Social rents policy: choices and trade-offs

5 November 2015
Policy background and trade-offs

Robert Joyce
% of population living in social housing (GB)

Source: Figure 2.1 of Social rent policy: choices and trade-offs
Social tenants are a relatively poor group

% of GB average

Source: Figure 2.2 of *Social rent policy: choices and trade-offs*
Who lives in social housing?

<table>
<thead>
<tr>
<th></th>
<th>Social renters</th>
<th>Whole population</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Age</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Under 16</td>
<td>24.3%</td>
<td>18.4%</td>
</tr>
<tr>
<td>16–64</td>
<td>59.9%</td>
<td>64.4%</td>
</tr>
<tr>
<td>65 plus</td>
<td>15.8%</td>
<td>17.1%</td>
</tr>
<tr>
<td><strong>Graduate (aged 25–64)</strong></td>
<td>8.2%</td>
<td>29.0%</td>
</tr>
<tr>
<td><strong>Receiving disability benefits (aged 16–64)</strong></td>
<td>17.6%</td>
<td>6.1%</td>
</tr>
</tbody>
</table>

Source: Table 2.1 of *Social rent policy: choices and trade-offs*
We focus on choice over level of rent they pay

• Social housing providers combine at least three functions:
  – Construction
  – Landlords
  – Sub-market rents

• We focus only on rents
  – Taking rest of social housing system as given
  – But rent changes can have knock-on effects on (e.g.) construction, which we discuss

• Analyse effects of big changes to social rent policy in England
  – ‘Affordable Rents’ (i.e. higher rents) for new tenancies
  – 1% annual cuts in social rents for next four years
  – ‘Pay to Stay’: market or near market rents for higher-income tenants
Rents in social housing

• Tightly constrained by central regulations

• Since early 2000s, each social property has a ‘formula rent’
  – Depends on capital value, local earnings levels and property size
  – Has increased in real terms each year
  – Properties below formula rent had to gradually move towards it
  – Central aim was to achieve ‘convergence’ between council and HA rents – process now largely complete

• Now, centrally-imposed constraints on most rents are:
  – Cannot be more than 5% above formula rent
  – Maximum annual rent increases for a given property
## Mean weekly rents, 2015

<table>
<thead>
<tr>
<th>Region</th>
<th>Private rented sector</th>
<th>Social rented sector</th>
<th>Estimated market rent on social properties</th>
<th>Estimated social rent subsidy</th>
<th>Estimated social rent subsidy (% of market rent)</th>
</tr>
</thead>
<tbody>
<tr>
<td>England</td>
<td>£172</td>
<td>£96</td>
<td>£136</td>
<td>£40</td>
<td>29%</td>
</tr>
<tr>
<td>North East</td>
<td>£118</td>
<td>£81</td>
<td>£99</td>
<td>£18</td>
<td>18%</td>
</tr>
<tr>
<td>London</td>
<td>£267</td>
<td>£123</td>
<td>£191</td>
<td>£68</td>
<td>36%</td>
</tr>
<tr>
<td>South East</td>
<td>£177</td>
<td>£107</td>
<td>£166</td>
<td>£59</td>
<td>36%</td>
</tr>
</tbody>
</table>

Source: Table 2.2 of *Social rent policy: choices and trade-offs*
Social rent subsidies: how are they financed?

• Social landlords are not-for-profit

• Can cover their costs at below-market rents because:
  – Construction was subsidised by central govt (so lower debt)
  – Much of stock old enough that debt paid off
  – Market rents have risen faster than landlords’ costs

• So despite many years of real increases in social rents, gap between social and market rents remains substantial
Housing benefit (HB) for social tenants

• 2/3 of social tenants receive further rent subsidy in form of HB
• HB entitlement is means-tested against current income and assets
• For poorest, it typically covers all rent. Exceptions:
  – Those affected by social sector size criteria (‘bedroom tax’): covers 75% or 86% of rent
  – Those affected by benefit cap

• HB will rise to fully cover a rent increase
  – Or fall to offset the gain to a tenant from a rent reduction
  – Only exceptions are those affected by benefit cap or ‘bedroom tax’
Raising social rent levels: impacts on households

• If not on HB, makes social tenants worse off
• If on HB, most tenants no worse off – HB rises to cover rent rise
• Work incentives typically weakened: more reliance on HB, eligibility for which depends on having low income

• Higher rents also make being in social housing less attractive
  – Weakens incentive to gain access to social housing in first place
  – Weakens incentive for existing tenants to stay in sector (e.g. rather than move for job opportunity or take up Right to Buy)

• These incentive effects could (though will not necessarily) affect people’s choices over work and housing tenure
Raising social rent levels: impacts on central government and housing providers

• Higher rents mean higher HB spending by central government...
• ...but more income for social landlords
  – As not-for-profits, that should get re-invested in housing
  – New construction, extra maintenance or management services, etc

• These indirect effects likely to offset some of overnight impacts
  – e.g. more construction $\rightarrow$ social housing extended to more people $\rightarrow$ more people get subsidised rents

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Social rent policy: choices and trade-offs

Stuart Adam, Daniel Chandler, Andrew Hood and Robert Joyce
Quantifying the effects of changing social rents

Andrew Hood
Data

- **Family Resources Survey**
  - Representative survey of 20,000 households
  - Records incomes, rents and other characteristics
  - We pool last four years of data to give us sufficient sample size (11,000 social tenant households in England, 1,800 in London)
  - Monetary values uprated to 2015-16 levels

- For some of the analysis, need estimates of the market rents that could be charged on properties of social renters in survey
  - We draw on estimates from Wilcox (2008)
Estimates of the direct rent subsidy

• Direct rent subsidy: difference between social rent and market rent that could be charged on that property

• Wilcox (2008) estimates average subsidy provided to social tenants
  – By region, landlord type (LA vs. HA) and number of bedrooms
  – Our key assumption that subsidy unchanged since 2007-08 as % of market rents

• These estimates are the best available to our knowledge
  – Figures on effects of cut in social rents not affected by any error
  – Any error will affect figures for Pay to Stay (and increasing social rents to 80% of market rents), but broad conclusions unlikely to be affected
Measuring net incomes

• Use IFS tax and benefit microsimulation model (TAXBEN) to calculate tax liabilities, benefit entitlements and net incomes

• Our modelling assumes full take up of means-tested benefits, including housing benefit (HB)
  – 12% of social tenants entitled to HB don’t claim

• For distributional and work incentive analysis, add direct rent subsidy to income
  – Treats HB and the direct rent subsidy the same
  – Captures the fact that the subsidy increases living standards, giving social tenants more to spend on other things
The effect of housing benefit on work incentives

Out of work

Weaker incentive to increase earnings

In work

Weekly housing benefit entitlement

£120

£100

£80

£60

£40

£20

£0

£0

£50

£100

£150

£200

£250

£300

Weekly income

Note: shown for single adult with weekly rents of £100 and £88, not subject to social sector size criteria
The impact of changing social rents

Weekly housing benefit entitlement vs. Weekly income

- **Before rent cut**
- **After rent cut**

**Out of work**
- No longer any housing benefit to lose

**In work**

Note: shown for single adult with weekly rents of £100 and £88, not subject to social sector size criteria
Two kinds of financial work incentive

1. The incentive to be in paid work at all
   - Replacement rate (RR): out-of-work income / in-work income
   - Participation tax rate (PTR): proportion of total earnings taken in tax and withdrawn in benefits

2. The incentive for those in work to increase their earnings
   - Effective marginal tax rate (EMTR): proportion of an extra £1 of earnings taken in tax and withdrawn benefits

• In all cases, higher numbers mean weaker work incentives
Cutting social rents by 1% a year for 4 years from 2016-17

- July 2015 Budget announced that social rents in England will be cut by 1% in cash terms for four years from 2016-17
  - 12% cut relative to previous plans (CPI + 1%)

- Average fall of £600 in annual rents for 3.9m households relative to previous plans
  - £2.3bn fall in rental income for social landlords

- Reduction in rental income could reduce new housing supply...
- ...as could uncertainty caused by U-turn on previous commitment
  - OBR assumes 14,000 fewer social homes by 2020 as a result
Impact on social tenants’ net-of-rent incomes

• Cut in social rents largely represents a transfer from social landlords to central government, rather than to social tenants
  – Housing benefit spending reduced by £1.7bn
  – Net-of-rent incomes up £700m: 1.6m gain average of £420 per year
Impact of a 12% rent cut by overall income decile

Source: Figure 4.1 of *Social rent policy: choices and trade-offs*
Impact on tenants’ work incentives

• Strengthens work incentives on average
  – Less housing benefit to lose by moving into work or increasing earnings

<table>
<thead>
<tr>
<th>Change in average:</th>
<th>12% cut in social rents</th>
<th>1p off all rates of income tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>Replacement rate</td>
<td>-0.3</td>
<td>-0.1</td>
</tr>
<tr>
<td>Participation tax rate</td>
<td>-0.9</td>
<td>-0.2</td>
</tr>
<tr>
<td>Effective marginal tax rate</td>
<td>-0.9</td>
<td>-0.6</td>
</tr>
</tbody>
</table>

• Size of impact on work incentives varies significantly by family type
Raising social rents to 80% of market rents

• Under ‘Affordable Rent’ model, rents on some new tenancies can be set at up to 80% of market rents
  – We look at impact of raising all social rents to that level

• Big difference in impact across regions: rents up by average of 41% in London, but only 14% in the North East
  – Would also be large variation within regions

• Among losers, those in London would lose average of £1,600 per year, compared to £317 in the North East
  – Weakening of work incentives correspondingly larger in London
Pay to Stay

• From 2017-18, social landlords required to charge tenants with incomes over £30,000 (£40,000 in London) market or ‘near market’ rents
  – LAs have to return additional income to Treasury; HAs can keep it

• We expect Pay to Stay to affect 250,000 social tenant households
  – Highest-income 7%
  – 80% of whom are in the top half of the overall income distribution

• Government currently consulting on precisely how social rents should increase as income rise beyond Pay to Stay threshold
  – Matters for impact on revenues, incomes and work incentives
Pay to Stay: direct rent subsidy by income

Annual direct rent subsidy

Cliff edge 50% taper 20% taper

150k people - mean EMTR 85%
300k people - mean EMTR 56%

Source: Figure 4.3 of Social rent policy: choices and trade-offs
The benefit cap and social rent changes

• From April 2016, total benefit receipt for most non-working families limited to £23,000 in London and £20,000 elsewhere
  – Estimate this will reduce incomes of 30,000 social tenant households
  – Affects the work incentives of a further 70,000 working households who would be capped if out of work

• For those affected, an increase in social rents can actually strengthen their incentive to be in work
  – Out-of-work income falls, as housing benefit cannot increase to cover
Universal credit and social rent changes

• Universal credit is replacing 6 means-tested benefits for those of working age
  – Income support, income-based JSA, income-based ESA, child and working tax credits, housing benefit

• Universal credit will slightly dampen the impact of changing social rents on tenants’ incomes and work incentives

• More working social tenants will be entitled to universal credit (51%) than are entitled to housing benefit (36%)
  – More working households see a change in rent offset by benefits
Summary

• 12% cut in social rents (relative to previous plans) will benefit central government more than tenants
  – Tenants’ work incentives will be strengthened
  – Incomes of social landlords cut, with potential effects on house-building

• Pay to Stay will increase rents for the highest-income tenants
  – Makes sub-market rents slightly more like housing benefit
  – Precise impact depends on how rents rise once incomes increase beyond Pay to Stay threshold
Recent rent policy displays lack of consistency

- Rents will fall for existing tenants, while ‘Affordable Rents’ mean higher rents for new tenancies

- Rent cut announced in Budget came one year into ten-year commitment to real increases
  - Danger of uncertainty over future – harmful for tenants and providers
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