	Increased receipts in specific LAs	No of LAs with increased receipts
		£'000s	£'000s	
ENGLAND	**3,287**	**-67,485**	**26,222**	**74**
North East	186	2,811	2,811	**6**
North West	152	2,833	2,871	**8**
Yorkshire & Humber	535	8,027	8,668	**9**
West Midlands	507	3,642	4,156	**11**
East Midlands	487	5,319	5,321	**24**
East	271	-7,457	1,682	**6**
London	757	-71,857	0	**0**
South East	239	-10,759	160	**4**
South West	153	-44	552	**6**

4.6 The table shows that the impact on sales volumes might be expected to not be insignificant, reducing them by c25% (3,000+) per annum, given that many households pursuing the Right to Buy will be particularly sensitive to price changes at the margins.

4.7 However, whilst the overall net reduction in gross receipts (as opposed to 141 receipts) would be £67m per annum, this masks a significant regional and individual local authority impact. There would be an estimated 74 authorities with a gain in receipts as a result of restricting discounts in this way, leading to the availability of £26m of investment potential (gross) at those authorities. This might translate into 141 receipts of £22m thereby facilitating an additional replacement programme of £75m which is around 600-700 additional replacement supply every year depending on the authority.

4.8 58 of the 74 authorities would be in the northern and midlands regions. Conversely, no authority would have a larger programme in London.

4.9 We have also modelled this approach with maximum discount changes of £10,000 and £30,000:

- Changing discount rates by £10,000 -> 1,751 fewer sales (14%) with an estimated 83 authorities with an extra £20.1m receipts.
- Changing discount rates by £30,000 -> 4,672 fewer sales (38%) with an estimated 61 authorities with an extra £21.5m receipts.

4.10 As would be expected, there is a similar impact by varying discounts by a fixed %age amount. The table below repeats the analysis above with a fixed reduction of 20% in discount levels across the board.

Figure 16: Impact of reducing maximum discount rates by 20% across all authorities

2017.18	Reduc-tion in sales	Reduc-tion in receipts NET	Increased receipts in specific LAs	No of LAs with increased receipts
		£'000s	£'000s	
ENGLAND	**2,120**	**-69,824**	**17,746**	**82**
North East	90	1,648	1,648	**6**
North West	69	1,504	1,514	**8**
Yorkshire & Humber	237	5,064	5,340	**10**
West Midlands	263	3,417	3,705	**12**
East Midlands	237	3,812	3,833	**24**
East	194	-6,394	599	**7**
London	757	-72,240	0	**0**
South East	172	-7,063	434	**6**
South West	101	425	674	**9**

4.11 The table shows that the impact on sales volumes is again not insignificant, reducing them by c17% (2,100+) per annum. Whilst the overall net reduction in gross receipts (as opposed to 141 receipts) would be £70m per annum under this scenario, there would be an estimated 82 authorities with a gain in receipts as a result of restricting discounts in this way, leading to the availability of £18m of investment potential (gross). This might translate into 141 receipts of £15m thereby facilitating an additional replacement programme of £50m which is around 400-500 additional replacement supply every year depending on the authority.

4.12 60 of the 74 authorities would be in the northern and midlands regions. Again, no London authority would have a larger programme.

4.13 We have also modelled this approach with discount changes of 10% and 30%:

- Changing discount rates by 10% -> 1,119 fewer sales (9%) with an estimated 81 authorities with an extra £10.6m receipts.
- Changing discount rates by 30% -> 3,051 fewer sales (25%) with an estimated 79 authorities with an extra £21.8m receipts.

In this case, restriction of discounts leads to a better overall replacement rate potential at 30% than 10% or 20%.

4.14 Finally, we have developed a hypothetical approach in which maximum discounts are reduced in those regions with the greatest capacity for increased programmes at lower discount levels. In order to illustrate this hypothesis, we have set a fixed reduction to discounts in the five regions of the north and midlands but left the prevailing level of discounts in the south/east and London regions as they are. This approach might be said to maximise the potential to act flexibly to encourage an optimal balance between sales and replacements based on a regional approach but is intended as an illustration (not a recommended approach) only.

4.15 As it would be to reasonable to expect that any fixed discount reduction would apply regionally irrespective of whether it led to an increase or reduction in receipts (in other words it would be difficult to allow individual authorities to "opt out" in these regions), the extract from the table above set out below exemplifies the illustration.

Figure 17: Impact of reducing maximum discount rates by £20,00 for all authorities in five regions

2017.18	Reduction in sales	Net increase in receipts
		£'000s
North East	186	2,811
North West	152	2,833
Yorkshire & Humber	535	8,027
West Midlands	507	3,642
East Midlands	487	5,319
Total	**1,867**	**22,632**

4.16 In this illustration, the net additional gross receipts to authorities would be £22.6m per annum with a reduction of sales of 1,867 (15% nationally but 26% of the forecast sales in these five regions). The use of these receipts would then break down as follows:

Gross additional receipts	= £22.6m
After deductions for admin/debt repayment	= £19.2m
Matched at 30:70	= £64.0m
Assumed build cost £100k/unit (no land cost)	
Total additional potential programme	= 640
Total 5-years' additional programme	= 3,200
Addition to baseline replacement forecast	= 8% (on 39,115)
Stock not subject to sale	= 1,867
5-years' stock not subject to sale	= 9,335
Net potential for more social units over 5 years	= 12,535 [5]

4.17 As set out above, we estimate that by capping discounts in the five northern and midlands regions by a flat £20,000 applying to all sales, this could lead to a net greater social/affordable housing stock of c12,500 homes over a 5-year period - this includes a reduction in sales in order to achieve a higher discount which then allows for a higher replacement programme.

Summary

4.18 There is substantial evidence that a selective reduction in the rates of discounts offered to households, whilst leading to a reduction in sales volumes, could lead to an increase in gross receipts - as the reduction in sales is more than offset by a higher average sales price.

4.19 We estimate that by capping discounts in the five northern and midlands regions by a flat £20,000 applying to all sales, this could lead to a net greater social/affordable housing stock of c12,500 homes over a 5 year period.

[5] *Assumes no restriction in matching funds*

5. Summary of Local Authority engagement

5.1 The "qualitative" part of this paper is based upon the engagement of 12 local authorities, selected for their geographical, regional, size, experience and political mix to provide a representative sample of the experiences of the RTB and 141 Retention Agreements policy since reinvigoration in 2012.

5.2 The authorities are scheduled at the appendix along with the ticksheet of issues which were raised and discussed with each one. Two engagements took place at face to face meetings, the remainder were telephone interviews. Set out below is a high level summary of findings from the discussions - we have not sought to highlight specific points relating to specific authorities as an undertaking of confidentiality was provided. However, we will be contacting the authorities again as part of the finalisation of this report and they may be comfortable at being directly quoted, and a more detailed analysis of responses will be appended to the final report.

5.3 The interviews relating to trends and volumes are consistent with the analysis within this paper. Half of the authorities are experiencing a tailing off or levelling off of sales following a peak in the period from 2014 and 2016; this is particularly the case in the London authorities contacted as well as in the wider southern regions. Some authorities are experiencing continued growth and expect no levelling off as sales volumes appear to increase year on year. In the London and southern/eastern regions, discounts are reported to be at the maximum pretty much for all sales. The discounts offered in the north and midlands make replacement of 1 for 1 impossible and in some cases lead to extremely low sales prices (in one case just £15k for a flat).

5.4 Authorities were asked to comment on their approach to securing a robust application process. A majority of authorities reported that they had deployed staff to check individual premises which are the subject of RTB applications so that basic checks on eligibility are covered. Around half of the authorities reported that they had utilised fraud prevention officers in dealing with spurious or false applications.

5.5 Two authorities have introduced an extensive addition to the standard forms requiring further information to be provided around funding and eligibility. This was reported as having a deterrent effect on those applications which are not directly from the occupying/tenant household.

5.6 One authority has not entered a 141 agreement as the forecast sales in the HRA self-financing settlement mean that there are few if any 141 receipts. Most of the other authorities had been able to sustain 141 agreements without paying any monies to Government but many reported that there are increasing pressures which might mean that money could be paid over in the near future without changes to the rules. These pressures are set out below.

5.7 The rule which states that there is only 3 years in which to reinvest receipts, calculated on a quarter-by-quarter basis was reported universally as an issue for authorities. Most felt that 5 years was a more realistic timeframe and many pointed to recent research by the Home Builders Federation that identified the average period from grant of planning to practical completion across all sites is 3.25 years.

5.8 The 30:70 funding mix works for some authorities. Others reported that a move to 40:60 and 50:50 would allow for more flexibility in the application of the receipts, particularly if this was able to vary between years, or the 30% element was able to be input up-front.

5.9 The debt cap was the single biggest factor affecting the consideration of a move away from 30:70. However, three authorities reported that a move away from 30:70 was likely to be necessary in viability terms as the costs of development were increasing.

5.10 Almost all authorities reported that their “Easy Win” programmes are running out as land and other resources are used up within the HRA. Typical was the sense that infill sites and garage sites are being utilised and that there might therefore need to be a significant change to the basis for the programme in order to enable longer term reinvestment to be sustained, including moving into the market to acquire land.

5.11 Several authorities have subsidiary companies and/or ALMOs in place to supplement the delivery of housing in their area. Many of these highlighted that it would be helpful to be able to deploy 141 receipts into these companies - this might offer increased value for money in terms of the type and nature of affordable housing that the receipts can be used for (for example at intermediate rent levels, the level of receipt matching might be lower than 30%) as well as avoid some of the complex structures now actively being considered by authorities in order to ensure that receipts are reinvested locally.

5.12 There was unanimity on the point that 141 receipts should be able to be utilised for a full range of affordable housing products in line with those supported by Homes England programmes (shared ownership, rent to buy, affordable rent, living rent etc), although not all said that they would immediately consider changing from re-provision of social rent in the HRA. Again, this might enhance value for money making supply go further for a given level of receipts.

5.13 One authority has in the past offered the use of receipts as a grant equivalent for local RPs to bid for and that has proved successful in a limited way. That authority has now moved on to direct re-provision in the HRA. Generally, however, authorities report that engagements with local RPs to take up allocations have generally led to low interest - perhaps locally-based RPs with limited development programmes may not have the appetite, capacity or land/opportunities.

5.14 We note that this might offer a challenge to the original Government thinking that RPs might “absorb” the balance of 141 receipts unable to be spent by authorities

Appendix 1 - schedule of authorities interviewed and issues covered

Derby, Oxford, Warwick, Harrogate
Hackney, Sutton, Haringey, Cheshire West and Chester
Wealden, Epping Forest, Slough, Sheffield

Local Government Association Research into the Right to Buy

Questions/topics to cover

Reminder... not about challenging the policy itself - making it work better in terms of reinvestment...

Policy / operation

General experiences of RTB since April 2012 - volumes, trends, any particular property types or areas that differ?

- Views on discounts - too high, too low... does this differ for different types/areas?
- Views on applicants - ending up with households?
- Steps taken to prevent non-tenant based funded applications?
- Expectations re future trends - stall, reduce, increase etc

Retention Agreement issues

Receipts and spending position - how's it going and threat of return to HMT
Any paid over receipts?

Issues with...?

- 3 year timeframe
- Finding land / sites
- Matching with the receipts as 30% (the 30/70 issue)
- Focus on particular types of affordable housing?
- Investment into companies
- Taken opportunities re RTB buy backs?
- Spent with other parties? Basis and process for this?

Open ended question
Top three things that would change in order to make more sustainable - increase reinvestment?

Appendix 2 - Description of discussions and responses with local authorities

The operation of the Right to Buy policy

Whilst it was outside the scope of this paper and project to question the operation of the Right to Buy scheme at all, and also not to model options in which local authorities had unrestricted access to all receipts, most authorities did feel that they wished to make the points that:

- In an ideal world, they would retain 100% of RTB receipts for reinvestment (8 from 12).
- It was reasonable however that there were expectations around how such funds would be reinvested - and most (of those 8) felt that it was equally important to ensure that RTB receipts were reinvested in new affordable housing (as opposed to general capital expenditure).
- Some felt (4 from 12) that RTB receipts provided a positive contribution to their programmes for new affordable housing and noted that a recent drop-off of sales and therefore receipts may affect their ability to full fund existing programmes of new development/regeneration.
- Unprompted, a significant minority (5 from 12) felt that discount rates were simply too high for some types of properties in some locations and questioned whether there was value for money for the public purse in letting go assets as such low prices.

General experiences of Right to Buy since April 2012

There was a wide range of experiences reported. In terms of trends and summaries, the following were the majority views.

There is a difference between authorities in London and the South East (on the one hand) and the northern and midlands authorities (on the other).

The former authorities are noting a reduction or tailing off of sales following a peak in 2015.16 affected by what was generally felt to be two drivers: 1) values have risen faster than discounts making purchase relatively more expensive and 2) the notion that there was a cohort of potential aspiring purchasers that were "log-jammed" prior to 2012 and it took a few years for this pent-up demand to wash through the application process. Two authorities in this group also felt that the actions that had taken to assess applications and confirm proper eligibility etc had also had an impact on dampening demand. A small number of authorities in this group felt that if it was desired to continue sales at higher volumes in order to generate receipts necessary to finance existing development programmes (and not leave them delayed or un-financed), that discounts would need to be increased; this is not to say that these authorities were in favour of such a move, rather than this describes a simple funding view. The overwhelming majority of sales are at, or very close to, maximum discount.

Conversely, most of the northern and midlands authorities were seeing sales volumes continue to rise with discount levels driving down sales values, particularly for flats. There was widespread frustration that this felt like the sale of an asset at such an under-value as to render the receipt next to meaningless in terms of provision of new supply, with all the attendant issues around management, lettings, stock availability etc.

Views on discount levels

As above, there tended to be separate London/South and Midlands/North responses to the points raised around discount levels.

Southern and London authorities felt that the high level of discounts had led to high volumes of sales but that rising values were beginning to lead to reductions in volumes. It was noted in many cases that the reduction in volumes was being sustained towards the end of 2017.18 and is likely to continue. In response to a question raised around setting discount levels locally, all authorities felt that they would wish to reduce discounts save for exceptional circumstances when a specific sale might want to be encouraged - this might be for example where there is one tenanted flat remaining in a block of flats. However, there was a strong feeling that the level of discounts in itself was having less of an impact of sales rates, with the underlying increase in values acting to reduce demand.

Whilst there was some feeling that the reduction in receipts might cause an issue in terms of financing capital and development programmes, this was acknowledged to be a temporary financing issue and one that did not generally outweigh the benefit of retaining more properties as tenanted in the first place.

For the midlands and northern authorities, the level of discounts cause a problem around low sales values and the inability to replace anywhere near on a one for one basis. Responses to the question around locally setting discount rates were therefore much more likely to be positive - the points were twofold: that reducing discounts was fairer in general in the market place, as this might prevent sales at significant under-value; and that more much-needed rented stock would be retained. It was noted that overall values would have to be very different in order to facilitate one for one replacement, however any increase in net receipt was felt to be welcome in funding future programmes.

In general therefore, there was a cautiously positive response to the notion that local authorities should be able to set discount rates locally.

Views on applicants

Every single respondent expressed a degree of frustration that some, and in some cases many, applicants were not likely to be the households that would be resident in the sold homes for very long. The predominant reasons quoted were:

- Family members assisting purchase by an elderly relative - so that the home passes into their ownership in due course.
- Tenants coming under pressure to purchase from funding/loan companies, which would then look to acquire ownership from the resident (perhaps through the operation of onerous financing-terms meaning that residents would be unable to keep up with payments).
- Applications from recipients of housing benefits.

Whilst these examples were most often quoted in a London/Southern context, there was some such evidence quoted by all authorities across the country.

A majority of authorities had implemented more stringent application processes, which has included in most cases site visits to confirm occupancy and conducting interviews to ensure that applications are bona fide. In around half of the authorities, fraud teams had been alerted, and the other authorities felt that they would (or should) take such action.

In two cases, more details of the financial means and source of funding had been requested as part of the application process along with a request for tax and other details - and this has had the effect of many applications being withdrawn as potential fraudulent applications are deterred.

Retention Agreement issues

The majority of the discussions was focused on the operation of the Retention Agreements and the potential changes that had been suggested.

One authority has not entered a 141 agreement as the forecast sales in the HRA self-financing settlement mean that there are few if any 141 receipts. It was noted that this authority was one of around half a dozen that either had not entered an agreement or where few if any 141 receipts had arisen. This authority disclosed that they were considering applying for an Agreement given that the progress of sales and receipts since 2015 meant that there was the potential for 141 receipts to be available if sales were sustained at current rates.

Payment of receipts?

In summary, most of the other authorities had been able to sustain 141 agreements without paying any monies to Government but many reported that there are increasing pressures which might mean that money could be paid over in the near future without changes to the rules.

There was absolutely no appetite for authorities to pay receipts to government for redistribution to other programmes - even if there was the opportunity for reinvestment via Homes England locally. Fundamentally, local authorities regard their receipts as "theirs" and resist the suggestion that any unspent receipts are being "returned" to government.

In four cases, monies had been paid over to Government, in one case this was a result of the application of the quarterly-mechanism (i.e. no monies would have needed to be returned if the receipts/investment had been reckoned on an annual basis).

For the majority of authorities, there was a general sense that the period was approaching when there was a risk of having to pay over significantly increased level of receipts to government. It is becoming increasingly difficult to find programmes, given the restrictions on what can be invested in. It is possible to capture this in the following summary: if the operation of the agreements are not made more flexible, there is a very great risk that authorities will not be able to generate sufficient development programmes to use the receipts. This would then carry the risk either that monies would be paid to government in much larger amounts, or that acquisition programmes would be required in greater measure, or most likely both.

On this latter point, acquisitions and the buy-back of former RTB properties had been a feature for a small majority of the authorities. This had been principally driven by the need to avoid an otherwise impending payment over of receipts to government. Whilst this approach does add to the quantum of affordable housing stock (or at least reduces the net loss), in particular if poor quality or empty homes are brought into more effective use, and does give the opportunity to better match local need with supply, most acknowledged that it would be better if receipts were able to be deployed more flexibly to new developments.

It is worth highlighting, however, that a programme of buy-backs should not be considered an inappropriate use of RTB receipts; for three of the authorities, re-purchase of poor quality stock for refurbishment and better use/match with needs is a necessary and required programme in terms of maintaining and improving housing conditions in the area. These councils were robust in defending their right to be able to use RTB receipts in this way.

3 year timeframe for reinvestment

The rule which states that there is only 3 years in which to reinvest receipts, calculated on a quarter-by-quarter basis was reported universally as an issue for authorities.

Most felt that 5 years was a more realistic timeframe and many pointed to recent research by the Home Builders Federation that identified the average period from grant of planning to practical completion across all sites is 3.25 years.

In addition to the overall 3-year timeframe, a number of authorities reported specific problems with the process by which the receipts/payments are reckoned on a quarterly basis. This process is linked to quarterly sales 3 years ago and therefore at risk from "spikes" or "troughs" in sales activities long before the delivery of a development programme in the present day. None of the authorities contacted could offer an explanation as to why this aspect of the Agreements had been introduced as the cashflow impact for government would be slight (at the most). The general response to this issue was to seek short-term acquisitions in order to use receipts - which was acknowledged as not ideal.

All authorities expressed frustration that the process of development is subject to risks and delays which are simply not acknowledged within the 141 Agreement process. One response might be to allow dialogue between authorities and government around specific issues, although most felt that this would be potentially unwieldy for government. The consensus therefore was that a move to extend the timeframe across the board would offer the flexibility required.

Finding land and sites

Almost all authorities reported that their “Easy Win” programmes are running out as land and other resources are used up within the HRA. Typical was the sense that infill sites and garage sites are being utilised and that there might therefore need to be a significant change to the basis for the programme in order to enable longer term reinvestment to be sustained, including moving into the market to acquire land.

This was not a universal issue - as a small number of the authorities engaged did have sufficient land upon which to sustain new development programmes for some time. However, the issue was raised by sufficient numbers for this to be highlighted as an issue nationally which might affect replacement and supply rates.

The main conclusions from this element of the discussions were to suggest that there might be more flexibility around the use of RTB receipts earlier within the development cycle, perhaps to allow the acquisition of land directly, and not relying on a need for matching resources (for example, a site purchase wholly funded by receipts followed by funding for the programme which ended up at 30:70). Authorities acknowledged the risk to government that the land might not be brought forward for development and that a clawback mechanism might be appropriate. However, this was a subset of a general view that authorities should be allowed to act flexibly in bringing forward non-owned sites for development utilising RTB receipts as a key resource.

Matching funding with the receipts as 30% (the 30/70 issue)

As might be expected, responses on this issue varied in the sense that the 30:70 funding mix works for some authorities and not for others. Those others reported that a move to 40:60 and 50:50 would allow for more flexibility in the application of the receipts, particularly if this was able to vary between years, or the 30% element was able to be input up-front.

It is important to highlight that there were two principal reasons why the 30:70 mix might not work at the individual authority level.

The first of these is the operation of the HRA debt cap: this was the biggest factor affecting the consideration of a move away from 30:70. Put another way, the response to the question "would 30:70 work if borrowing was not artificially constrained by the cap" was generally positive.

The second of these is the sustainability of borrowing 70% of build/development cost in the context of the overall viability of the business plan. Three authorities reported that a move away from 30:70 was likely to be necessary in viability terms as the costs of development were increasing compared to the level of rents (net of costs). This is an important point to emphasise when reviewing policy in this area as the underlying "30% grant assumption equivalent" does not universally work from a viability perspective across the country. In many northern authorities in particular, net rent levels may not be sufficient to sustain 70% borrowing for build costs in an acceptable payback period. However, the issue was felt to apply also in London and southern authorities if land values needed to be included in development costs.

The main response to this part of the discussion therefore was that there should be flexibility to allow bidding for grant alongside the deployment of RTB receipts and borrowing.

Regeneration investment

A number of authorities made the point very strongly that calculations of additionality around property numbers should take account of the obsolescence of existing stock, and that newly built homes should not have demolished homes "netted off" if it was clearly the case that the demolished homes were unable to be brought back into use.

Most felt that while they could understand why the government might have included this element of the rules within the Agreement, this was actively inhibiting the delivery of much-needed regeneration and redevelopment programmes.

Types of affordable housing

There was unanimity on the point that 141 receipts should be able to be utilised for a full range of affordable housing products in line with those supported by Homes England programmes (shared ownership, rent to buy, affordable rent, living rent etc). The restriction to HRA "products" was felt to be anachronistic, counter to government policy around increasing affordable housing supply and inconsistent with the new National Planning Framework (and 2017 White Paper definitions of Affordable housing).

However, not all authorities said that they would immediately consider changing from re-provision of social rent in the HRA, as this is always a local priority.

The ability to invest in other forms of affordable housing tenures might enhance value for money making supply go further for a given level of receipts.

Investment into companies

Several authorities have subsidiary companies and/or Arms Length Management Organisations (ALMOs) in place to supplement the delivery of affordable housing in their area.

Many authorities therefore highlighted that it would be helpful to be able to deploy 141 receipts into these companies - this might offer increased value for money in terms of the type and nature of affordable housing that the receipts can be used for (for example at intermediate rent levels, the level of receipt matching might be lower than 30%).

This might also act to avoid some of the complex structures now actively being considered by authorities in order to ensure that receipts are reinvested locally - in one case, an authority was considering a joint venture structure between partners in which it had a 50% stake specifically in order to be able to deploy 141 receipts, when it was likely to have been better value for money to have invested these into a wholly-owned subsidiary.

Investment with local Registered Providers

One authority has in the past offered the use of receipts as a grant equivalent for local Registered Providers (RPs) to bid for and that has proved successful in a limited way. That authority has now moved on to direct re-provision in the HRA.

Generally, however, authorities reported that engagements with local RPs to take up allocations have generally led to low interest - this was felt to be because locally-based RPs with limited development programmes may not have the appetite, capacity or land/opportunities to partake in such a programme. In fact many small-medium RPs are moving away from small-sized, s106 scheme acquisitions in favour of larger land-based programmes - and this experience was recognised at many authorities.

Top three things that would change in order to make more sustainable

Whilst the summary below is not intended to be scientific, the table sets out a summation of the responses to the question: what would be the top three things you would change? It should be noted that some issues were always issues (the 3 year timeframe for example, although this was not in the top 3 for all authorities). This is felt to be a reasonable proxy for the nature and importance of each of these issues as they affect authorities, and chime closely with the overall findings of this research.

Area/flexibility	Number *
3 year timeframe should be a minimum of 5 years	8
More flexibility over the 30:70 matching // extension of debt cap	6
Investment of receipts into a wider range of affordable tenures	6
Investment of receipts into companies/subsidiaries/ALMOs	3
Ability to apply discounts locally	3
Ability to invest receipts alongside grant	2
Other issues	5 **

** Note one authority had not entered a 141 agreement - hence total responses 33 from 11 authorities*

** For completeness, the five additional areas identified individually to be top priorities by individual authorities were:

- Making sure that eligibility of households is able to be tightened through the application process
- Ability to invest receipts into urgent refurbishment (e.g. fire safety)
- A Right to Buy holiday to allow replacement provision to "catch up" with homes lost to social rent
- Predictability around future rent policy
- Extension of the Cost Floor to include more items (land value) and for a longer period.