House of Commons
Committee of Public Accounts

Financial viability of the social housing sector: introducing the Affordable Homes Programme

Thirteenth Report of Session 2012–13

Report, together with formal minutes, oral and written evidence

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The Committee Name

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Committee staff

The current staff of the Committee is Adrian Jenner (Clerk), Sonia Draper (Senior Committee Assistant), Ian Blair and James McQuade (Committee Assistants) and Alex Paterson (Media Officer).

Contacts

All correspondence should be addressed to the Clerk, Committee of Public Accounts, House of Commons, 7 Millbank, London SW1P 3JA. The telephone number for general enquiries is 020 7219 5708; the Committee's email address is pubaccom@parliament.uk

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Summary

In December 2010, the government announced the Affordable Homes Programme (the Programme), under which there is £1.8 billion capital funding in government grants to social housing providers. The Department for Communities and Local Government (the Department) has overall responsibility for the Programme, which is delivered by the Homes and Communities Agency (the Agency) through contracts with housing providers.

The Department expects the Programme to support the provision of approximately 80,000 homes in the four years from April 2011 to March 2015. The Agency secured commitments from providers to build 24,000 more homes than its initial target of 56,000. Through negotiation the Agency reduced the average grant per home to £20,000; a third of that under the previous programme. At the time of our hearing in July 2012, construction had started on 13,800 homes.

It is not yet clear whether the Programme will deliver better value for money in the long term. The reduction in the grant paid to providers for each home will be funded in part by housing providers being able to charge higher rents to tenants, leading to an estimated £1.4 billion increase in housing benefit payments over 30 years. The Programme therefore shifts cost from one department to another.

The Department needs to do more work to understand the impact of the Programme on tenants and its interaction with wider welfare reforms. On the one hand more of the new housing, both for rent and for sale, may be taken up by people on higher incomes so that the programme fails to meet the most pressing housing need. At the same time, the poorest tenants may be unable to afford the higher rents. Those who receive higher benefits may in turn find it even harder to find employment that pays enough and so there will be more people who are more likely to be locked into benefit dependency. We are also concerned that the allocation of funding does not fully target people and areas of greatest need.

Delivery of the new homes is heavily skewed towards the end of the Programme, with many due to be built in the final year on sites which are not yet confirmed, or have not received planning permission. This leaves very little room for slippage. The Agency will need to maintain a tight grip on progress and act promptly to address any delay if the Programme is to deliver all that is promised.

The Programme has taken advantage of housing providers' current ability to borrow and so finance a greater proportion of the cost of building social housing themselves. This has been based on balance sheets strengthened by the rise in property values. However, this is a one-off opportunity and it is far from clear whether providers will have the financial capacity to take part in another round of the Programme after 2015. The Department will need to give the sector more certainty about its future plans as soon as possible. We welcome the prospect of 80,000 new homes, but with 4.5 million people waiting to be allocated an affordable home in England, it will not solve the shortage of social housing

alone, and wider action is needed.

On the basis of a Report by the Comptroller and Auditor General,[1] we took evidence from the Department for Communities and Local Government and the Homes and Communities Agency on the financial viability of the social housing sector and the Affordable Homes Programme.

1 C&AG's Report, *Financial viability of the social housing sector: introducing the Affordable Homes Programme*, Session 2010-12, HC 465

Conclusions and recommendations

1. **The Department has not done enough to understand the full impact of higher rent levels on tenants.** Housing providers can charge higher rents than before (on average 65% of market rents in London and up to 80% elsewhere). This will affect tenants' ability to afford the new housing and may exclude some of the poorest from accessing this new housing. Where higher rents are paid through increased housing benefit, tenants may find themselves caught in an even stronger benefit trap where it has become even harder to find sufficiently well paid employment to make working worthwhile, countering the Government's objective of ensuring that the benefit system makes work pay. However, the Department does not hold information on the rent levels being charged for individual properties and it has not considered the impact on tenants or prospective tenants of these rent levels or the interaction with wider Housing Benefit reforms. The Department should consult tenants and providers to understand the impact of the higher rent levels on tenants, and commission research into the financial and other characteristics of those tenants living in 'affordable rent' homes and build the results into future programmes.

2. **The allocation of funds under the Programme did not fully focus on the areas of greatest need.** The Agency allocated funds across regions, and the level of grant per home was the main factor behind its decisions on which housing providers' bids were successful. It was not clear to us whether and how funds were targeted at specific areas of greatest housing need. We are also concerned that people in the greatest need may not benefit—higher rent levels may mean that new social housing ends up with the 'richest of the poor' and we are aware of areas where larger properties in London have gone to couples instead of families. The Department and the Agency should ensure that decisions to allocate resources in future social housing programmes prioritise areas of greatest need and target families in greatest need.

3. **It is unclear whether the shift of public resources from capital grants to increased housing benefits will provide better value for the taxpayer.** The Programme will be delivered with an average government grant per home of around £20,000, compared to £60,000 under previous housing programmes. In part this will be funded by a one-off use of capital surpluses held by housing associations. In part it will be funded by providers charging higher rents to tenants, two thirds of whom are supported by housing benefit, with a consequential increase in the housing benefit bill of an estimated £1.4 billion. To inform decisions on future housing programmes, the Department should review whether and how the current mix of revenue and capital funding provides best value for money for the taxpayer and tenants over time and take the results into account in future programmes.

4. **The Programme has a risky delivery profile with little room for slippage.** Half of the new homes expected to be built are planned for the final year of the Programme, and half do not yet have confirmed sites or planning permission. If providers fail to make agreed progress, the Agency will need to reallocate funding to others. The Agency should monitor providers' progress closely, and, in particular, when funds

are re-allocated, ensure that replacement schemes still meet the specific housing needs previously identified.

5. **The Programme has taken advantage of the sector's current financial capacity but this may be a one-off opportunity.** With the rise in the value of property in the preceding 10 years, housing providers have strengthened their balance sheets and were able to use their surpluses and borrowing, as well as other sources, to provide around £10 billion of funding alongside government's contribution. Whether or not this approach is repeatable will depend on the future financial health of the sector and its ability to continue to borrow on the scale required, which will in turn depend on factors such as interest rates and the strength of the housing market. To enable the sector to play its part in meeting the substantial unmet demand for social housing in the future, it needs clarity on the government's plans and the role it will be expected to play. The Agency should analyse the financial position of providers to assess whether the model can be repeated, providing more certainty to the sector on its intentions for social housing beyond 2015.

1 Delivering the Programme

1. In December 2010, the government announced a new programme to build affordable housing (defined by the Department as below market price) in England. The Affordable Homes Programme (the Programme) allocated £1.8 billion capital funding in government grants to social housing providers. The Department for Communities and Local Government (the Department) has overall responsibility for the Programme, which is delivered by the Homes and Communities Agency (the Agency) through contracts with housing providers.[2]

2. The Department expects the Programme to support the provision of approximately 80,000 homes in the four years from April 2011 to March 2015, less than 5% of the total number of families on local authority waiting lists in November 2011.[3] The Agency secured commitments from providers to build 24,000 more homes than its initial target of 56,000. At the time of our hearing in July 2012, the Agency told us that they are on track with work starting on 13,800 homes.[4]

3. Most of the Agency's work to date has been on appraising and selecting applications from housing providers. Through negotiation the Agency reduced the average grant per home to £20,000; a third of that under the previous programme.[5] Most notably, government funding in London has reduced from around £90,000 per home under the previous National Affordable Housing Programme, to around £26,000 per home under the current Programme.[6]

4. The delivery of new houses is skewed towards the end of the Programme, with more than half planned in the final year. The Agency told us they have revisited the timetable for planned completions and have brought forward the development of 6,500 new homes for areas outside of London.[7] There is also a provision to move funding allocations between providers if it looks likely that they will not be able to deliver on their commitments.[8]

5. In addition, in order to get the Programme moving, the Agency revised its payment structure. The Agency originally planned to pay providers 100% of agreed funding once the homes had been delivered. However, to encourage providers to start earlier, the Agency paid 75% of the grant to housing providers who started development by March 2012, with the remainder to be paid on completion.[9] The Agency told us it considers paying 25% on completion a sufficient incentive for providers to deliver on their commitments but they

2 C&AG report, paras 1-3

3 http://www.communities.gov.uk/documents/housing/xls/2039614.xls

4 Qq 87-89

5 C&AG report, para 2.20

6 Q 68

7 Q 126

8 Qq 125, 128

9 Qq 91, 126-127

plan to review how paying 75% of funding upfront will impact on the flexibility to move between sites or between providers.[10]

6. Some 51% of schemes are indicative, because sites have not been identified, projects are not sufficiently progressed, or do not yet have planning permission.[11] The Agency explained that having indicative sites is a symptom of the fact they invited housing providers to submit offers for the whole four-year Programme. The Agency plans to work closely with housing providers to firm up the schemes. Where a provider is not able to deliver indicative schemes, there is an opportunity within the Programme to move to alternative sites that are more certain.[12]

7. Under this Programme, providers are required to finance a greater proportion of the cost of the new homes themselves. The NAO report estimates that housing providers will spend some £12 billion on new homes, funded by a combination of the £1.8 billion government grant, £6 billion in borrowing and £4 billion from other sources.[13] Providers told us that they have used their surpluses, profits from selling stock and re-letting some properties, to borrow more.[14] They have also benefited from stronger balance sheets as a result of the rise in the value of their housing assets in the last ten years.[15] The Department told us that the sector has £11.6 billion in undrawn borrowing facilities.[16]

8. The Agency told us that as part of its application process, the Tenant Services Authority, (the then regulator) assessed whether housing providers were in a financially viable position. It told us that it looked at each of the associations that put forward a bid and identified a few where there were some concerns.[17] We queried how the assessment took into account changes to interest rates given that the current rates are so low.[18] The Agency told us that each housing provider has different arrangements for its borrowing and it was therefore not possible to identify a 'tipping point' at which a change in interest rates could impact on the financial viability of all providers. The Department also told us that due to the size of their portfolios, housing providers were able to secure preferential interest rates and are less affected by short-term movements.[19] Most of the borrowing for this Programme is on fixed rates and the Agency told us that, in its view, interest rates would not affect this Programme, but could affect housing associations overall.[20]

9. We asked about the sustainability of the Programme in the longer-term. Witnesses from housing providers raised concerns about whether they could continue to borrow at the

10 Qq 126-129

11 Q 125; C&AG report, para 2.25

12 Q 125

13 C&AG report, para 3

14 Qq 18, 94,

15 Qq 47, 82

16 Q 81

17 Q 74

18 Q 76

19 Qq 76-78

20 Q 80

same scale and therefore, if the model could be repeated.[21] The Department thought that there was still 'headroom' with capacity in the housing sector to do more. It admitted that it still had to make decisions on the size, scale and form of the Programme post 2015 as part of the next spending review.[22]

10. More broadly, there was acceptance from all the witnesses of the urgent need to find a way to fund the growing demand for social housing, given that 4.5 million people are still waiting to be allocated an affordable home in England. The sector cautioned that there needed to be serious attention given to where the subsidy for social housing will come from post 2015.[23]

21 Qq 3-4, 42-43

22 Q 94

23 Qq 15, 114

2 Impact of the Programme on tenants

11. The Programme will be delivered with less capital funding than previous housing programmes. This reduction will be partly funded by tenants paying more rent. Some two-thirds of social housing tenants are supported by housing benefit so this effectively shifts costs from the Department for Communities and Local Government to the Department for Work and Pensions. The housing benefit bill is expected to rise by £1.4 billion over 30 years as a result of the Programme.[24]

12. We debated the value for money case of shifting from a capital subsidy to a revenue-based subsidy. Witnesses from the sector told us that based on research and modelling, a capital subsidy appears more cost-effective if over a longer period (say eight or ten years). However, they acknowledged that this work needed to be updated and was dependent on a number of factors including: how long people are in receipt of benefit, what happens to the home when people move on and whether the homes being built should permanently be for people who will need support.[25]

13. Under the Programme, housing providers can increase their rent levels - up to 80% of market rent, though in London providers have committed to 65% on average. This equates to an average rent of approximately £182 per week in London, compared to a market rent of £280 a week in comparable properties.[26] The Department has done some work to analyse the costs of the Programme to all tenants, but this was not presented in the impact assessment for the Programme.[27] We were also surprised to hear that the Agency has not collected information on the rents that tenants will be expected to pay for individual properties, nor has it consulted with tenants to understand how they will be affected by increased rent levels.[28]

14. We asked witnesses whether the higher rent levels charged under the Programme could have a negative impact on those on lower incomes. In particular, we queried whether the homes being built under the Programme would be 'affordable' to the people in most acute need. Witnesses talked about a drift towards families with higher incomes who could afford the higher rents.[29] We heard that those on low income or out of work will have to earn more to be able to escape from being dependent on benefits.[30] Poorer tenants could find themselves unable to get employment that pays enough to cover the higher rent levels charged.[31] We are therefore concerned that the 'affordable' housing may end up benefiting those whose income is greater but whose need may be less.[32] The Department explained

24 Q 22; C&AG report, para 1.8, Figure 6

25 Qq 38, 43-46

26 Q 70

27 Q 137

28 Qq 111, 113, 116-117

29 Qq 31, 48

30 Q 48

31 Qq 107, 110

32 Q 115

that housing delivered through the Programme would still be cheaper than renting through the open market.[33]

15. This Programme addresses a small fraction (2%) of the unmet housing need in England and we were concerned about the way the planned homes were spread across the country. Rather than targeting specific areas in greatest need, the Programme funds were allocated based on a broad geographic spread.[34] When asked about how the housing need was defined, the Agency told us it considered a range of factors when assessing applications. It assessed the value for money of the bids, the grant rates and consulted with local authorities within Local Enterprise Partnership (LEP) areas.[35] The Department told us that the Programme was heavily weighted to the places of highest housing need with 23,000 homes (27%) planned within London.[36] Even within areas of need, we questioned whether the properties are going to the right-sized families. We are aware of cases where four bedrooms homes have gone to a couple with no children or a couple with one child. Witnesses told us that there was a drift towards people on higher incomes as they can most afford to buy, which seems to us to be against the spirit of an affordable homes programme.[37]

16. In some areas where rent is already low, the Programme may not be workable, because housing providers would have to charge above market rents in order to cover costs. The Department told us that all areas, even those that appear to have less need, received funding because they had specific housing needs which were not being met by the current housing stock.[38] The Department explained that the Programme included a range of property sizes and types with a third of the Programme made up of larger properties and around 9,500 homes offering supported accommodation to meet the needs of the elderly and those with special needs.[39]

17. There are wider welfare reforms that run alongside and will affect the Programme. One such change proposes that housing benefit will be paid directly to the tenant rather than to the housing provider. Our experience suggests that this may lead to difficulties, with providers not receiving the money they are owned in rental income on time.[40] The Department told us they have started running four demonstration projects to test how these changes will impact on rent arrears and speed of payment.[41]

33 Qq 107-108

34 Qq 95, 97, 121

35 Qq 98-100

36 Qq 104-105

37 Qq 31-33

38 Qq 121-124

39 Q 102

40 Q 131

41 Qq 131, 133-134

Formal Minutes

Monday 17 September 2012

Members present:

Rt Hon Margaret Hodge, in the Chair

Mr Richard Bacon
Jackie Doyle-Price
Chris Heaton-Harris
Meg Hiller
Mr Stewart Jackson
Fiona Mactaggart
Mr Austin Mitchell
Ian Swales
James Wharton

Draft Report (*Financial viability of the social housing sector: introducing the Affordable Homes Programme*), proposed by the Chair, brought up and read.

Ordered, That the draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 17 read and agreed to.

Conclusions and recommendations agreed to.

Summary agreed to.

Resolved, That the Report be the Thirteenth Report of the Committee to the House.

Ordered, That the Chair make the Report to the House.

Ordered, That embargoed copies of the Report be made available, in accordance with the provisions of Standing Order No. 134.

Written evidence was ordered to be reported to the House for printing with the Report (in addition to that ordered to be reported for publishing on 5 September 2012).

[Adjourned till Tuesday 18 September at 10.00 am

Witnesses

List of printed written evidence

List of Reports from the Committee during the current Parliament

The reference number of the Government's response to each Report is printed in brackets after the HC printing number.

Session 2012–13

Oral evidence

Taken before the Committee of Public Accounts

on Monday 9 July 2012

Members present:

Margaret Hodge (Chair)

Mr Richard Bacon
Stephen Barclay
Matthew Hancock
Chris Heaton-Harris
Meg Hillier
Mr Stewart Jackson
Austin Mitchell

Amyas Morse, Comptroller and Auditor General, National Audit Office, **Gabrielle Cohen**, Assistant Auditor General, NAO, **Chris Shapcott**, Director, NAO, and **Marius Gallaher**, Alternate Treasury Officer of Accounts, were in attendance.

REPORT BY THE COMPTROLLER AND AUDITOR GENERAL

Financial viability of the social housing sector: introducing the Affordable Homes Programme (HC 465)

Examination of Witnesses

Witnesses: **David Lunts**, Executive Director, Housing and Regeneration, Greater London Authority, **David Montague**, Group Chief Executive, L&Q, **David Orr**, Chief Executive, National Housing Association, and **Professor Christine Whitehead**, London School of Economics and Political Science, gave evidence.

Q1 Chair: Welcome. I thank you all very much for agreeing to be here. We have a rather big group of people here today, so if you can keep your answers to the point, we should be grateful. This initial section before we move to the accounting officers is for the Committee to get a handle on the key issues that we should be pursuing. You are more front-line to the impact of the programme, so hopefully you can give us some helpful insights into our lines of questioning. I will start with you, Christine, if I may. Looking at this programme in relation to your knowledge of everything else, what do you think are the key advantages and the key question marks that you have observed in the early stages of implementation?
Professor Whitehead: Obviously, in many ways the programme is just a continuation of a long history of transfers from public finance to private finance and from supply-side subsidies to demand-side subsidies. I guess that most of us thought we would be here 10 years ago. In that sense, it is something that is reasonably well tried, not particularly new, but it is being put in place in a very difficult economic environment.
Significantly, the programme is dependent on what is going to happen in the market. There are risks associated with the extent to which the associations are dependent on sales and other aspects of their work. The third issue is the obvious one that when housing benefit was with supply-side subsidies, you made a coherent decision about it; when you are making it in two distinct Departments, there are different trade-offs to be made. Those are the obvious areas of difficulty.

Q2 Chair: What contribution will the programme make, in your view, to meeting housing need? There is a figure in the report of some 4.5 million people, which I assume is a waiting list figure from last November. This is 80,000 homes, which is less than 2%.
Professor Whitehead: That goes back to how much money you have at the start of the thing. Obviously, if that is what they have been told, they have to do the best that they can within that number. Obviously, we would all like to see rather more housing being built of all types, but that was not the remit at that time. That is, of course, the reason why there is underlying pressure to move from supply-side subsidies to demand-side subsidies, because demand-side subsidies go to those who “need it,” while supply-side subsidies go to whoever happens to be in the sector.

Q3 Chair: Moving to you, David Montague, because you are having to implement this on the front line. Does it cause you worries about the financial viability of L&Q over time?
David Montague: It does not cause me worries about the financial viability of L&Q. We only take risks we believe that we can afford to take. If you look at the sector as a whole, we are looking at borrowing something like £15 billion over the next four years, so the impact on our gearing will be significant. That in itself poses a question about whether affordable rent is sustainable over the longer term.

Q4 Chair: What is your view there?
David Montague: In the longer term we will have to revisit this. As we approach the limit of our gearing covenants with lenders and seek to borrow more, that will require a renegotiation of those covenants, which in turn will open a door to a discussion about the re-pricing of our existing loans. That’s the biggest risk

that housing associations face at the moment. In my experience, certainly from L&Q and I know from colleagues in the sector, we welcome the flexibility we have been given and we are using it in a responsible way.

Q5 Chair: I do not know how countrywide L&Q is. Where is your focus nowadays?
David Montague: Our focus in on London and the south-east only.

Q6 Chair: Is that viable for you in London?
David Montague: We are using our annual surplus to cross-subsidise affordable rents.

Q7 Chair: But that's a one-off isn't it?
David Montague: It is what we typically do. We build for sale as well as for rent. The profit that we make from our sales pipeline and from driving efficiency within our own business is used to cross-subsidise affordable rent. Affordable rent needs subsidy, and that is the limit of our ambition, the amount of subsidy that we can invest.

Q8 Chair: In this programme, when are you going to start trying to sell?
David Montague: We are selling already.

Q9 Chair: So you have homes almost complete? Or, when in the pipeline are they going to come out?
David Montague: We have a development pipeline of 10,000 homes; that includes 1,800 homes at affordable rent. Within those 10,000 homes there is still a long tail of social rents. The vast majority of what we are doing is on the old social rent programme, but about 50% is for sale.

Q10 Chair: 50%?
David Montague: So 50% of those homes are for sale.

Q11 Chair: When are you starting to put them on the market?
David Montague: The spike in our sales programme is over the next two years. The profits that we make in the next two years will be used to invest in affordable rents.

Q12 Chair: I don't know if Professor Whitehead wants to come in with an analysis of the housing market in two years' time.
Professor Whitehead: I think this is the biggest risk at the moment, because it is not obvious that the mortgage market is going to be much better over the next two years. Therefore, particularly if you are doing mainly shared ownership, or low-cost home ownership, which anyway have significant risks attached to them, it is the biggest risk.
David Montague: We are a London-based housing association where the market is still buoyant.
Professor Whitehead: So you should be able to sell.
David Montague: There are bigger question marks in different parts of the country.

Q13 Chair: Do you want to comment on that, David Orr? Given where the London housing market is, does the model work better in London? From your experience nationwide, how does it look?
David Orr: As with most models, it works differentially. There are some parts of the country where it is easy to see that as a model it is perfectly sustainable.

Q14 Chair: Are there housing associations operating in Norfolk, Suffolk and around there that are going to be in greater difficulty because the housing market is flatter?
David Orr: Yes. In Norfolk, Suffolk, the north of England, parts of the south-west and lots of parts of the country, this model will be problematic.

Q15 Chair: Are you getting housing associations that are reluctant? They may have been granted an allocation under the programme but are not taking it forward. Is there any evidence of that? Or are people going ahead, fingers crossed that they are going to be able to sell the part of their development that they have to sell to make the financial model stack up?
David Orr: There is no evidence of people withdrawing from commitments that they have already made. As David Montague suggested for L&Q, housing associations across the country have done the sums and worked out what the risk exposure is. This programme will work for this spending review period. It will use up a lot of capacity. One of the risks is the question of what will happen in the sales market, both for outright sales and for shared ownership, and what will happen to rents in the private rented sector. Of course, there are some parts of the country where private rent is less than the social rent—not many, but there are some. This model does not work there. You have to approach it in a different way. In those places, it is a question of finding different ways of providing the subsidy.
What we have at the moment is an acceptance that you need subsidy to provide affordable homes. The balance between demand and supply-side subsidy, as Christine described it, has been well known. This is a rapid transfer to a revenue subsidy based model—housing benefit. As housing benefit is squeezed, it becomes more difficult to see how that model will work. It is also less cost-effective to the public purse over time to have that housing benefit basis, rather than a capital investment basis. I understand why it was done at the time when it was done, but it is not a good use of public finance in the long term.
The issue that we have to confront collectively is that if we are to develop subsidised housing, where will the subsidy come from in future? Some of that can come from more active asset management by housing associations, selling some of the stock. It might come as a capital investment, or it might come from free land, but unless we address this question seriously and rapidly, it will be very difficult to see how a programme of the size that we need can be delivered post-2015.

Q16 Chair: David Lunts, I will ask you about London, because, again, if you look at the Report, it is London where the subsidy has completely collapsed. Figure 10, on page 26 of the Report, shows a massive cut in the subsidy in London. You wonder what has fallen off the end because of that. First, with the GLA, what is your view of how this will work in London? Secondly, you have a bit more flexibility, so how are you choosing to use that flexibility?
David Lunts: You are right that the loss of subsidy in London was more dramatic, so the gearing issues that David and others have spoken about are more dramatic in London. Under the old programme, about 44% of scheme costs were grant, and it is about 14% under the new programme, which is a very significant reduction. What does that mean? It obviously has big implications in terms of borrowing. To some extent, it has been possible to ameliorate some of those issues in London because build for sale and shared ownership have been very well supported over recent years, so there is still, in some housing associations' business models, quite a lot of cross-subsidy coming in.
The other issue that is a concern across the housing association sector, and which, I think, represents certainly a short-term risk, but perhaps a longer-term risk too, is trying to calibrate the affordable rent programme for housing need, rather than just numbers of units. We have done very well in this round to ensure that about 36% of the rented units are three-bedroom or larger, which is where the need is in London.

Q17 Chair: 36% of the rented units in London have three bedrooms or more?
David Lunts: Yes, but that becomes increasingly challenging, because they are expensive to build, and rents have to be suppressed, obviously, because of the new household welfare cuts.

Q18 Chair: I do not understand the business model. Are they just using their surpluses? It is all being funded through surpluses, but that is just a one-off, is it not?
David Lunts: Well, it is partly funded through surpluses, asset management changes, re-lets of voids—

Q19 Chair: What does "asset management changes" mean? Selling?
David Lunts: Yes. It means that there is rationalisation of stock going on in some cases, but it also means that there is a reliance on re-lets of stock at affordable rents as well. In London, our biggest challenge has been to try to find a solution that gets the gearing in from higher rent levels at levels that do not completely compromise the benefit position.

Q20 Chair: Who has lost out? I looked at this graph and thought, "Crumbs, it is such a cut." Either the subsidy was OTT before—I do not think my constituents in Barking and Dagenham would think that—or somebody is losing out. It is not clear in the Report, so it might be clearer from your experience. What has changed, or what will change, as a result of this? Is it that poor people simply will not be able to access this? Will only people who are totally, rather than partially, dependent on benefits be able to access it? Will young people not be able to access it? What is going to fall off?
David Lunts: To some extent, that will be conditioned by what happens with welfare reform in the future, because some recipients of housing will struggle more than they do at the moment.

Q21 Chair: Who?
David Lunts: Well, it depends. If we see the loss of housing benefit for younger people on a more categorial basis, that is obviously going to impact on who is able to qualify for affordable housing in future. The other thing to say is that there is a concern in the sector about the extent to which nominations for new homes at affordable rents will benefit recipients, rather than those in work who are perhaps still able to get housing benefit and are not caught by the £26,000 cap. There is a very active debate among housing associations in some London boroughs on who the priority groups are for new affordable housing.

Q22 Chair: I will come to you Stewart, but David wants to come in on that point very quickly.
David Orr: I do. The main impact will be on the state, somewhere else. The cost of housing benefit over time will rise, because the rents that are being supported by housing benefit are higher. Some people will pay the rent themselves, and will therefore pay much higher rents, but other people will continue to be supported by housing benefit. A very important tactical question is whether the affordable rent product should be for people who are earning more, therefore reducing the opportunity for people on very low incomes to get social housing, or whether this is the new offer for people who are on very low incomes at much higher rents, which leads to the probability that people will be even more comprehensively trapped in benefit dependency than they are now. It is an absolutely clear rebalancing away from the up-front capital investment that costs more on day one, in favour of the long-term revenue subsidy that costs more over time.

Q23 Chair: PFI by another name.
David Montague: The other price that we are paying is in terms of volume. Broadly, housing associations—certainly the G15, of which L&Q is a member—are delivering something like half of what we delivered before. We are absolutely committed to doing as much as we can, but we can do less with less support.

Q24 Mr Jackson: Specifically on the affordable rent model, is there a need to revisit the operation of the model, given regional differentials in affordable rent and market rent, and do you see that as an option? That is the first question. The second quick question is this: would you have preferred an affordable homes programme that looked at discrete projects on a site-by-site basis, or is there a risk in having a time-based, holistic group of projects over a number of years that might not be delivered for the reasons you mentioned to do with the housing market? Finally, do you see affordable rent in the context of wider social welfare reform, the diversification of income and funding streams for housing associations, and tackling the problem of welfare dependency, which David mentioned? Some people would say that welfare dependency has been embedded by the fact that social providers have only effectively had one income stream, which is housing benefit.

Professor Whitehead: Just to be awkward, I will start with the middle question about discrete projects. The nature of this model ought to be that the people who are bidding for it and win, after regulatory checks, have as much freedom as possible within the general framework. The more you tie it down, the less they are able to use their management skills effectively. That would be my concern if you went for discrete projects, but clearly there is an issue, because although surpluses happen every year, or have happened every year up till now, and therefore we can build in the capacity to use those surpluses, that varies regionally, and they will be looking to try to maximise their potential to keep their funds low. Going back to the question of who suffers in the long run, it will be future tenants, but you can also argue that because interest rates are so low at the moment, and because they can tie in early, we are actually using that quite effectively by taking out bigger debt at this point.

Q25 Chair: At the moment.

Professor Whitehead: At the moment, precisely.

David Montague: Continuing that point, the flexibility that we have been given to manage on a programme basis is very much welcomed, as Christine said. If we are going to take on an additional amount of risk, the ability to manage that risk comes from the flexibility of having a programme approach. The big issue we have is the drop-dead date in 2015; if developments fall a few days after that date, there is no funding, and that is obviously a big concern for us. It is more of a concern because between now and then we should be building up our land bank, and obtaining planning permission for whatever comes after 2015. It is trickier to do that if we are not sure what the world will look like after 2015. We are very keen on a programme basis.

As far as revisiting rents is concerned, there is not just a regional perspective, but a London perspective. Every housing association has a different approach, and every local authority has a different view. Over the next four years, we are building something that will become very complex. At the end of this four-year period, it will do us all some good to stand back, look at what we have created, and try to simplify it.

David Orr: I agree that we have to do some kind of review of this programme. Any assumption that we can just repeat it as is for the next spending review period would be a mistake, partly because of the capacity issues, but partly because when you introduce something new and as significantly different as this, you have to take time to understand what its impact has been. I am strongly in favour of a programme basis to it. Indeed, because the amount of capital investment is so small in relative terms, I would prefer to see Governments saying, “These are the outcomes that we wish this money to deliver,” and then going to housing associations and others and saying, “Come with your very best, most creative thinking about how we can deliver those outcomes with this amount of money.” That would be a much better way of engaging some creative thinking than creating another set of rules to which you have to conform.

On the welfare reform agenda, one of my frustrations is that this programme and the welfare reform agenda seem to have been operating in parallel, and they have such an immediate impact on each other that that has been very frustrating. My own view is that this programme will make the welfare reform agenda more difficult to deliver. There is an absolutely critical issue about welfare reform, however it is calibrated: as many people have said, if you want people to be in work, it has to pay. People have to believe that they will be better off in work than out of work. As you see rents go up, you feel more trapped by that, and it looks like the salary you have to earn becomes higher and higher. Psychologically, as much as anything else, it will make people feel more trapped and less able to get out.

Q26 Chair: Do you want to add anything to that, David?

David Lunts: Just two points, very quickly. There is a need to look again at the regional position in London. Partly that is because of some of the anomalies created by the interface with the new welfare reforms. It is most dramatically seen where we have, as I have already mentioned, a fair proportion of larger homes. In many respects, they are having to be let at lower rents than the smaller homes in order to operate within the welfare cap ceilings. I am not sure that that is sustainable in the long term. It is a very difficult thing to present.

On the point about discrete projects as opposed to a programme, David has already said that it makes sense in many ways to move to a programme basis. It is a lot more efficient, and the sectors generally welcome that. What tends to lose out a little is the fact that there will always be those projects that have huge local or strategic significance, and where you need a slightly different funding solution than you do for a vanilla project. It is those schemes—the big estate regeneration projects, for instance—that are very difficult to fund under this model. That perhaps needs a fresh look.

Q27 Meg Hillier: We have talked quite a bit about the value for money for the council versus revenue funding, but we are also keen to see what the value for money is for tenants—we have touched a bit on that—but not just for tenants, because this is wider society. This is a question for both Davids—sorry, there are more witnesses called David than there are women on the panel but, hey, it’s Parliament. Perhaps I could ask you, David Montague and David Orr, whether you have had any local authorities that have not wanted to work with you because of the 80% affordable rent model.

David Montague: Perhaps some have. You have to bear in mind that this is very much a London perspective, because L&Q operates almost entirely in London. Our experience is that local authorities in London are, on the whole, taking a pragmatic approach. It is something to which there are some philosophical objections, but everybody wants to get new homes out of the ground, so we are co-operating on a very pragmatic basis with local authorities.

On the whole, housing associations are using the flexibility that they have been given in an entirely responsible way, so you are not seeing housing associations across the board increasing their rent to 80% of the market rent. Because our starting point has been to look at what we believe our residents can afford and shaping the rents that we are charging around what we believe they can afford, and because the GLA has taken exactly the same approach, the London position is that, on average, we are charging around 65% of market rent. Our rents are less than what we could have charged, and as a result, they are affordable.

Q28 Meg Hillier: But even 65% of market rent in some areas—think of Shoreditch—would be pretty unaffordable. Are there areas that you are not going to be working in?

David Montague: Again, I can speak for L&Q on this point: the 65% is an average. In Bexley, our rent is likely to be higher, whereas it will be considerably lower in Westminster. On average, across the whole of our 1,800-home programme, it will be around 65%. It is based very much on local affordability.

Q29 Meg Hillier: David Orr, with the national picture for housing associations, is there a pattern here? Are local authorities playing ball?

David Orr: Yes, I think David's word "pragmatic" is exactly right. I think that housing associations and local authorities have approached this in an entirely pragmatic way. Even those associations and authorities that do not like it have said, "There is an overwhelming need to get the new homes built. If this is the only offer on the table, we'll make use of it." There are one or two exceptions to that. There are some places where some housing association boards have said, "We don't like this product, so we are not going to do it," and there are a small number of local authorities that have said, "We don't like this product, so we are not going to support it." What has happened in those cases is that the investment potential has just been relocated; it has gone elsewhere.

We knew from the start that it was always possible to do this. You can build homes with no capital subsidy and charge market rents, and then see the whole of the support coming from a revenue subsidy. That would not work very effectively. I think that the picture across the country is, "Even if we don't like it, we need to do what we can to make it work, because the alternative is doing nothing, and that is not a good alternative."

Q30 Meg Hillier: May I touch on shared ownership sales, because David Montague talked about having your ownership market? I know that for the big G15 that is very much a model, but not for older or smaller housing associations. Are you seeing difficulty in shifting shared ownership properties?

David Montague: At the moment, no. Bear in mind, again, that this is a London perspective. It is a product that is in very high demand. We have developed products within L&Q to support those potential homeowners who cannot raise the money for a deposit and the products that we have created have not been used. So, somehow, people are finding good deposits and raising the mortgage.

Q31 Meg Hillier: That is good news, but are they going to the right-sized families? I have come across a number of examples in my own constituency with shared ownership of four bedrooms going to a couple with no children or a couple with one child, but that was not quite what they were being built for, in terms of value for money for the taxpayer and for big families.

David Montague: There is certainly a drift towards people on higher incomes and people who can afford to buy. I think that that is a fair point.

David Orr: There is demand for this product across the country. It is not just in London. There was a spell when there was a significant number of shared ownership properties unsold. We have got past the peak of that. The number unsold is reducing steadily. Mortgage finance remains critical. Shared ownership can work if the mortgage finance is available. It can work for people on low to medium incomes, as well as higher incomes.

Q32 Chair: If you are just selling to people at the higher end, that is not the purpose of this programme, is it?

Meg Hillier: That is part of my point. And also selling to people who have a need—everyone needs something in housing terms—but if you are building four-bedroom or three-bedroom properties, they are mainly for families. If they are going to be without children, even if they hope to have children, is that really what the programme was supposed to be doing?

David Montague: Typically we agree a cascade mechanism with local authorities, so we prioritise those people whom local authorities would like to see us sell to. If we fail to do so, we can go back and seek authority to sell at the next tier within the cascade.

Q33 Chair: How much do you not get through local authority nominees, so that you are then almost like any old seller on the market?

David Montague: There tends to be bands, so the people in greatest need are prioritised and then, with the permission of the local authority, we will go to the next need category, but it is always with the permission of the local authority.

Q34 Meg Hillier: Do you monitor at L&Q—I do not know if the National Housing Federation monitors this—what percentage do not go to those in greatest

need and what percentage go to perhaps key workers in the next band down?
David Montague: We do monitor that. I do not have the statistics here, but I can provide them to you.

Q35 Meg Hillier: It would be really helpful if you could.
David Montague: It tends to be, naturally, in higher-value areas where we struggle to sell to people in greatest need.
Meg Hillier: Which is most of my constituency.
Chair: And mine.

Q36 Meg Hillier: May I ask a final question about providers and the market? You are one of the big G15—L&Q—and David Orr represents every range from the tiniest through to the biggest—
David Orr: Tiny to huge.
Meg Hillier: Are people falling out of the market with this model? There must be some housing associations that will never develop again because of this model—their gearing would never allow them to do it.
David Orr: There are some housing associations that will not be able to do very much more than they have done, at least for a period of time. It is of course possible, if you are a housing association, to withdraw from development and rebuild balance sheet capacity over time, which makes sense from a business point of view, but from a mission point of view is pretty disastrous.
A number of housing associations that still have some capacity have not been part of this programme, in some cases because they do not like the product and do not think that it is a good use of their resources, and in some cases because it was not possible to get into the programme. We need to explore ways of encouraging those people back into the market, but we may have to think a bit more laterally about the nature of the product and how we can invest in it.

Q37 Meg Hillier: Can I just quickly fire to Christine Whitehead: do you think that is a problem, in terms of reduced competition in the market, or does it not really matter whether it is 10, 15 or 500 housing associations?
Professor Whitehead: I think it is likely that who is going to develop will change over the next five years, as it has done over the past five years. Big does not necessarily mean no risk. There are a number of associations that have taken a subsidy in the past and are not prepared to play ball at present, and that is an issue that will probably get addressed.

Q38 Matthew Hancock: I want to tease out a bit more, and get your view on, the value for taxpayers' money in all this, because that is what this Committee is about. Of course, provision of housing for everybody is a vital role of the Government, and the CLG Committee looks into the policy behind that, but what we really care about is value for taxpayers' money. When I hear that housing associations are going to deliver the target but it is tougher because there is less money available, from this Committee's point of view that is a good thing, because we are delivering more for less—the Government rather; we deliver as much as we deliver—so the value for money has improved if it is tougher for housing associations.
I have also heard some concerns that if people drop out of the market, it might become more difficult. I can understand that, and it is something that needs to be borne in mind. However, in the switch to revenue funding and in the subsequent delivery of the programme, which you, David Orr, expect to happen within this CSR period, even despite the tightening up of the rules on benefits, what are your main concerns for value for taxpayers' money in the delivery of social housing?
David Orr: There are a variety of different views about the relationship between demand and supply-led subsidies. We did a piece of work a few years ago, which needs to be refreshed because the world has changed a bit. It suggested that if you expect a revenue subsidy to be required for seven or eight years or less, that is more cost-effective to the public purse than a capital subsidy. If you expect it to be used for more than that period of time, a capital subsidy, over time, is more cost-effective.

Q39 Matthew Hancock: At what interest rate?
David Orr: This is why we need to re-do this exercise.

Q40 Matthew Hancock: You cannot translate a capital into a current subsidy without knowing—
David Orr: Exactly, but this is why we need to re-do the exercise to take account of the circumstances now. The point I am making is that if you take the view that the subsidy goes to an individual household—in other words, the people in that house—they will move around.
Matthew Hancock: Yes, because it is people who you really want to support.
David Orr: However, if you build a new home for affordable rent and you are a housing association, it will be your expectation that that home will be used for people who are in housing need for the whole period of time that that property is there, which might be 60, 80 or 100 years. If you have a capital subsidy that reduces rents, that is a more cost-effective use of public money over time than having a revenue subsidy that you will be effectively charging during the whole of that period.
Professor Whitehead *indicated dissent.*

Q41 Matthew Hancock: Professor Whitehead, you disagree—sorry, I do not want to misrepresent you, but you were shaking your head.
Professor Whitehead: I was shaking my head because I do not think that that distinction between 80 years and changing tenants works. It does matter how often the tenants turn over, but it also matters that tenants have different experiences over their lifetimes. Most of the work shows that tenants will not need subsidy for all of a 30 or 40-year-period, so it is not quite as straightforward as David is saying, although I do not blame him for saying it.
David Montague: From a value-for-money perspective and from a G15 perspective—G15 is the

15 largest associations in London—I would say that for every £1 of Government money, we invest £6 of our own. That is pretty good value for money. Looking nationally, £4.5 billion of public investment is being matched with £15 billion of private investment which, again, is pretty good value for money.

Q42 Matthew Hancock: The question of value for money is what would happen to the private investment, given a change in the public investment. If public investment decreased, but the private investment carried on at the same level, it would be even better value for money.
David Montague: Yes, it would, but the issue then is one of sustainability.

Q43 Matthew Hancock: Exactly. It is about what happens to the private side.
David Montague: We can do this once, but we will have to think carefully about how we do it, if we do it again.
Briefly on the issue that David Orr raised, we are in the process of modelling the scenarios that David has also modelled, and now our conclusions are that if you take a seven-to-10-year view, revenue funding is more effective, but if you take a longer term view, capital funding is more effective. It depends very much on whether you believe that the homes that we are building should permanently be for people who will need support.

Q44 Matthew Hancock: Or how long people are in receipt of benefit.
David Montague: Yes; and what happens to the home when those people move on.

Q45 Chair: There is an interesting thing about the Report. Obviously, to maximise the number of units, you reduce the level of subsidy on capital. That is clear, but the Report says that in terms of value for money—this is the point that we are discussing—having a greater capital subsidy is better value. There is a dilemma, isn't there?
Matthew Hancock: Over the long term, yes, but it all depends on what the long term is, which was Professor Whitehead's point, and how long people stay in the system.
David Orr: If you develop new homes as a housing association and you receive any capital subsidy, one of the commitments that you make is that that property will be available for that purpose in perpetuity. If people move out, you would anticipate that the next household that moves in will be a household that is in housing need and in need of that subsidy.

Q46 Matthew Hancock: But you also have to assume that people will move out when they no longer need the house, and that is one of the sticking points in the system, isn't it?
David Orr: It is, and there are some people presently occupying subsidised rented homes who do not need the subsidy—that is true. It is a relatively small proportion and there is more movement than some of the popular discussion would suggest. People on average stay for seven to 10 years, although some people stay for their entire lives. There is then a social policy question about whether that kind of security and stability in local neighbourhoods is more or less important than the financial subsidy, and that question is well worthy of debate.
David Montague: In the unlikely event that capital subsidy proves to be less value for money in seven to 10 years, there is always the option to cash in Government investment. In my view, however, it is extremely unlikely that the homes that we are building today will not be needed in seven years' time for people on low incomes.
Professor Whitehead: You could argue that this has dug out a lot of money from housing associations. To that extent it is value for money, but it is a one-off exercise. It was not happening before. They were taking more and more subsidy, so one could argue that a one-off exercise is worth it. The sustainability is a different story.

Q47 Matthew Hancock: That is because their balance sheets have been strengthened significantly by the rise in the value of the housing.
Professor Whitehead: Precisely; you can do it every 10 years.

Q48 Austin Mitchell: What we are actually doing is replacing Government subsidy with rent increases. "Affordable" is an indefinite, stretchable term. If we take into account high-rent areas such as London, with an increase in rent to 80% of market rates, plus the higher prices of houses, which have not come down all that much, plus the fact that you have been asked to build more houses with less money, and plus the fact that housing benefit is going to be cut, is the end product going to be affordable, and who to? It will surely not be affordable to the people in most need in our present housing situation.
David Orr: You are right to say that "affordable" is a pretty elastic concept. Defining affordable is always something of a challenge. The bottom line is exactly as you say: under this programme rents will be higher. If you are on a very low income, or out of work and already some distance from the jobs market, a higher rent means that you have to earn more to be able to escape from being dependent on benefits. It is absolutely crystal clear that that is the case.
The alternative is that you offer this higher rent product to a different group of people who are more economically active and able to pay that higher rent, but perhaps cannot afford a market rent or cannot afford to buy on the open market, and there is a perfectly sustainable argument that that is a good thing to do. The difficulty is that if you do that, you reduce the amount of supply for people who are in the most acute housing need and therefore create even greater pressure there.
It does not matter how many times you go round this circle—there is only one solution, and that is a major new house building programme. A lot of the conversation at present is about how you ration a

resource that is already too scarce. The real problem—the real debate that we need to have—is: by what process can we see significant growth in new house building for all tenures across all parts of the market, and across all parts of the country? Until we do that, these problems will remain acute. We are on the verge of a significant housing crisis, which will have an adverse effect on the future potential of the national economy.

Austin Mitchell: Thanks. That is a good, clear answer. I say that because I agree with it.

Q49 Chair: Christine, do you take the same view?

Professor Whitehead: I take generally the same view, but in relation to the argument about whether they will end up on housing benefit, the alternative is that they are going to end up in the private rented sector. The Government have modelled, on the whole, moving a private tenant to a social tenancy, and clearly that reduces the amount of housing benefit and makes it easier for that person to get into a job, so it works in both directions.

Q50 Austin Mitchell: But your Cambridge centre and Alan Holmans work have been saying for many years that there has been a gap of about 100,000 houses between what we are building and what the need is. That must be a cumulative problem. Is this new policy going to do anything to close that gap?

Professor Whitehead: This policy is simply an outcome of there being assets that can be used to borrow to build. If you are going to cut capital subsidies for other reasons—if you are going to cut what is available—this is the best way of getting something now. That is all.

Q51 Austin Mitchell: A bit more out, but will we get enough out to close the gap?

Professor Whitehead: Of course not, but we were not there in the first place.

Q52 Chair: Have you got a view on what proportion of disposable income should be spent on housing? Is there a current view on that?

Professor Whitehead: It is interesting that it keeps going up in people's minds.

Q53 Chair: What is the general academic thinking on it?

Professor Whitehead: Academics do not like proportions, because they are proportions for large incomes as well as for small incomes. The traditional NHF thing has been 25%. In most countries, it is now up at 30%. I am not saying that that is good.

Q54 Mr Bacon: It sounds like there is a tablet somewhere that you can go and consult; if you just dig hard enough, you will find the right number on it with a percentage sign. Is that correct?

Professor Whitehead: No.

Q55 Mr Bacon: I am reassured. I want to ask you a question about something else that Mr Orr said—the same point, really. Mr Orr's answer essentially was that we need an increase in supply, if I understood him correctly.

David Orr: Indeed.

Q56 Mr Bacon: You, Professor Whitehead, are a professor of economics at the London School of Economics so this might sound like a basic question. We have markets for a variety of things that seem more or less to be in equilibrium. Let us take two examples of things that people definitely need in addition to housing: food and shoes. There is generally enough food around for people, and we do not need a massive rise in the supply of food in order for this market to be in equilibrium. It seems to work and to be in equilibrium, more or less. So we have enough food to go around. In fact, the problem is a different one: that we generally eat too much food. Basically, the market seems to operate.

The same is true of shoes. Generally speaking, when you walk around in any city, you do not tend to see people barefoot—mostly, they have got shoes. By the way, we do not suggest that the answer to any problem is to introduce a national shoe service in order to solve an impending shoe crisis.

Can you just explain in simple terms why it is that we do not seem to be able to get equilibrium in this other market: the housing market? You have been studying this for many, many years and it seems to me—and, indeed, to Mr Orr—that the answer is that we need an increase in supply, but we are not getting it and have not had it for many, many years. Why can't we get this equilibrium in the way that we seem to be able to, without any difficulty and without huge state intervention, for food and for shoes?

Professor Whitehead: Food and shoes on the whole cost something like £5 or £10 per unit at most. Well, houses cost £100,000 per unit, so indivisibility is enormously important in why it does not work. The result is that demand varies enormously quickly and supply does not vary very quickly. We are building 0.5% of the total stock. In food, you are producing most of it each year, which makes it much easier to adjust supply to a change in demand. That is one of the big issues. The second is the land market, and the third is the distribution of income.

Mr Bacon: I am sorry. Can you say that second bit again?

Professor Whitehead: The second is the land market, which generates land prices that reflect the capacities of much richer people to buy, other uses of land, the planning system—

Q57 Mr Bacon: And the total supply of land. The total availability of land on which you can build is the real issue, is it not?

Professor Whitehead: Yes, so if we were in the DCLG Select Committee, we would discuss all the difficulties about land supply.

Q58 Mr Bacon: I assume that the second point is the main one, surely.

Professor Whitehead: But the third point is also that the distribution of income in Britain is very, very uneven. As richer people get richer, they want more housing as well.

Mr Bacon: You mentioned that you can buy shoes for £5 or £10. I am not sure that that is true.

Professor Whitehead: Well, £25.

Q59 Mr Bacon: How important is this indivisibility argument? There are lots of markets for expensive things like linear accelerators and they seem to work okay.

Professor Whitehead: Heavily regulated.

Matthew Hancock: Well, so is this one.

Professor Whitehead: Absolutely.

Q60 Mr Bacon: The housing market is heavily regulated. Is the market for linear accelerators heavily regulated?

Professor Whitehead: Most large-scale industries are heavily regulated, yes—although not as heavily regulated as housing. We have never produced more than 2% of the total stock in new output every year. But this is an accelerator-type model, so demand can go up by 5% in a year; if we have a good growth in income and the taxman is generous, it can go up 8% in one year.

What happens then is that house prices go up, we have a great crisis and there is not enough housing for poor people. At the moment, we just have a system that is fundamentally out of sync because of things like the land price and the fact that the price that is on the balance sheet is not the price it will sell for in the marketplace, so nobody is building until the balance sheets are sorted out and so on.

Q61 Matthew Hancock: You mentioned the land price, but, of course, the land price for land without planning permission is remarkably low in comparison with the price for land with planning permission. That means the granting of planning permission gives a great big bonus to whomever it is granted.

Is not a value-for-taxpayer-money way to build housing to grant more planning permissions? Would that not have the twin effect of allowing that uplift to be used for the building of affordable homes—in other words, affordable with a capital 'A'—and for making homes more affordable by increasing their supply? That does not cost the taxpayer a penny.

David Lunts: This is interesting. Of course, what you describe is what happens wherever it can happen, so there is a significant supply of new housing in London, for instance, that is generated through section 106 agreements. By and large, if there is a section 106 agreement producing affordable housing, we will not grant-fund it.

In London, I think there are something close to 200,000 fully consented housing plots, yet most of those plots are being built out at a very slow rate, and many of them are not being built out at all. Even though they may have planning consent, sometimes the owners of those sites are not interested in building; they are interested in trading the land. It is also the case that the structure of the house building industry in this country is generally more interested in protecting margin than delivering volume. So the industry is not particularly interested in exposing itself to large volumes of delivery—even, frankly, when times are better than they are today.

Q62 Mr Bacon: You are saying there is not enough competition and that there is basically an oligopoly, aren't you?

David Lunts: There is not enough competition in the housing market. That is true.

Q63 Mr Bacon: In a reasonably competitive situation, you would not be able to sit there and say, "Well, I'll protect my margin." I have seen this happen with people not releasing land: even though they have planning permission, they would prefer to protect their margin, eke it out and make a nice fat margin on each one.

Professor Whitehead: That is not necessarily an oligopoly.

Q64 Mr Bacon: It is not a complete oligopoly, but what Mr Lunts has just described is a definition of the absence of competition: "They are not that interested in volume; they prefer to protect their margin." In conditions of reasonable competition, you could not do that. Have I missed something, Professor Whitehead? Isn't that a definition of a reasonably competitive market?

Professor Whitehead: It is extremely difficult to get really competitive markets in a situation where your major factor of production is location-specific. You cannot import it, and you cannot do any of the things that you do in ordinary markets.

Chair: I will move us on, because we are getting a bit theoretical.

Mr Bacon: It is not theoretical at all; it is the absolute essence of why the housing market has not worked and why hundreds of thousands of people have nowhere to live. That is not theoretical at all.

Chair: I do not agree with your analysis.

Mr Bacon: We spend billions of pounds of taxpayers' money on it, and we have done so for 30 or 40 years—*[Interruption.]* No, I'll finish this. We have representatives sitting here from an industry that has failed for 30 or 40 years to deliver enough housing for people in this country, and you call it theoretical. I am sorry, but it is not. If you think I have a bee in my bonnet about this, you are right.

Q65 Austin Mitchell: Well, they will be bringing people up from London to Hull, so we could offer you refuge in Grimsby, if you want.

I have a quick question on financial viability. A lot of housing associations are facing real financial difficulties, because right-to-buy sales have fallen right off and they are finding it difficult to raise money on the market. So it is tough for them, yet they will have to change their attitude to become competitive builders and salespeople.

As for local authorities, where they control the housing stock, they have no money at all. Local authorities are facing a 26% cut over the period up to and including 2015. Is this going to be financially

viable for most housing associations? Are we going to see collapses and mergers? What is going to happen?
David Montague: If you look at the HCA's global accounts, which they produce on an annual basis, they add together all of the accounts of the housing association sector. In each of the last four years, housing associations have reduced their costs, improved their margins and annual surplus, increased their borrowing, completed the decent homes standard and built more homes, even though grant has reduced. Over the last four years, in the most difficult time in living memory, housing associations are stronger today, in my view, than they were—

Q66 Austin Mitchell: Now, life is even tougher.
David Montague: We have seen this coming, and we have prepared over the last four years for this moment. We are now embracing these very difficult times and getting 170,000 new homes out of the ground. The big issue is how we look in four years, once we are at the end of this programme. At the moment, we are strong and we are ready to take on this challenge; in four years' time, we are going to have to think very carefully before we do it again.

Q67 Austin Mitchell: Does the same go for local authorities?
David Montague: Well, local authorities are in a very different position from housing associations.
Matthew Hancock: They have to think, as well.
David Orr: May I say something?
Chair: I want to stop this, because we have to move on to the other one.
David Orr: Okay, I will be very quick. There are two or three things that will have an adverse impact on viability for this kind of development in the future. The first is that capacity will be used up—and when capacity is used up, you cannot do any more of the borrowing, even if the model says that it works theoretically. Second, income streams are under pressure because of the welfare reform agenda, and every housing association in the country is making contingency plans for seeing significant reductions in income because of that. Third—and perhaps the most important thing in some respects—we have, as David said earlier, no idea what happens after 31 March 2015.
The Government could do a couple of things now that would make a very significant difference. First, introduce rent certainty by saying that the present rent regime will last until 2020, and, second, they could confirm that there will be a programme after 31 March. They do not even have to say what the programme is, but if we did the old 80% of the past year and then 80% of that as a planning basis, those two things would make a huge difference.
Austin Mitchell: Thank you.
Chair: Thank you very much indeed. That was a very interesting session, and we wandered across the piece.

Examination of Witnesses

Witnesses: **Sir Bob Kerslake**, Permanent Secretary, Department for Communities and Local Government, and **Pat Ritchie**, Chief Executive, Homes and Communities Agency, gave evidence.

Q68 Chair: Welcome. It looks as if the programme, within the parameters set for it, is working well, so can we take all our questioning in that context? It looks as if you are, with one or two provisos, on target to meet the objectives that were set for you in policy. What I do not get—it is really out of my London model—is that if you look at figure 10 on page 26, the subsidy going to London housing associations under the new programme has been massively cut. Are social housing providers therefore—specifically in London, but across the programme—going to be letting to a different breed of tenant? Is that an intent behind the programme, or are tenants going to be paying a much higher proportion of their income in rent? Have you thought through that and the implications of that in establishing the programme?
Sir Bob Kerslake: Let me come back on that. There are two or three points in that question. The first thing to say is that there was clearly a reduction in the proportion of subsidy into affordable housing. It is worth taking it in context actually, because what happened here was, if you take the total cost of the properties, on average the subsidy reduced from a third to a quarter. As I am sure you have heard previously, that was consistent with a trend over a number of years. In that sense, this was not a massive shift in direction, but a continuation of a policy that had happened before. Quite clearly, the compensating factor in that equation, alongside efficiencies through the bidding process, was the impact on rents. Rents did change, but those rents went up within a context of the wider market, so they remained typically below the local housing allowance rents, and typically well below market rents. If you take the situation in the country as a whole, as against London, we were talking about up to 80%. In London, in reality the actual figure was 65% of market rents. So, you still had rents well below the market rate within the local housing allowances, but higher than they were under the old regime. I can give you numbers on that.

Q69 Chair: That is what has happened; we understand that. Does that mean that rents have gone up? Does that mean people are paying a larger proportion of their income in rents? Or does it mean that this programme is providing for a different group of people, in terms of meeting housing need?
Sir Bob Kerslake: Apologies, I missed that point. It doesn't mean that we are providing for a different group per se. Clearly, local authorities allocate linked to their own policies on need.

Q70 Chair: That will be in some senses. Sorry, I usually try not to be so London-specific, but the

impact of this programme is dramatic in London. There has been a dramatic shift from a capital subsidy to rent and therefore housing benefit. Either that means people are spending more or that maybe a different sort of person is emerging as a tenant of new housing created by the affordable housing programme.
Sir Bob Kerslake: Not necessarily. If you think who might be moving into that housing, it may well be people who are currently in market rented housing in London. If you look at the numbers, the market rent of comparable properties is £280 a week. If you go into the affordable rent property, you are paying £182 a week.

Q71 Chair: In London?
Sir Bob Kerslake: In London. Those are the London figures. The point I am making is that for those people moving out of market rented property into the affordable rented properties in London, they will be seeing a reduction in the level of their rents, not an increase. Bear in mind, this is about new tenants. It is not about existing tenants. Existing tenants have not been affected by this model. Those who are in existing properties, either in housing association or council properties, continue to pay the rent they were previously paying as social rent. This affects new tenants going into properties.

Q72 Stephen Barclay: But, Sir Bob, if they got into difficulty that would affect not just new tenants but existing tenants, would it not?
Sir Bob Kerslake: If the housing association got into difficulties, that would clearly be a different story.

Q73 Stephen Barclay: It would affect existing tenants.
Sir Bob Kerslake: Yes, but it is important to talk about the context. Housing associations are in a regulated sector, and it has been a well regulated sector for a long time. You can tell that from the fact that it managed to work its way through the impact of the housing downturn in 2007 which, as we all know, affected many private house builders severely. Housing associations were affected but were able to manage the impact pretty successfully. This is a regulated sector with a high level of financial capacity. Pat can say a bit more about this, but none of them was able to take on parts of this programme without advice from the then regulator, the Tenant Services Authority.

Q74 Stephen Barclay: But the banking sector was a well regulated sector, at least in theory, with financial acumen as well, and we all know what happened there. Can I come on to that point, in terms of how well regulated it is? Could you talk us through the modelling that you have done on the impact of interest rate changes on providers?
Pat Ritchie: In relation to the process that we went through when we looked at the bids for the programme, the regulator, who was part of the TSA at that time, worked closely with HCA, which was looking at the overall programme, to look at the viability of each of the associations who were putting forward bids. They reviewed all 120 bids and then identified a few where there were some concerns.
Chair: Are you answering the question? I am sorry to interrupt. Maybe Stephen should repeat his question.

Q75 Stephen Barclay: What modelling have you done? I take the point you are talking about is 3.9. My question was about what modelling you have done on the impact of interest rates. What is the tipping point for providers?
Pat Ritchie: The impact of interest rates on this particular programme—
Stephen Barclay: What is the tipping point for providers, from your modelling?
Pat Ritchie: The majority of the modelling that we have worked on is with the debt at a fixed rate.

Q76 Stephen Barclay: Sir Bob was talking about this as a well-regulated sector. I was struck with this idea of it being stand alone. There could be contagion. One assumes that asking providers to borrow is obviously attractive at the current time, because you can borrow at very cheap rates. It is not this Committee's job to look at policy, but one understands the policy. What I am interested in is what the tipping point is in terms of changes to interest rates.
Pat Ritchie: It varies across individual providers. Each provider has different arrangements around the borrowing that it has to support both this programme and its broader business. Part of the role of the regulator is to ensure that each provider meets clear standards of economics and governance by ability.

Q77 Stephen Barclay: Of course it varies. With respect, that is motherhood and apple pie. What I am trying to get to the bottom of is what the start is at which there is a tipping point for some providers, and what sort of percentage there is. What is your tolerance? Obviously, there is tolerance built into this. It is acceptable that there will be a tipping point. I am just trying to understand how much that has been modelled and what proportion of the market it would be at different rates.
Sir Bob Kerslake: I think, if I might say so, that we are struggling with the question because each housing association will have its own borrowing portfolio, large amounts of which are, of course, in existing stock rather than what they are borrowing for new stock. Housing associations as a total have just over £60 billion, and large parts of that are in back-book, and large parts are secured long term—30 years—at very preferential rates. So movements in the short-term rates are not the big issue for housing associations, because they have secured most of their debt on long-term borrowing and are currently securing it through bonds more than through bank finance.
It is not a question for them of whether, if the interest rate moves by x%, they are viable; it is down to each individual housing association. What we can say, and I think Pat has already said this, is that we have a very good understanding of where they are financially, and of their resilience as individual organisations. This sector is pretty robust.

Q78 Stephen Barclay: So you are relaxed, Sir Bob, about movement in interest rates during the period up to 2015 not having an impact on the viability of providers.
Sir Bob Kerslake: I am not saying that it couldn't have any impact but, in terms of what we know now, it is a programme that can be delivered with some changes in short-term rates.

Q79 Stephen Barclay: Has that modelling been shared with the NAO?
Sir Bob Kerslake: Not that I am aware of.
Chair: I don't think it's been done.
Stephen Barclay: It must have been done for Sir Bob to give that answer.
Pat Ritchie: May I just add to what Sir Bob said? The majority of the facilities—
Stephen Barclay: Sorry, but has it been shared with the NAO? Can I just check that?
Pat Ritchie: The modelling of each of the individual bids was shared with the NAO, and the way we went through the process was shared with the NAO—

Q80 Chair: But Pat, did the modelling have regard to shifting interest rates?
Pat Ritchie: The majority of the facilities in place on this programme are on fixed rates. There is very little that is on variable rates through the programme, and that was shared with the NAO as part of the overall process. As part of the treasury management of individual associations, the regulator will track, across the whole portfolio, any differences in interest changes and the way in which the association had managed that. But in relation to this programme, because borrowings were in place and you check that as part of the process of going through bids, we are of the view that interest rates will not affect the specifics of this programme, but they could affect associations overall. Generally, in 2009, when there was a significant drop in interest rates, all the associations were able to manage.

Q81 Chair: They had built up a surplus—we know that. Chris, did you want to come in?
Chris Shapcott: I just want to make one point. We looked at what was done for a sample of cases rather than for every single one. There is an issue with interest rates at both ends: there is an issue when they go up, and there is also an issue with low rates. We have a comment at the end of paragraph 3.13 about exposure to swaps. A number of associations have used swaps to fix their rates at higher levels than they currently are, and they are currently having to put up collateral to protect their position with their lenders. So low rates can be a problem for some as well.
Sir Bob Kerslake: Yes, but the point I was trying to make, perhaps not very clearly, is that you cannot talk about this in general; you have to talk about the individual housing associations and where they are in terms of their debt portfolio. Taken as a whole, the sector has been able to borrow long at low costs and still have substantial undrawn borrowing facilities. As of the present, £11.6 billion in undrawn facilities is available to the sector.

Q82 Matthew Hancock: But that is because, as we heard earlier, the asset side of their books has gone up substantially in the last couple of decades, so they are bound to be pretty strong.
Sir Bob Kerslake: Absolutely. They are bound to be in strong order. The change that has happened is not due to their financial position but that the banks have moved away from long-term lending, essentially. They have moved shorter.

Q83 Matthew Hancock: Yes, let's not go down that route in this hearing. On specifics, how many homes have begun construction under the scheme?
Pat Ritchie: Last year, in the programme, we had 13,800 starts on site through the new affordable homes programme.

Q84 Matthew Hancock: And how many now?
Pat Ritchie: We do not count them until six months, and then at the end of the programme. We track them on a six-month basis. So our results are based—

Q85 Chair: So that takes us up to what date?
Pat Ritchie: The end of this financial year.

Q86 Chair: April 2012?
Pat Ritchie: Yes.

Q87 Matthew Hancock: And what was the number you gave?
Pat Ritchie: It was 13,800 starts under the new affordable homes programme.

Q88 Matthew Hancock: So 13,000?
Pat Ritchie: Yes.

Q89 Matthew Hancock: Are you on track to hit 80,000 by March 2015?
Pat Ritchie: Yes, we are confident. That is where we expected to be at this stage in the programme, and we are on track to hit the overall HCA contribution to the 80,000. Some of that 80,000 will be delivered through London and the GLA.

Q90 Matthew Hancock: Yes. How much has been paid out on your scheme so far?
Pat Ritchie: We have paid out 75%. I do not have the actual amount.

Q91 Matthew Hancock: So you pay out in advance?
Pat Ritchie: Last year, in order to stimulate activity and get the programme going, we paid 75% in start on sites for that particular year.

Q92 Matthew Hancock: And what is your assessment of the value for money question that we were debating earlier? Were you in for the earlier session?
Pat Ritchie: Yes.

Q93 Matthew Hancock: Clearly, this is a different way of doing it. It allows you, especially when budgets are tight, to keep the building going, and we heard before that it also allows draw-down from

housing association assets to keep building going when money is tight, but there is a question of value for money. What is your response to the former assessment, before the crash, that anything over seven to eight years is better done through subsidy for building rather than subsidised rents?
Sir Bob Kerslake: I think we would challenge that particular argument, but the NAO Report captures the position pretty well. If you take it over a 30-year period, the old funding model comes out ahead—not by a lot, but it comes out ahead. But if your judgment is that you need to see housing impact and development now, there is a perfectly good and strong case for doing what we did and moving to reduce capital and increase rents in order to sustain supply. Had we not done that, that 80,000 figure would have been 27,000. If you take account of the economic and social impact of failing to supply in a period when the capital had already been constrained, I think the value for money works. I think the VFM point is well handled in the NAO Report, which comes down on that point.

Q94 Matthew Hancock: And what about the argument that the way that it has been structured allows you to get to the higher figure in constraint times, but requires draw-down on HA balance sheets, and is therefore not something that can carry on in perpetuity?
Sir Bob Kerslake: It certainly does increase the level of borrowing by housing associations, by definition. Again, Pat can talk from the HCA's detailed knowledge of the housing associations, but we know that there is still some headroom there. We have not completely exhausted the headroom available for new housing supply. I think a key question will be what that looks like in the next spending review. But we are some time ahead of that. No decisions have been made on the size, scale and form of the next programme and we would have to have that conversation then, but we know, from the work that has already been done, that there is still some capacity in the housing association sector to do more along these lines.

Q95 Chair: You know that, but is it in the right places? Housing need is not uniform across the country. There is much greater need in London and the south-east than in some northern cities. I am interested in whether you are looking for the houses to be built wherever the housing associations have that headroom.
Sir Bob Kerslake: No.

Q96 Chair: No. Your allocation and rationing was good: you had bids in for 160,000. You could only allocate half of them. What was the geographic spread, and how did you relate that to need?
Sir Bob Kerslake: Again, that is to do with the detail of each of the areas, but if you look at London, the ambition was to secure the same proportion of housing in London as under the previous programme.

Q97 Chair: Was that a good distribution? I have to say that even under the previous Government, I felt too much was being spent. I know it was in the days when you were in Sheffield, and you probably welcomed it, but in terms of housing need, too much was being spent where the need was not necessarily the greatest, even in those constrained times.
Sir Bob Kerslake: Obviously, that is a policy debate, and there will be differing views, I suspect, among MPs.

Q98 Chair: I am just interested in how you chose to ration. You had bids for 160,000 and you allocated 80,000. Was that on need?
Sir Bob Kerslake: Yes.

Q99 Chair: And how did you define need? Numbers on the waiting list? What did you look at?
Pat Ritchie: Again, I think the Report highlights this quite well. It was quite a complex process, with a very over-subscribed programme—we could have funded twice the number of bids, if we had taken all the applications. We went through a process of looking at the value for money of the bids, and the grant rates in individual operating areas—largely LEP areas—and compared them against each other. We then went out and renegotiated offers with providers to bring the grant rate down from £22,000 to £20,000—that was the average grant rate. During that process, we also consulted with local authorities. We talked to local authorities in groups in local enterprise areas and looked at their assessment of need, and looked at the bids and tried to get to a balanced programme in different geographies across the country.

Q100 Chair: Can I unpick all that a little bit? So you concentrated the programme in LEP areas, did you?
Pat Ritchie: We compared the programme within LEP areas with local authority need. We had to look at some form of geography to make comparisons. It is difficult to make national comparisons, given the differences in the housing market and the difference in need, so we looked at LEP areas, and we consulted local authorities through the process. We also renegotiated offers on the basis of value for money. We looked at the viability of offers, through the regulator. They were the different issues we took into account in looking at how we would allocate the programme. We ended up with a programme where 9% of it is rural, so it is reasonably balanced and similar to the previous programme.

Q101 Chair: Reasonably balanced against what?
Pat Ritchie: Well, the previous programme was about 10%-plus rural.

Q102 Chair: And that was reasonably balanced against what?
Pat Ritchie: That reflected housing need in rural areas. It was a sort of benchmark that gave us at least some indication of the spread of the previous programme. A third of the houses being built are larger properties, and around 9.5% are supported

accommodation, meeting the needs of elderly and special needs.

Q103 Chair: I was asking about geographic spread. I have a figure; you said that you were 9% or 10% rural, based on what happened last time, which I do not believe is necessarily an objective definition of where the housing is needed most.
Sir Bob Kerslake: What I would say on this, Chair, is that there has been a lot of work over many years by different Governments to try to assess relative need in relation to social, and then affordable, housing. You can come out with arguments in different directions. Typically, London has done pretty well out of it, in terms of outputs, and it has done pretty well out of the current affordable housing programme.

Q104 Chair: So what proportion came to London?
Sir Bob Kerslake: London was 23,000 out of 80,000.

Q105 Chair: A quarter.
Sir Bob Kerslake: Over a quarter.

Q106 Meg Hillier: I wanted to say something on affordability. We had the view from previous witnesses that it felt like the housing model was going in one direction, and universal credit was going on a parallel tram track. How much are you talking, Sir Bob, with your colleagues in DWP—and, indeed, with BIS and the Treasury—about job creation? A lot of this depends on tenants getting jobs.
Sir Bob Kerslake: We have a special team who work on nothing but welfare reform within CLG, and they are linked very closely with DWP, because we understand that the interaction between what we do and what they do is absolutely critical. It is important to say that, for this scheme, it is a small part of the story on welfare reform. If you look at the annual cost of housing benefit, it is something like £22 billion; if you look at what we say in the Report and scale it back to an annual figure, we are talking about £45 million, so this has a relatively small impact on the big welfare story. When we came to make decisions, as I said earlier, the trade-off with much reduced capital was on whether you built 27,000 homes, or 80,000 with some impact—a very modest impact—on the benefit story. Relatively, this is actually a pretty small part of the welfare reform story, and we work very closely indeed with DWP on all the other issues that I am sure will come up this afternoon.

Q107 Meg Hillier: My concern is that I think of tenants who might, with a good wind, do better one year, but who then lose hours and go back. Sometimes they may have moved out of the cheapest form of housing, but, because rents are going up, find it hard to secure that again if their hours went down. Some of them will never be able to earn a great deal.
A man who came to see me was a kitchen porter who could not even afford the travel and child care costs that would be associated with the longer hours if he worked very far away from home. I looked at everything he brought me, and it was absolutely clear he could not easily increase his income. Even if he did, the offset of the extra costs would be great. That, I know, could be said to be straying into policy, but if we are trying to provide affordable homes for people on the lowest incomes as part of this mix, it seems to me that there will be real challenges with this new model, as new lets of existing low-rent tenancies are going to be at higher rents.
Sir Bob Kerslake: You rightly say that there is a very big and wide story on the impact of welfare reform, so for this purpose I am really talking about it in the context of this scheme. As I said earlier, on this scheme, we are talking about rents that are not caught by things like the local housing allowance; we are talking about new tenants going into properties; and we are talking about rents that are substantially below market rents. It has some impact, but we must not overplay its impact in terms of those wider welfare issues. Those are real and big issues, but I do not think they are central to this scheme and its impact.

Q108 Chair: That hits me. If you are in Barking and Dagenham on the ground, Sir Bob, what is happening is you are not housing anybody who is not homeless. You are doing one or two odd decants, because you have got properties that are about to fall down on you, but you are not housing anybody who is not homeless. There is not the luxury of taking people who can afford these higher rents. They cannot do more than that, so how on earth is this contributing to—
Sir Bob Kerslake: I made the point earlier that if we build fewer affordable houses, the likelihood is that the people not going into those affordable houses are in market rented houses, which are a lot more expensive. It is not a question of either social housing or affordable housing; it is a question of market rented properties, most likely.

Q109 Chair: But that is taking people off waiting lists, and I do not think there is any London council that is ever thinking of taking anybody off the waiting list at the moment. That is almost like saying, “You go into private rented accommodation and put your name on the waiting list, in the hope that something happens in the future.” They are just miles away from you. We are literally talking about the homeless, people with probably really big special needs, and decant—that is it. I do not see how this in any way helps you to meet the priorities on the ground that a local authority has.
Sir Bob Kerslake: I am saying that it helps you meet it because you are building more housing, and more affordable housing.
Chair: No.

Q110 Meg Hillier: Only if you are earning a certain amount of money. Otherwise, you are perpetually trapped. A number of my constituents come to see me who cannot afford to work, because even with some housing benefit, private rents in Hackney South and Shoreditch are now so high that they cannot afford to rent locally. Even if they look at moving, that is challenging. Possibly Barking and Dagenham used to be the cheap place to go, but that is getting increasingly pressured now. Walthamstow used to be

cheap; that is certainly not the case now. They have not got many places to run to find housing. That has to be a responsibility for all of Government. We can argue about the social policy, about how much and when, and about whether people should save for ever; that is not what we are here to do. Those people will be taking more housing benefit if they are in the private rented sector, which is the only option if there is no more social housing, and often they will not be able to afford to work more, because if they work more, they lose housing benefit but still cannot afford the rent.
Sir Bob Kerslake: I am not in any sense denying the scale of the challenge regarding housing supply and rent levels in London. What I am saying is that in this scheme, we are talking about a relatively small proportion of the available housing stock—about 4%. As I said earlier, for a lot of people, the alternative may well be private rented, which is at a higher cost. That is all I am saying.

Q111 Meg Hillier: It is a strange policy. It is a question of whether you are trying to subsidise people who can already afford the private rented sector, or helping people who cannot afford to get out of this, or afford a home, indeed. May I ask Pat Richie a question? When you looked at the modelling, did you do anything to ensure that private rents were not being artificially inflated by the providers to make the 80% model higher, to help them manage their costs? Did you look at that at all?
Pat Ritchie: I am not sure—
Meg Hillier: Some of the providers provide across a range: they provide housing for sale; housing for private rent; intermediate housing for key workers, or whatever; and affordable housing. If they can charge up to 80% of private sector rents, did you do any analysis of the private rented market to see whether there was any artificial inflation of the private rented market locally by those people bidding, and also by other landlords?
Pat Ritchie: We looked at the average rent in each of the operating areas—the LEP areas, as I said before. We looked at what the market rent was compared with the offers that were coming in. In some places, there was no difference, and in some, the 80% market rent was much the same, but in others, there was a big difference, particularly in London; the GLA ended up in a position where we looked at bids of, on average, 65% of market rent, as opposed to the 80% of market rent model used in other parts of the country.

Q112 Meg Hillier: One of the things that the Government have been keen to stress is that there is a belief that in some areas—this is what the Government would say—housing landlords have been putting the rents up because they think that housing benefit will meet that; that is why local housing allowance caps and so on are being introduced. Was that something that you looked at when you were looking at the average rents? Was there any help from fixing of the markets?
Pat Ritchie: No, we did not look at that specifically in individual offers.

Q113 Meg Hillier: You spoke to tenants. Paragraph 2.6 of the Report talks about how you discussed issues with housing providers, and it says that you "analysed the cost to all tenants, including those who would not have all their rent paid by housing benefit, but the published analysis did not explicitly refer to the number of tenants in this group who would be affected". Do you have more details that you can provide us with on that?
Pat Ritchie: We did not talk directly to tenants through this process. We talked to housing providers as we were developing bids, rather than talking directly to a sample of tenants.

Q114 Austin Mitchell: I think that Sir Bob has done a marvellous job in making summat out of nowt. In other words, the Government were not going to provide the amount of subsidy for housing that was provided in the past, or that was necessary. They will cut down, and will build more hypothetical houses. As for the big build in the last year, 56% of the houses that were going to be built in the last year were hypothetical houses, based on a hypothetical concept of what is affordable, which is a very clever conjuring trick. However, it does nothing for those people who, at present, are facing a housing crisis, or for the housing problem that is building up. Under this system, Cathy is still not going to come home, is she?
Sir Bob Kerslake: I am not going to deny in any sense that we have a major housing crisis in this country, in terms of scale of build. We know that, and we know that we need to build more; I do not think that anybody would debate that point. The issue here was how we got maximum benefit from the capital funds that were available to us to build affordable housing. I think that, as you rightly say, we got the best out of the money available, but that does not deny the fact that there is a wider housing challenge in this country, and there has been for quite a long time.

Q115 Austin Mitchell: You could have fooled me. I have had serious representations about the housing crisis. Even in Grimsby it is building up. London MPs are overwhelmed with problems. Let us move on. It was said by the last group who gave evidence that this would benefit mainly the people who were the better-off among the worst-off, if you see what I mean. They are the ones who will be able to afford to buy the new affordable housing. I do not know what proportion of the population that is, but it might be about a fifth of the population who cannot afford to buy houses, even at affordable prices, certainly at the present higher level. They need public housing for rent to live in. It will not benefit them at all, because their rents will be increased. Incumbents are okay, but not new people coming along in that category.
Sir Bob Kerslake: As I said earlier, a high proportion—a higher proportion than under the old schemes—are going for rent, rather than shared ownership, so there is a higher number in this particular programme. The rents are higher than they were for social rents, but they are still significantly lower than market rents, so it is more affordable for those going into those properties. As I said earlier, if

they are moving in from market rented properties, they will see a reduction in their rent.

Q116 Austin Mitchell: But why do you not collect and provide the information, so that we know what rents would be charged and what the effect of the affordable rent model will be?
Sir Bob Kerslake: We know what the estimated rent levels will be in different areas. I quoted them for London, for example. What I cannot say is that I know exactly who moves into those properties once they are built, and where they come from. We do not have that detailed information, but we do know what, broadly, rents will be in areas from the new affordable housing. They will be estimates, and they will vary from scheme to scheme, as I am sure David said to you, but we have some sense of what the average will be.

Q117 Austin Mitchell: But surely this is what housing associations and would-be tenants and would-be purchasers need to know, so that they can assess the prospects for the next couple of years?
Sir Bob Kerslake: It is not difficult to tell people what potential rents will be in an area. We know what those are. I am sure that we can advise people of what those rents are. What I cannot say, as I said earlier, is who is moving into those properties and where they come from.

Q118 Austin Mitchell: It would be nice to know the affordable rent level in Westminster. IPSA says it is £1,400 a month for MPs. I wonder what it is going to be. London affordable rents will be so high it will drive people out of London, surely.
Sir Bob Kerslake: As I said earlier, although rents are clearly higher in London, and they are very high in certain parts of London, we are danger of seeing London as a homogenous whole, when it is not. The actual affordable rents are a lower percentage of the market rents. Across the rest of the country, they are nearer 80% of market rents; for London, they are 65%.

Q119 Austin Mitchell: That is no consolation if market rents are too high.
Sir Bob Kerslake: The average rent in London on affordable rent is £182 a week. That was the figure I quoted earlier.

Q120 Austin Mitchell: I have one more grievance from Grimsby. This will hit higher-rent areas such as London, but it will also presumably hit lower-rent areas such as Grimsby. Our housing association, Shoreline, which is a good housing association and does its best, got nothing at all from the Homes and Communities Agency, on the grounds that it needed to contribute a rent increase to the money granted in order to be able to afford to build. It was deemed that rents were so low locally that it could not put the rents up. Therefore it got nothing. For the first time ever, a housing association got nothing. Why was that?
Pat Ritchie: It is a difficult model to deliver in areas where rents are at a lower level, such as in parts of the north, the midlands and other parts of the country. I cannot comment on an individual application, but a number of associations in the north subsidised the programme in other ways—by, for example, putting land into the programme, investing surpluses, and doing more conversions to affordable rent.

Q121 Chair: That is what seems so stupid. The Labour Government got this wrong, too. We are forcing in mechanisms to build housing where the market is more than providing. You do not need to intervene in the market, because market rents are lower than you are able to produce through this particular product, and you have this appalling housing shortage, particularly in the London and the south-east. It is just a potty way of rationing what is less than 2%—this 80,000—of the 4.5 million on the housing side. I cannot understand why you went for this broad geographic spread, rather than using this small product to help those areas in greatest need.
Sir Bob Kerslake: This programme and the previous programme are very heavily weighted to the places of highest housing need.

Q122 Chair: Not if they were looking at these subsidies, Sir Bob.
Sir Bob Kerslake: If you look at the proportion of houses built, and percentage of subsidy, it is absolutely clear on both measures that London and the south-east get the highest number of houses and the highest quantity of subsidy.

Q123 Chair: I hear that, but we should not have ended up putting housing into areas where this product meant that the rents were higher than the market rents, and therefore we had to look at other mechanisms of subsidy. It just seems to me that when you have a tiny little programme—this is the extent of our publicly subsidised housing capital programme—to put it into areas where you cannot do it at market rents just seems wrong.
Sir Bob Kerslake: But the percentage in those areas is much, much smaller—

Q124 Chair: But you did it.
Sir Bob Kerslake: That was because if you go to those areas, you will see that they do have defined specific needs in relation to affordable housing, which could be to do with changes in the stock. It is simply not the case to say that because of their particular market situation on housing, they do not need any allowance for affordable housing at all. If nothing else, there are things like special needs housing as well.

Q125 Chair: I just wanted to ask about several areas that we have not covered. In the Report, on page 27, it says that 51% of the schemes under this very limited scheme are either indicative or provisional, which means that either you have not bought the land, or you are not sure that you are going to be able to deliver.
Pat Ritchie: As it is a four-year programme, we ask providers to come forward with bids that would be across that whole four-year programme. By its nature, that means that some of the schemes within the programme are indicative. We have been doing

reviews with all providers since the end of the year to firm up the schemes and to move them from indicative to firm schemes. We have quite a bit of flexibility within this programme to be able to move sites around, so if a private provider is not able to deliver on a specific site that was identified when the bid was first made, there is the ability within the programme to shift to firmed-up sites.

There is also the provision to move around between providers, so if one provider is not delivering because they have not been able to firm up the sites that were originally indicative in their bid, we can move within the programme to other providers in order to deliver overall. That is combined with very close working between the HCA's local teams and local providers and local authorities to free up issues around planning permission, infrastructure or some of the other issues that might be constraining the sites from becoming fully viable.

Sir Bob Kerslake: May I add a couple of points to that? First, this is not a new phenomenon. It has been the case on programmes in the past. There have always been things to tie down, on individual schemes, two or three years ahead. That has always been part of the way that the programme works, and there is flexibility, as Pat says, to deliver it. If you look at the track record over quite a long period of time, the HCA, and the Housing Corporation before that, has delivered on its numbers.

Q126 Chair: But this is a huge bias towards the final year—50% in the final year.

Sir Bob Kerslake: The numbers have come forward from that.

Pat Ritchie: We have moved 6,500 into earlier years—in the HCA part of the programme only—so that reduces the numbers in the final year. We will look at whether, subject to the availability of funding, we can do anything more around that. As was indicated earlier, we paid 75% start on sites in the new programme in the first year to get the programme moving. We can look at whether or not we need to do that to incentivise the programme, but that is subject to the availability of money as well.

Sir Bob Kerslake: Again, with a start-up programme, it is not surprising that the highest proportion of delivery comes in the final years. It is absolutely a part of the way we work.

Q127 Chair: If you pay 75% upfront, does that not constrain your flexibility?

Pat Ritchie: It may do, and that would be something that we would need to look at when we do the individual reviews with providers of the programme. We would take a view on that once we have gone through the review process that we are undertaking at the moment.

Q128 Chair: Would you take money back off them?

Pat Ritchie: We will certainly shift money around if providers are not delivering.

Q129 Chair: But would you take money back off them? You give them 75% upfront, and they run into problems for their programme. What do you do then if you decide you want to shift the money to another provider in another area?

Pat Ritchie: We pay the 75% when they have made a start on site. So when they have actually started work on the ground, we pay the 75%. We do not pay the 25% until it is certificated that the house is finished. There may be some delays to that, but the incentives are to finish off the unit that has been started.

Q130 Chair: Has the pressure on quantity had an impact on quality?

Pat Ritchie: As part of the assessment process, we looked at the design and space standards of each of the offers in order to get a programme that reflected our quality standards. That was one of the things we took into account when we were looking at the offers and proposals.

Q131 Chair: Finally, on the new system that you have, where the housing benefit is paid to the tenant and not the provider, I know from experience in this world that that will invariably lead to difficulties, particularly for housing associations more than local authorities. What are you trying to do to mitigate that?

Sir Bob Kerslake: It is a big change, and a significant part of the changes around universal credit, as you know. Because it is a big change, and because housing associations have raised some concerns about it, we are doing four demonstration projects to test the impact. Those are under way now, and we will be able to learn from them what the impact is, particularly on rent arrears and speed of payment, which is where the main risk would be.

Q132 Chair: What action can you take to mitigate it?

Sir Bob Kerslake: There are actions you can take, but we need to see the actual projects first.

Q133 Mr Bacon: Can I just explore what you mean? You are doing these pilot projects before it is brought in elsewhere.

Sir Bob Kerslake: We are doing these pilot projects to test the impact of it before it is brought in. As you know, the change comes in, or is planned to come in, on a rolling basis from October 2013, as you move people over to universal credit. That is when the change happens, and it runs from October 2013 through to 2017.

Different client groups will come into universal credit, and therefore, under the current plans, they will be subject to direct payment. We are now running four demonstration projects ahead of that, with the co-operation of the housing associations and local authorities, in order to test what the impact of moving to direct payments has on the timeliness of payment and arrears.

Q134 Mr Bacon: It is not going to make it better. It is going to erode the timeliness of payments to some extent.

Sir Bob Kerslake: It will have some impact, but we need to see how great the impact is and then form a judgment. There are things you can influence that will help in the way this works—for example, how long you allow for arrears to build up before you switch back to the old system, and things like that.

Q135 Mr Bacon: This is an issue that my local housing association—the most important one in my area—has raised repeatedly with me. One concern they have is about the relationship with pensioners, for whom the situation is not really going to change. Their income will not change, and it is clear how their rent will get financed. A very significant percentage of the total falls into this category. It is, for many people, just one more thing to worry about; instead of, previously, having one payment, they will have a whole series of several thousand payments, which will inherently increase the cost. It is not obvious what the benefit is.
Sir Bob Kerslake: You will know that it is a direct goal of the Government to move towards this model. Part of its intention is that people are aware of the full costs, including rent—that is why it is being done. We shall see how much—

Q136 Mr Bacon: But it is meant to alter behaviour, isn't it?
Sir Bob Kerslake: My sense is that it is most likely to be the case that those, such as pensioners, will find that they will be able to manage it, but we shall have to see through the pilots.
Mr Bacon: Sorry; could you speak up?
Sir Bob Kerslake: I am saying that I think for the people with constant incomes and known costs, this ought to be something that they can predict and manage in the same way as they do now, but we need to test through the demonstration projects what the impact is. Until we have done that, it is hard to give you a view on that.
Chair: Good. Anything else? Austin, one more—go on.

Q137 Austin Mitchell: Paragraph 2.6 states that the Department, in its impact assessment, "analysed the cost to all tenants, including those who would not have all their rent paid by housing benefit, but the published analysis did not explicitly refer to the number of tenants in this group who would be affected or by how much." Why was that?
Sir Bob Kerslake: I think we did as much analysis as we could on this and we have published the information we had, so we have not held back any information from the NAO or anybody else on this issue. As I said earlier, it is very hard to form a judgment about the impact, because it depends on who gets allocated to the property, so that is why it is—

Q138 Austin Mitchell: But it was not a figure that would have frightened people.
Sir Bob Kerslake: I do not think that there is any evidence of a problem of a figure that would frighten people, no.
Chair: Good. That was a nice brief one. Thank you very much, indeed.

Written evidence

Written evidence from L&Q

Throughout 2011–12 the average age of purchasers across all shared Ownership sales was 33 years. Incomes are recorded by first applicant, second applicant (where applicable) and household total. For this period the average income of the first purchaser for sales was £30,329 and the average household income was £37,289. Average Household savings was £15,576. This covers both new sales and re-sales of existing shared ownership properties.

For all purchasers, we record their previous living status. The following are the results for 11–12:

Living Status	*New Sales %*	*Re-sales %*
Local Authority	1.1	2.27
Housing Association	1.65	4.55
Friends & Family	31.8	40.91
Renting Privately	62	52.27
Other	2.75	0

Allocations

We are required to prioritise to those people whom local authorities would like to see us sell to and these requirements differ from one LA to the next.

Our allocations policy explains that, along with other criteria, applicants will normally be offered a home with up to one bedroom over and above their current need. This eliminates any situations of smaller families being allocated larger homes. Attached is a copy of the Allocations policy for information.

Allocation of shared ownership homes in London is guided by the Mayors London Housing Strategy and promoted through the First Steps HomeBuy Agency service. This sets an upper income limit of £64,300 for households requiring one and two bed properties and a limit of £77,200 for families requiring three beds and larger. Underneath this Local Authorities will set additional eligibility criteria based on a range of criteria such as housing need, affordability and local connection. Existing social tenants have the highest priority for shared ownership properties, as this provides a pathway into ownership and frees up existing social homes.

Consequently, despite the higher upper income limits, in reality the vast majority of shared ownership sales go to households earning much less than this. We monitor this through our own records and targeting and also through the CORE (continuous recording of lettings and sales) which all Registered Providers are required to use to record data on who we let and sell our homes to. The CORE data for London in 2010–11 shows 2,691 shared ownership sales recorded with an average household income of £32,785. L&Q's own date for the same period shows an average household income of £37,289.

David Montague
Group Chief Executive

July 2012

Written evidence from the Department for Communities and Local Government

Thank you for a constructive discussion about our work on the Affordable Homes Programme at the hearing on 9 July. I committed to providing further information on Affordable Rent levels in comparison to other rented tenures.

The Affordable Homes Programme Framework document sets out the expectation the Homes and Communities Agency (HCA) has of providers seeking funding under the scheme. It makes clear that providers are able to let a property at an Affordable Rent (inclusive of service charges, where applicable) of up to 80% of the gross market rent which reflects the property size and location. The maximum rent level for Affordable Rent should be assessed according to the individual characteristics of the property. Landlords are required to assess the gross market rent that the individual property would achieve and set the initial rent (inclusive of service charges) at up to 80% of that level, using approved RICS valuation methods.

Table 1

COMPARING WEEKLY RENT LEVELS

Average weekly rent	*Affordable Rent (2011–15 AHP allocations)*	*Market Rent (of comparable properties)*	*Affordable rent as %age of market rent*
London	£182	£280	£65%
England	**£133**	**£182**	**73%**

Affordable rent figures above are based on the rents successful bidders to the Affordable Homes Programme proposed to charge, with the market rent figures based on these providers' estimates of how much the rent on the same properties would be if let at market rates.

To put the above figures in context, the average social rent charged on new properties built in London under the previous National Affordable Homes Programme was £108 a week.

Table 2

PROPORTION OF NEW AFFORDABLE RENT SUPPLY HOMES OFFERED AT LESS THAN 80% MARKET RENT

	Less than 80%	***80%***
London	95%	5%
England	**37%**	**63%**

We would normally expect Affordable Rent tenants would otherwise have been housed more expensively in the private rented sector; by taking an Affordable Rent property they are less dependent on the State for revenue support, increasing their incentive to work. Where appropriate, Affordable Rent tenants are eligible for housing benefit up to the full value of the rent, subject to any deductions such as the social sector size criteria and the overall benefit cap. The National Planning Policy Framework is clear Affordable Rented housing is a form of social housing in the same way as social rent and existing allocations procedures apply. Local authorities have considerable discretion in this area.

Yours sincerely
Sir Bob Kerslake
Permanent Secretary

23 July 2012

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