ROTHERHAM BOROUGH COUNCIL – REPORT TO MEMBERS

1.	**Meeting**	**Cabinet Member for Safe and Attractive Neighbourhoods**
2.	**Date**	**28th May 2012**
3.	**Title**	**Changes to the Right to Buy**
4.	**Directorate**	**Neighbourhoods and Adult Services**

5. Summary

Government published the details of the 'reinvigorated Right to Buy' (RTB) on 12th March 2012 and the new scheme was implemented from 3rd April 2012. The two main changes are the increase to the discount cap from £24k to £75k, and the treatment of RTB capital receipts. Based on the average market value and average length of tenancy in Rotherham, a tenant can expect a £12k increase to the discount they would be entitled to under the RTB. We anticipate a large increase in the volume of queries and applications, and an increase in RTB sales. The Government intends 'one for one' replacement by diverting a larger proportion of the capital receipt to delivering new housing, but this ratio will not be achieved in Rotherham based purely on RTB receipts.

This report sets out the implications for tenants and for RMBC in more detail.

6. Recommendations

that Cabinet Member is asked to:

- Agree that a Members' seminar should be held to discuss the changes in detail.
- Note that a workshop has been arranged for 30th May 2012 involving representatives from all RMBC services that will be affected by an increase in RTB applications and sales, to explore opportunities and threats, identify short and medium term actions and establish a clear monitoring process.
- Note that monthly monitoring information will be provided to Directorate Leadership Team.
- Note that further detailed financial modeling will be carried out, to enable us to understand the impact on the 30 year HRA business plan.
- Note that RMBC's website will be updated with accurate information about the new scheme.

7. Proposals and details

7.1 Introduction

CLG published the details of the reinvigorated Right to Buy (RTB) scheme on 12th March 2012 and the changes went live on 3rd April 2012. The two main changes are that the discount cap has been increased from £24k to £75k, and the way the capital receipts from sales are to be treated has changed, to support the delivery of new affordable housing.

7.2 £75k discount cap – what does this mean for tenants?

The formula for calculating discount RTB discount remains unchanged. Secure tenants of at least five years can apply to buy their Council house for a discount of 35% of the property's value plus 1% for each year beyond the qualifying period (five years) up to a maximum of 60%. (For flats: 50% plus 2% for each year beyond the qualifying period up to a maximum of 70%).

The average RTB house price in Rotherham is £80k, and the average length of a tenancy is 15 years. The following table sets out three scenarios to show the minimum, average and maximum impacts the new rules could have on discounts:

	Example to show min. impact	Example to show ave. impact	Example to show max. impact
Property value	£60,000	£80,000	£130,000
Length of tenancy	5 years	15 years	30+ years
% Discount	35%	45%	60%
Previous discount	£21,000	£24,000 (due to cap)	£24,000 (due to cap)
New discount	£21,000	£36,000	£75,000 (due to cap)
Increase in discount	0	£12,000	£51,000

It is useful to compare the costs to the tenant of owning as opposed to renting. A mortgage for £43,690 on 20 years at 3.5% would cost £312 per month in the first year (including a constant principal repayment of £188 per month – NB interest only would be much cheaper). This equates to approximately £74 per week, which is less than the current average rent for a two bedroom Council property (£77.51). The average rent for a three bedroom Council property is £92 per week. This is dependent however on a number of factors, including the ability to secure a mortgage for a long enough period (say 20 years, before or on 60th / 65th birthday), and the certainty of low interest rate for the first ten years.

7.3 Will this result in more RTB sales?

This is likely, but difficult to predict with any degree of accuracy. The RTB has been popular in Rotherham, with over 17,000 Council properties sold via this route since its introduction in 1980. Numbers have tailed off dramatically in recent years, from 972 in 2004/5, down to less than 25 units per year since 2008/09. Such low figures can be explained as follows:

- Low income (67% of Council tenants are in receipt of housing benefit) therefore people less able to access mortgages
- People not wanting to remain in their current property in the longer term
- People happy to continue to rent
- Difficulties in securing a mortgage and levels of deposits required
- Reluctance to commit to owner occupation in uncertain economic times
- Strict capping of RTB discount discouraged tenants to switch to homeownership

The increased discount may persuade those who would otherwise consider home ownership to be unaffordable to them, to enquire about RTB. While on the one hand the economic recession means that fewer people are in a position to save a deposit / access a mortgage, the low interest rates and recent rent increases may encourage people to respond to the 'reinvigorated' RTB offer. We anticipate that the groups that are more likely to respond are:

- 33% of tenants (c6900) who pay their full rent (although it should not be assumed that home ownership is unaffordable for people on benefits if the current interest rates are maintained and when the mortgage value is less than say £40k).
- Elderly tenants, who are entitled to the maximum 60% discount, whose relatives may wish to take advantage of the offer on their behalf.
- People who live in the highest value areas i.e. Whiston, Broom, Wentworth and other rural areas, where the discount increase is most dramatic.
- Companies and individuals who exploit the discount rules by offering cash incentives to council tenants on resale of their homes. The five year qualifying period may no longer be sufficient to deter these transactions.

We expect to see a rise in enquiries and applications. A proportion of these will result in sales, but we cannot predict the volume, therefore rigorous monthly monitoring is essential.

7.4 What does this mean for capital receipts?

Changes have been made to the way RTB receipts are treated, in order to allow more affordable housing to be built to replace the properties lost through RTB.

Previous treatment of income from RTB sales

Example to illustrate calculation:

- Gross capital receipt from a RTB sale: £60,000
- Less administrative costs: £1,000
- Less cost of improvements to property during preceding three years: £10,000
- Net receipt: £49,000
- 75% of which to Government: £36,750
- 25% of which to be retained by RMBC as 'residual receipt': £12,250

In practical terms RMBC has used this 25% share to fund private sector Disabled Facilities Grant improvements.

In preparing for RMBC's HRA self-financing settlement a number of assumptions were made in the business plan, including:

- 23 RTB sales per annum (based on recent experience)
- Based on the previous system, this would have yielded income to Government of £931,500 per annum and £310,500 per annum to RMBC. These figures have been kept as 'assumed income' targets under the new system, see below.

<u>New system</u>

The Government's intention is that once these income targets have been met each year (i.e. £931,500 to Government and £310,500 to RMBC), any additional receipts should be spent on new affordable homes to replace the additional units lost through the RTB.

Until the targets are met each year, the treatment of RTB sales is largely the same as before, with the following amendments:

- No deduction of cost of improvements during previous 3 year period (it is assumed that this will not be too problematic as Decent Homes ended in 2010)
- For all the properties over and above the assumed number of RTB sales, i.e. 23, we are permitted to deduct a figure that represents the amount of HRA debt attached to each property
- Provision to be made for 'buy-backs' of 6.5%

Taking the above into account, once a sufficient number of properties has been sold to reach the assumed income targets (£931,500 and £310,500), the receipts are treated as follows:

Gross capital receipt from a RTB sale after new discount applied	£43,690
Less administrative costs	-£1,300
Less cost of average debt in HRA settlement per property	-£15,735
Less buy-back provision	-£1733
Net receipt to be spent on re-provision of affordable homes	c£24,922

In summary, until we have reached the assumed income targets, the treatment of capital receipts will be largely the same as before (75% / 25% split) and there will be no additional resources to fund new affordable homes. The number of homes sold before the new treatment is triggered is predicted to be 34, due to the increased discounts. Once this has been reached, i.e. in simple terms from the 35th property sold onwards, the residual receipt to invest in new homes will be in the region of **£25k per property**.

7.5 Will we be able to deliver more affordable homes?

The Government's intention is that the new RTB will see 'no reduction in the number of affordable homes, with any additional homes bought under the scheme leading directly to the provision of new affordable homes for rent'. Detailed modeling has been carried out and the 1:1 replacement target will not be achieved in Rotherham based purely on RTB receipts.

It is assumed that a new build property would cost £114,700 (based on a three bed house at SY Design standard meeting Code Level 4 Sustainable Homes and a number of other assumptions). Government states that no more than 30% of the cost is to be funded by the RTB receipt, explained as follows:

"Drawing on evidence from the 2011-2015 Affordable Homes Programme – for which most agreements have now been signed - we are clear that that it should be possible to fund new homes let at Affordable Rent levels, with no more than 30% of the cost of the new homes needing to come from the Right to Buy receipt. As in the Affordable Homes Programme, the remainder of the cost will come from borrowing against the net rental income stream from the new property, and cross-subsidy from the landlord's own resources, including (in some cases) land.

As we set out in our consultation paper, our aim is to deliver one-for-one replacement nationally. We recognise that the remaining receipt will not be large enough to fund one-for-one replacement in some areas, and we are not requiring councils to do so. If a council wishes to retain the remaining receipt, all it must do is spend that receipt on new affordable rented homes, making sure that no more than 30% of the cost of the new homes comes from the Right to Buy receipt. It can provide the new homes itself, or contract with another social housing provider".

30% of the cost is £34,410 and we therefore take this to be the assumed cost of a replacement home.

As shown in section 7.4, for the first 34 homes sold each year there will be no additional resources for new affordable housing. Once the new rules are 'triggered' we can expect to receive in the region of £25,000 per property to spend on new housing, which is approaching the £34,410 required to fund 30% of total new build cost ('one for one' provision). However, the first 34 homes lost each year are not replaced. We had previously not assumed replacement of the 23 homes we expected to sell, therefore we could argue this is an additional loss of 11 homes (34 minus 23) per annum.

In summary, based on RTB receipts, we will be able to deliver new affordable homes if we sell more than 34 units per year, but not enough to replace the number sold, over and above the level we expected, due to the increased discounts. However, in order to deliver the replacement we would need to borrow an estimated £91k per property.

Conversely, if we sell *less* than 34 properties, the assumed income targets to Government and RMBC will not be met and the implications of this are currently being explored.

We are in the process of developing a local authority new housing programme, which will identify additional sources of finance to deliver new Council housing and replace the stock lost through increased RTB sales.

<u>Two final points:</u>

The amount of HRA-owned land on which we could build Council new build homes is also limited, and a detailed local authority new housing strategy will be required to address these issues and ensure all available routes to delivering new affordable housing are explored.

All LANB homes (built since 2008) will be excluded from the revised RTB scheme under the 'cost floor' rule for 15 years. (The cost floor means that properties could not be sold for less than they cost to build). Government acknowledges that "without these changes, we recognise there could be a financial disincentive for local authorities to provide new affordable rented homes in future".

7.6 Implications for the HRA business plan

The impact of the new RTB scheme in the first year of the 30 year HRA business plan is summarised as follows:

	Number of sales			
Impact on the business (in 1 Year)	**50**	**100**	**500**	**1,000**
Loss of Income in the first year (£)	88,128	251,328	1,556,928	3,188,928
Less costs incurred per year per property (£)	-60,318	-172,018	-1,065,618	-2,182,618
Loss of Annual Surplus (£)	27,810	79,310	491,310	1,006,310

Further modelling will need to be carried out to show the detailed implications.

7.7 Providing information to tenants about the Right to Buy

We are in the process of developing a new information sheet for tenants to be accessible via the Council's website, and to be provided to all applicants. This will reflect the position in Rotherham and will contain useful information about costs and affordability.

8. Finance

- The changes to the treatment of capital receipts and implications for building new homes are set out in 7.4 and 7.5.
- Implications for the HRA business plan have been briefly summarised in 7.6 and further detailed modelling will need to be carried out. The impact on the HRA business plan will vary enormously depending on the number of RTB sales and this will need to be monitored on a regular basis.
- An additional point to note is the potential increase in staffing resources that will be required if there is a large volume of calls and applications. Initially this can be managed within the Contact Centre but a meeting will be needed to consider other areas such as valuation and legal services.

9. Risks and uncertainties

The list below is not exhaustive and a workshop will be held with all affected services to explore the risks and opportunities in more detail.

Risk / uncertainty	**Suggested action**
We do not know how many additional RTB sales to expect. The impact on the HRA business plan will vary enormously depending on the number of RTBs, as will the pressure on existing resources.	The increase in the volume of queries and applications should be monitored from April 2012 onwards to allow us to make projections and the staffing resources required should be reviewed on an ongoing basis.
There is a risk that RMBC would not meet its	It is recommended that we upload

Risk / uncertainty	Suggested action
legal duty to advise tenants of their extended RTB rights, if we do not communicate the new scheme.	information on the RMBC website and provide staff with a clear briefing and updated scripts. Debt management advice will be provided to tenants to inform on the financial risks that homeownership entails for people on low income (mortgage repayment, maintenance and repairs).
We may not be able to replace the number of units sold, resulting in a loss of Council stock, and income through rents received, at a time when the need and ambition for more new Council housing is higher than ever.	Review local authority new housing strategy to ensure every opportunity is explored to deliver new Council build and enable other affordable housing delivery in the borough.
Existing problems with the RTB process will be magnified if the volume increases, for example recovery of service charges.	Meeting with all services involved to identify lessons and improve the end to end process (arranged for 30th May 2012).
People may exercise their RTB in response to the increased discount, and find themselves in unaffordable home ownership.	Ensure clear information is provided and detailed affordability assessments carried out. Debt management advice will be provided to tenants to inform on the financial risks that homeownership entails for people on low income (mortgage repayment, maintenance and repairs).
In Rotherham, RTB receipts have been used to top up the Disabled Facilities Grant, and if we divert new receipts for replacement homes there will be an impact on private sector aids and adaptations.	The increase in the volume of queries and applications should be monitored from April 2012 onwards to allow us to make projections and quantify this impact.
There is a risk of unscrupulous landlords and mortgage companies taking advantage of the increased discount by targeting council tenants and persuading them to take up the Right to Buy, when they are not in a position to afford this. The Government does not intend to make any legislative changes to the Right to Buy to require financial checks or limit purchase with family members although plans to 'keep the potential for any abuses under continual review'.	This will be addressed by including additional information sheets in the advisory information issued to RTB applicants.
It is possible that older residents with long tenancies (50+ years in many cases) may submit the RTB, to take advantage of the	This will be addressed by including additional information sheets in the advisory information issued to RTB

Risk / uncertainty	Suggested action
enhanced discount, for the benefit of their children. This could lead to an increase in the following scenario, which we understand already occurs, albeit anecdotally. -A long standing tenant exercises their RTB, the tenant is retired and has no income so although the deeds for the property appear in the tenant's name (as RTB rules dictate) the property's mortgage is in the name of, and paid by, a younger relative. -The elderly tenant's health deteriorates and they need substantial care. -When the elderly tenants dies the state seeks to recoup care costs from the estate which can cause issues with the relative who has paid the mortgage.	applicants.

Finally, Legal Services have advised that the new legislation states that any currently active application (including any applications with legal for completion) needs to take into account the changes in discount amounts. To this effect it is necessary for Legal to re-issue S125 valuation letters to all active applications where we have already sent letters out. It is estimated that there are approximately 25 valid applications. This may result in increased discount for these applicants and therefore reduced capital receipts to RMBC.

10. Background papers and consultation

- Previous reports to DLT and Overview and Scrutiny Management Board (27th January 2012) presenting RMBC's response to Government consultation
- Reinvigorating the Right to Buy and One for One Replacement – CLG website
- Marketing posters, leaflets and letter templates provided by CLG in April 2012

Consultation: RotherFed were consulted on RMBC's response to the original consultation. Corporate Finance have been engaged in the production of this report.

11. Contact details

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