The Affordable Rent Model

Registered Social Landlords (RSLs) have recently begun bidding for part-funding to build homes under a new model of housing finance known as the Affordable Rent Model (ARM). The model allows social landlords to charge new tenants up to 80 per cent of local market rents to help fund new building and the government believes the plan will enable 150,000 homes to be built between 2011 and 2014. This briefing explains the principles and mechanisms of the ARM and its implications for the supply of affordable homes in the capital.

Overview

First unveiled in the October 2010 Spending Review and formally launched in February 2011, the government's Affordable Rent Model (ARM) offers social landlords access to £1.8 billion of Homes and Communities Agency (HCA) funding over the next four years. Landlords bidding for grant funding under the scheme are expected to part finance developments and will be allowed to charge higher rents for the new housing, at up to 80 per cent of local market levels. The model also expects RSLs to charge higher "affordable" rents on a proportion of existing homes when they become empty.

The ARM is being introduced against the backdrop of a huge reduction in grant funding to supply affordable housing. To put this in context, the previous Comprehensive Spending Review (CSR) 2008-11 allocated £8.5 billion to fund new affordable housing through the National Affordable Housing programme, with a target of 155,000 new homes. The latest CSR (2011-15) has allocated £4.5 billion (of which £2.2 billion has already been committed) to fund a similar target of 150,000 new affordable homes. The grant element (which has to be topped up with increased rents and loans) attributes just £30,000 per housing unit, compared to the previous sum of £115,000 per unit in London.

The underlying principle behind the ARM is that, at a time when less public subsidy is available, allowing landlords the flexibility to generate additional rental income will provide money to invest in building new homes.

The London context

London's housing supply and affordability crisis is well documented, with 36,000 households in temporary accommodation and more than 350,000 Londoners on council waiting lists. It is anticipated that this situation will be exacerbated by changes to the housing benefit system, including rent caps, potentially making parts of the capital unaffordable for those currently in the private rented sector.

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Based on its current commitments, the HCA expects to be on target to deliver 150,000 homes nationally in 2010/11. But new starts are expected to drop in 2011/12 with the number of planned completions falling dramatically in 2012/13, unless the ARM proves it can deliver new homes.

The Mayor's draft replacement London Plan set an ambitious target to deliver an estimated 32,210 homes across the capital annually, of which 13,200 should be at the affordable rate. There is a commitment in the London Plan that 30 per cent of this total will be family-sized homes. The Mayor will be responsible for housing investment in London and funding new supply from RSLs after April 2012.

London's local authorities are currently looking at evidence for affordability at different levels and bedroom sizes, but there is already a widespread recognition that the ARM will fail to deliver on larger sized family properties; and that, at 80 per cent of market rates, the model's maximum rent level will be unaffordable in the capital.

Key features of the ARM

On 14 February 2011 the HCA published the Affordable Homes Framework prospectus setting out the new bidding process guiding investment for 2011- 2015.

The HCA is seeking bids direct from RSLs that, unlike previous development bids, will establish a four-year contract based on the RSL's business plan. The HCA is looking for schemes that deliver strong value for money with a mixture of tenure that includes affordable rent and shared ownership properties. Importantly, bids must show evidence that the proposed development will meet local housing need as identified by the local authority. This approach will require RSLs to work closely with their local authority partners and develop a good understanding of local borough needs.

Key features of the Affordable Rent Model include the following:

- RSLs will be able to charge up to 80 per cent of market rent for new homes built under a much reduced grant regime
- The cost of new homes can be supplemented by receipts from property disposals and existing empty stock re-let at a higher 'new affordable rent' level
- There is a presumption that RSLs will be supported/supplemented with funding from local authorities using the New Homes Bonus[1], or using free or discounted local authority land
- 'Flexible' tenancies (the minimum period would be two years) are expected to apply to all new affordable rental properties or re-lets. However, tenancy strategies should be aligned with a borough and providers can offer lifetime tenancies should they wish to do so
- At the end of the affordable rent tenancy, providers and their tenant may choose to convert it to shared ownership
- Local authorities will also be allowed to bid for funds to build new homes using the ARM once the new self financing system for housing is implemented in April 2012.[2]

The closing date for bids to the HCA is 3 May 2011, with assessment and negotiation of offers taking place over May and June. The HCA London Board expects to approve the bids by early July 2011.

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[1] The New Homes Bonus (confirmed by the government on 17 February 2011) is intended to incentivise the building of new homes by rewarding local authorities for each new home built for a period of six years. Funding for the scheme will come from a central government pot and from relocated money from formula grant.
[2] This will replace the Housing Revenue Account (HRA) system, a separate London Councils briefing on this topic will be sent to members shortly.

Implications for London

London Councils has expressed concerns about the practical operation of the model, the lower number of units it will deliver and the extent to which it will address the housing needs of existing tenants and homeless households.

Key areas of concern include:

- the ability to secure the required number of homes London needs
- the ability to deliver family homes in London
- unaffordable rents for low income working households in some parts of London creating a benefit trap, particularly in three bedroom and larger homes.
- the impact of Universal Credit caps on high rent areas and families
- the potential for the income generated by the conversion of re-lets and disposals to be used outside London for new build elsewhere
- the very nature of the ARM will lead to a situation in London where developments will attract less grant funding on the basis that local rents can make up any grant deficit and be an alternative source of funding
- the long term cumulative shrinkage of available social affordable rented property in London (that is, below market rent and the new affordable rent levels)
- housing allocations will be driven by the overall cost per unit, which is high in London - the difference between existing market and social rents being greater in London
- there will be a built-in incentive in the model for RSLs to maximise an increase in rental income through the re-letting of property, especially in high rent areas
- there will be a lack of incentive for households on lower rents to transfer into homes at a substantially higher rent level
- lower overall supply will lead to a lower level of nominations that boroughs will be able to take up, this will impact on the management of homeless and high priority housing needs cases.

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Maximising the number of new homes

In a recent London Councils survey, more than half of London boroughs reported that RSLs expected fewer homes would be delivered via the ARM. This will result in fewer properties being available for applicants on boroughs’ housing registers, including homeless households.

To maximise the supply of new homes in the capital London Councils will continue to:

- work closely with the HCA and Greater London Authority on the development and roll-out of the ARM
- explore if there is scope and appetite for boroughs to exploit borough resources, such as HRA surpluses, in a devolved commissioning approach working with RSL partners
- continue to work with RSLs and local authorities and engage in proactive dialogue with each other to secure the best possible bids for the benefit of London.

The focus of our work will be to:

- encourage the devolved delivery of the ARM in a way that works both for London, individual boroughs and RSLs
- maximise the number of larger units provided
- maximise the level of borough leverage (on scheme profile, rent levels, tenure approach).

Commentary

The proposals contained within the Welfare Reform Bill[3] (published on 17 February 2010) could significantly impact on the number of new homes, particularly larger-sized properties, the ARM can deliver in the capital. While it is hoped that the Universal Credit proposals will simplify the existing benefit regime the proposed total benefit cap of £26,000 (this would include all living and housing expenses) that will be introduced from 2013 for all new claimants will fall far short of current private sector rent levels and RSL affordable rent levels in many instances in London.

Research commissioned by London Councils confirms that the majority of private landlords in London are unlikely to reduce their rents, resulting in families in high cost areas having potentially to move to cheaper areas in London, or out of London.

Equally, in order to fund the contribution of new homes, RSLs will be placed in a position in many instances where the rent they will charge will exceed the £26,000 universal credit cap.

London Councils is hosting a joint event with the National Housing Federation looking at Challenges and Solutions for London's Housing on 14 April 2011. The event is free and a limited number of places are still available for interested members. For more details or to book a place, click on the link below.

[3] See London Councils Member Briefing No.02 for more information on the Welfare Reform Bill

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Links:

Homes and Communities Agency (HCA)

The Mayor of London's London Plan (GLA website)

Welfare Reform Bill (DWP website)

Survey of London landlords (London Councils' research)

Challenges and Solutions for London's Housing (Event)

This member briefing has been circulated to:

Portfolio holders and those members who requested policy briefings in the following categories: Housing