

31 January 2017

## Submission:

# Budget 2017

## Powering the Modern Industrial Strategy

### Summary of key points:

Housing associations are ready and able to play their part in helping to deliver a modern industrial strategy that builds a stronger economy and fairer society. This submission sets out three key areas of that strategy that housing associations are well placed to actively support and that measures in the Budget could power:

- **Cultivating world-leading sectors - foster greater innovation, responsiveness and impact by giving housing associations rent freedom**
  - Remove the biggest regulatory burden hampering the sector – government control over housing association rents
- **Upgrading infrastructure – class housing as infrastructure and release land for housing associations to build**
  - Include housing in the remit of the National Infrastructure Commission
  - Ensure land is locally coordinated, fairly sold and designated for housing in advance
- **Driving growth across the whole country – a renewed focus on regeneration that frees up housing associations to do more**
  - Put regeneration at the heart of the modern industrial strategy
  - Take a flexible approach to government investment that supports regeneration

To support this housing associations match £6 of private investment for every £1 of public money, offer flexibility in the way they use their existing resources and guarantee that all profits are reinvested in homes and communities. They look forward to working in partnership with the Government to help build a country that works for everyone.

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## 1. Introduction

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The Budget takes place a matter of weeks before Britain begins the formal process of leaving the European Union. As the Prime Minister has rightly argued this moment of national change is about far more than our relationship with the EU. It provides a once-in-a-generation opportunity to build a stronger economy and a fairer society by embracing economic and social reform. Housing associations are ready to play their part in this modern industrial strategy, working to ensure that everyone in the country can live in a quality home that they can afford.

Housing associations have a one hundred and fifty year track record of tackling the daily injustices that hold people back. Last year they built 40,000 new homes, boosting growth to support our overall prosperity. But more than that, they are rooted in communities across the nation, working to ensure that prosperity is shared by people in every corner of our country.

The housing measures announced in the Autumn Statement will make a real difference in their efforts to deliver on that ambition. Additional investment and greater flexibility over how it is spent will allow housing associations to develop even more homes across the country. The sector wants to build on that and looks forward to working with the Government on its modern industrial strategy. This submission sets out three key areas of that strategy that housing associations are well placed to actively support and that measures in the Budget could power:

**1. Cultivating world-leading sectors – foster greater innovation, responsiveness and impact by giving housing associations rent freedom.** The Government has set an ‘open door’ challenge to sectors to come up with transformational proposals. One measure that would transform housing associations’ ability to deliver for their communities is rent freedom. Removing government control over the sector’s rents would allow housing associations to offer the best deal to their customers, use their assets more effectively and better meet the needs of the communities they serve.

**2. Upgrading infrastructure – class housing as infrastructure and release land for housing associations to build.** We were delighted that the Government put housing front and centre of the Autumn Statement. Additional investment and greater flexibility is already making a difference. The Budget provides an opportunity to build on these measures and make housing a key part of its modern industrial strategy. By classifying housing as infrastructure and making better use of public land, government could better join up housing and infrastructure and support housing associations to further ramp up supply.

**3. Driving growth across the whole country – a renewed focus on regeneration that frees up housing associations to do more.** The Prime Minister has argued that the central challenge of our time is to bring our country together by ensuring everyone can share in the nation’s prosperity. To achieve this the Government should put regeneration at the heart of its modern industrial strategy and change the way it invests in these schemes to free up housing associations to do more.

As we begin the process of leaving the European Union, the task of building a country that works for everyone has become ever more urgent. The Budget provides an opportunity to drive this forward by powering the Prime Minister’s modern industrial strategy. Housing associations are ready and able to play their part and look forward to working with the Government to build a stronger economy and fairer society.

## **1. Cultivating world-leading sectors – foster greater innovation, responsiveness and impact by giving housing associations rent freedom.**

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As part of its modern industrial strategy, the Government challenged sectors to come to it with transformational proposals. One measure that would transform housing associations' ability to deliver for the communities they serve is rent freedom. Now is the time to remove the most significant regulatory burden that hampers the sector's ability to make best use their assets, innovate and respond to the needs of their communities – government control over housing association rents.

### **The case for rent freedom**

Housing associations want to offer the best deal to their customers and use their assets as effectively as possible. The sector's ability to do that is currently limited by government control over their rents, fixing them at either a percentage of the average local private rent or at the lower social rent level. Due to the fact that private rents vary hugely around the country and do not rise and fall in proportion to wages, their homes are less affordable for customers in some places than others. In addition, housing association boards' ability to make long-term strategic decisions about the future of their businesses is constrained by the fact that they do not control their core source of income.

Strong investor confidence in the sector is central to their vision for the future, and this has been significantly shaken by the current uncertainty around rents. The 10 year rent settlement agreed with the Government and implemented in 2015 provided certainty to associations and investors. However, the decision by the Government to unilaterally remove it injected significant uncertainty into housing association business plans and lenders' risk appraisal of the sector. The lack of clarity regarding the rent regime post-2020 is therefore having a dampening effect on sector and lender confidence, and therefore its ability to take on risk and boost supply.

The Budget provides an opportunity to offer the sector and lenders the certainty they need. However, rather than going back to the bureaucratic system of the past, the Government should deliver a new approach to rents, providing rent freedom to housing associations. Having the freedom to set their own rents would allow housing associations to better meet the needs of the communities they serve, by providing genuinely affordable rents and increasing the number of new homes they build.

### **How it would work**

Housing associations want to be able to reflect local market conditions and customer circumstances in their rents. Rent freedom would allow them to develop rent policies appropriate to the local housing market, the local labour market, and household profile locally. In keeping with the sector's social mission housing associations would look to balance tenant affordability with strategic delivery, thus ensuring rents do not entrench welfare dependency or poverty but also continue to support the development of new affordable housing.

To make the most of this freedom, associations could work with local authorities to tailor local allocations agreements to ensure each customer gets a home that suits their needs. All of this would be backed up by clear, transparent, published rent policies agreed by boards.

### **The impact of rent freedom**

The National Housing Federation has conducted preliminary analysis to explore the additional capacity that could be generated if housing associations had freedom to set their own rents. As a starting point this analysis was based upon two principles: that rent freedom will not increase the Housing Benefit bill and that rents will be fair and affordable for tenants. In the example below, we have modelled the impact of a one-off readjustment of rents for higher income tenants. This is for illustrative purposes only, to demonstrate the options that become available when a centralised and rigid rent structure is reformed.

The analysis shows that a small weekly rent increase (£10) for higher income households (household income over £40,000) could generate nearly £96m extra rental income annually, nationwide. There are a number of possible uses for this additional resource – including using it to support additional new supply or to lower rents for those households on the lowest incomes.

For example, over a five-year period this additional income would stand at nearly £480m and could therefore support the delivery of over 3,200 homes nationally without any public subsidy. Alternatively, it would be possible to lower rents for households with incomes of less than £10,000 per year by £7.50 per week and still maintain the overall national rent roll. This would represent a saving to the taxpayer as it would reduce the Housing Benefit bill, and would also increase the overall affordability of the property – reducing welfare dependency and increasing work incentives.

This initial analysis is indicative only and will be expanded upon and refined as we consult with our membership on the future of rents. However, it is helpful in demonstrating some of the possibilities that could be created by putting housing associations in charge of their rents and asking them to innovate in order to deliver best value for their customers and the taxpayer.

The importance of rental income to housing association business plans cannot be overstated. Not only must rent cover day-to-day management and repairs, it must also provide a stable long term income stream against which private finance can be leveraged. Rent uncertainty can therefore have far-reaching consequences on business plan assumptions, development capacity and risk appetite. Housing associations tend to model 30-35 year forecasts to reflect the usual repayment term for sub-market rented housing and the long-term debt used to fund development. If it is unclear how rents will be determined in the short to medium term, it becomes prudent to use very conservative assumptions in these longer-term forecasts, and thus development plans must be adjusted accordingly.

#### **Case study 1 – North Star Housing Group, North East**

Rent freedom would free up capacity to build more homes. Certainty of income is critical to future lending and the extent of the risks we are prepared/able to take. It is also critical when negotiating with institutional lenders about building for rent as they clearly want certainty of return. We are in discussion with a pension fund about building in the Tees Valley devolution area, and there is an orderly queue forming of other investors wanting to get involved because of the land availability. Uncertainty around rents and future increases is a major barrier.

The more certainty we get, the more risks we will take, and sweat our assets even further than we currently are. We would also be more relaxed about deals with institutional lenders. It is simply not in our interests to make rents unaffordable in areas of steady demand where private landlords compete with us. We are fundamentally a charitable housing association with a strong commitment to ensure affordability and strong governance overseeing this. It is a low wage, low rent economy across Tees Valley which will be fundamental to rent policy.

### **Case study 2 – L&Q, London and South East**

The rents L&Q can charge have a dramatic impact on our business plan viability and, by extension, the ability to invest and take long-term risk. Current rent policy hampers long-term decision making on investment as our key revenue stream is not guaranteed or fully predictable. Rent flexibility would enable L&Q to make more informed decisions, decreasing risk and enabling a greater long term investment into affordable housing.

Our secure rental stream supports borrowing for new development. Through this mechanism L&Q converts rents into additional building, with uncertainties or fluctuations in rental income impacting upon development capacity. For example, at a top level, the difference between a rental increase of CPI and CPI + 1% creates sufficient capacity for L&Q to potentially deliver an additional 1,500 units over a decade, on top of existing commitments.

The balance between rents and capacity is about finding the point of developing as many units as possible whilst maintaining the affordability of such units for residents. Currently our rents are a patchwork derived from the funding and local market conditions when the units were first developed. The current system is riven with inconsistencies, inefficiency, complexity, and unfairness. With greater flexibility L&Q could rationalise rents to make them fairer across the areas we work in, bringing homes more appropriately in line with current conditions and customer circumstances.

A number of organisations have done interesting work already in this area, providing a useful basis for future policy development. Prominent examples include the personalised rent model developed by Dolphin Living on the New Era Estate in Hackney, a new Living Rent product proposed by Savills in conjunction with the Joseph Rowntree Federation (JRF) and the National Housing Federation, and the London Mayor's desire to implement a London Living Rent. These models share an explicit link between income and housing costs, something which is not possible under the existing rent regime for housing associations.

### **Case study 3 – Dolphin Living, New Era Estate, London**

Tenancies on the New Era Estate are not subject to the Regulator's Rent Standard. This has allowed Dolphin Living to develop a Personalised Rent model which balances tenant affordability with overall scheme viability. The Personalised Rent is based on the household's net income and the latest JRF Minimum Income Standard (MIS). By deducting the MIS from net income it is possible to identify the household's residual income and therefore their relative ability to pay. In this way it is possible to set rents which are fair because they are tailored to the individual household's circumstances, and affordable because they directly relate to earnings and more general living standards.

In the future, housing associations free to set their own rents, could maximise their economic and social impact by offering genuinely affordable rents to households on a range of incomes.

## **2. Upgrading infrastructure – class housing and infrastructure and release land for housing associations to build**

We were delighted to see the housing announcements in the Autumn Statement. Additional investment and greater flexibility over how it is spent will support housing associations to build more homes across the country. The Budget provides an opportunity to build on these important measures. By classifying housing as infrastructure and making better use of public land, the Government could better join up housing and infrastructure and further support housing associations in their ambition to significantly ramp up supply.

## **Housing as infrastructure**

The launch of the Housing Infrastructure Fund at the Autumn Statement, as well as the connection the National Infrastructure Commission made between the supply of new homes and the infrastructure needed to support them, offered welcome recognition of the link between housing and infrastructure. However, there is scope for the National Infrastructure Commission to go further and explicitly include housing in its remit.

The National Infrastructure Assessment should be used to set the agenda for large-scale housing developments across the country, allowing local authorities to opt in to the Nationally Significant Infrastructure Project process. Allowing proposals for large-scale housing developments of 1,500 homes or more to be assessed through this route would offer greater certainty around the timescales for decision-making – leading to more new homes being built more quickly.

A key barrier to delivering large-scale housing developments is the complexity and uncertainty of the planning system. Research by planning consultancy Nathaniel Lichfield Partners shows that, on average, it takes some 73 months for developments proposing 2,000 new homes or more to receive planning approval. Alongside this there are difficulties associated with local opposition, local authority capacity and high costs and uncertainty.

The Nationally Significant Infrastructure Project route offers a smoother and speedier process for approving major development. Allowing local authorities to ‘opt in’ to this process for large-scale housing development would result in quicker decision-making, with housebuilding starting more quickly. The Planning Inspectorate estimates the process would be complete within 15 months – saving 58 months (or almost 5 years) compared to the planning permission route. These timeframes don’t include the time needed for public consultation, but the Nationally Significant Infrastructure Project also offers more meaningful engagement with communities. Public consultation takes place before the application is made, with the Planning Inspectorate expecting communities’ feedback to be taken on board before the application is finalised. These factors combine to provide developers, housing associations and funders with more certainty, making large-scale housing development more attractive and deliverable.

## **Land and planning**

A more certain supply of land, at the right price, would support housing associations to further ramp up the number of new homes they are able to build. The availability and affordability of land continues to be the biggest constraint on increasing house building. If land were locally coordinated, fairly sold and designated for housing in advance, housing associations could deliver even more affordable homes and make the best use of public assets. The following five interventions would deliver on that ambition.

### **1. Local control of public land**

Local authorities are best placed to understand and plan for the needs of their communities, but they struggle to identify enough land for housing because ownership and control over public land is fragmented. It is not always clear where ownership of land sits, and land is not disposed of in a strategic way to make the most of its capacity for housing and infrastructure. Local authorities, or groups of local authorities, should be given the power and incentives to identify, map and assess the potential of all public land in their areas and design a coordinated strategy

for its release. This should look not only at housing, but also at supporting infrastructure, public services and economic growth. A way of delivering this in the future could be through the emerging Combined Authority's Land Commissions, coupled with their spatial planning powers.

## **2. A fair price for public land**

The Government should encourage public bodies to sell their land at a fair price, taking into account the wider social, economic and environmental value as well as the cash received. It should update Treasury guidance on 'best value' to reflect this, ensuring that competition for land focusses on who can deliver the highest quality for an agreed price, rather than focussing on cash value alone. The local and national contribution to the economy of housing and housing associations is clear. For every pound invested in affordable housing, a further £1.42 is generated in the UK economy; one of the highest multiplier effects of any industry. It is vital that public bodies take these longer-term benefits into account when pricing and selling land.

## **3. Effective use of local plans**

The recommendations of the Local Plans Expert Group, which reported in March this year, highlighted that planning for housing was a key barrier to plan progression. The Government should prioritise the implementation of these recommendations, particularly the single standard methodology for assessing local housing need, and that it should be a clear, objective calculation. Linked to this, it is also vital that once objectively assessed need is determined, a five-year land supply is also identified that is updated regularly. This will provide certainty to all involved in the development process.

## **4. Making the most of Permission in Principle**

The Housing and Planning Act established a new Permission in Principle which allows local authorities to designate land for housing. It also allows for developers to apply directly for Permission in Principle. We believe that local authorities should be incentivised to proactively designate areas with Permission in Principle, which should include setting out expectations on number of units, density, affordable housing requirements, community and social infrastructure and other permitted uses. Clarity and certainty over these aspects of development expectations would send clear signals to the market over land values and speed up planning decisions.

## **5. A standardised approach to demonstrating viability**

In the 2015 Comprehensive Spending Review, the Government announced proposals to bring forward a more standardised approach to viability assessments, but this has not yet been taken forward. A standardised process would assist in speeding up negotiations, providing a level playing field for all involved in the development process, and avoiding overbidding for land. This additional certainty and transparency in the system would bring about more planning permissions for new homes, allowing housing associations to further deliver on their ambition to significantly increase supply.

Together, these changes would lower the cost of land, improve planning certainty and allow housing associations to further deliver on their ambition to significantly increase the number of new homes they build.



### **3. Driving growth across the whole country – a renewed focus on regeneration that frees up housing associations to do more**

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The vote to leave the European Union highlighted just how divided we have become as a nation. We need to bring our country back together and the Prime Minister is right to argue that this requires a modern industrial strategy that ensures everyone can share in Britain's prosperity. This hasn't been the case for some time. Economic imbalances between different parts of the country are larger than other countries, with incomes and living standards lagging behind in too many parts of the nation. These disparities hold back the country's growth and limit opportunities for too many people.

Housing associations are rooted in communities in every part of the country and want to explore with the Government how they can help put regeneration at the heart of its modern industrial strategy. Now is the time to begin a national conversation about how we, as a nation, can renew our focus on regeneration. That means ensuring that everyone has the opportunity to improve their life and that of their family by having access to a decent job, a good education and a quality home. To deliver on this housing associations want to work with the Government on a major national summit that brings together leaders from business, education and housing to discuss how we transform communities that have felt left behind for far too long.

#### **Flexible approach to government investment**

In the meantime, there is a change to the way government invests that could free up housing associations to deliver more in this area. The Homes and Communities Agency currently administers a raft of interventions - providing capital grant, equity investment, soft loans and debt guarantees - each seeking to address a specific housing issue or incentivise a particular course of action. Alongside this, there are different funding streams that can support regeneration through infrastructure, land remediation, improving existing homes, and employment and skills initiatives available at the local, national and European level. This has led to a highly fragmented approach, which both limits the effectiveness of funding and dilutes the economies of scale that can be achieved.

For more effective investment in housing, existing funding streams should be consolidated into a single fund to deliver strategic housing outcomes, set at a national and local level. This would allow housing associations to target existing funding at regenerating areas that have felt left behind for far too long.

### **4. Conclusion**

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In a matter of weeks Britain will begin the formal process of leaving the European Union. This Budget provides the opportunity to take advantage of this moment of national change to power a modern industrial strategy that delivers real economic and social reform.

Housing associations have a one hundred and fifty year track record of not only increasing overall prosperity but also in ensuring that this is shared by people in every corner of the nation. They look forward to working in partnership with the Government to build more affordable homes, lead regeneration in communities that have felt left behind, and drive growth across the whole country.