



Social Housing Policy Working Group Paper

Funding new social and affordable housing

Ideas, evidence and options

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Executive Summary

There is only a finite set of well-established ways in which sub-market housing can be delivered involving different combinations of elements from land, finance, construction costs and equity (including subsidy). Whichever combination is chosen, political support for programmes and the necessity to provide value for money must be established. There is no silver bullet.

In recent years, the principle of a general funded programme to support social and affordable housing has been replaced with multiple top-down interventions from government and, increasingly, a diverse set of local tailored affordable solutions from housing associations, councils and other local initiatives.

It is likely that future affordable supply will come from pro-cyclical cross subsidy, multi-year partnership agreements between developing associations and Homes England, greater use of existing assets as collateral, local housing companies and some traditional council housing, with new projects supported by wider use of guarantees, local planning agreements and recycled funds e.g. shared equity.

Other options can be considered in the absence of a significant shift in political support for subsidised scalable housing programmes: equity interests in public land used in partnership developments, revenue subsidy or other contributions or outcome-based payments, reformed personal housing subsidies, and local or regional development bodies tasked to assemble, service and co-develop.

Introduction

Preamble

A key feature of housing in England after the global financial crisis has been the retreat from building new social housing. This reduction has of course in large part been driven by the financial and subsidy environment. The dominant model of council building was undermined in the 1980s, never to return, and after a quarter century or so of relative stability, the mixed funding model of housing association social housebuilding and in particular the significant upfront capital grants it enjoyed, also collapsed in the face of the challenges emerging after 2008. Despite creative efforts to sweat assets, cross-subsidise and exploit remaining S106 affordable housing planning agreements, most of what has been built by housing associations in recent years has been affordable home ownership, affordable rent and market new build for sale or for rent. At the same time, many local authorities are establishing local housing companies as alternative ways to contribute to local housing solutions of different kinds.

In this context, it is only natural to ask what other feasible models might be considered, what are their features or defining characteristics, and what prospects might they have as alternatives or supplements to the range of models already in use or planned? The intention of this paper therefore is to generate discussion and debate about how we might make progress with feasible models that would deliver more affordable supply (including social housing) under different local and national scenarios and contexts.¹

We begin, in the introduction, by contrasting the basic models that delivered most of the existing social housing stock and the more recent attempts to overcome institutional and funding or subsidy barriers before noting that the present arrangements in England are not completely given. We only have to look to divergence in approaches in Scotland in the last 10 years to see what might be possible. The next section of the paper stands back and asks, what are the fundamental constraints and requirements of delivering subsidised affordable or

¹ The paper is a review of academic and grey literature but also draws on recent research by the author for the Joseph Rowntree Foundation (Gibb, Maclennan and Stephens, 2013), for the European Housing Partnership (Gibb and Hayton, 2017) and as part of an ongoing three country study of housing policy (Shaping Futures: Housing Policy in the 21st Century) working with Duncan Maclennan, Hal Pawson and David Hulchanski.

social housing²? This in turn leads to two sections considering, first, a range of recent developments introduced or planned to be introduced in the UK and internationally; and, second, a reflection on new ideas and thinking that may have mileage and the capacity to reshape things on the ground. The final section of the paper is a discursive conclusion that summarises the policy implications of the preceding discussion and considers key ways to make progress.

The way things were

The traditional council house building core model was a revenue deficit model (via the housing revenue account) financed from long term public loans. This long-standing system was gradually undermined from the early 1980s onwards by policy change such as the cumulative impact of council house sales. It was also subject to critical changes to the finance and subsidy system at two main levels.

First of all, the UK government in the 1980s (and its predecessor after 1976) targeted housing public capital spending programmes (in this case, the right of local authorities to borrow to build) as a key source of public expenditure savings (even though there remains controversy over the public accounting treatment of self-financing public sector projects like council housing), through imposing a long standing housing-specific borrowing limit on local authorities³. Second, the housing revenue account, in essence a comprehensive income statement of the council housing sector based on rent income and on-going capital and revenue expenditure, including management and maintenance (M&M), was able to receive annual subsidy if there was a projected deficit. However, from the early 1980s onwards, successive governments were able to tinker with the system (allowances for M&M, imposing a forecast rent increase, etc) in order to force rents upwards and gradually move councils out of subsidy. Inevitably, new build was replaced by the evolution to a more asset management-oriented approach to the existing housing stock and the capitalisation of surpluses to fund

² This section draws extensively on the finance analysis carried out for the Shaping Futures project by Derek Ballantyne.

³ The Conservative Government announced the repeal of the local authority council housing borrowing cap in the autumn of 2018 – see Gibb and Cain, 2018.

improvements and long-term maintenance. At various points, receipts from council house sales were used to directly reduce council housing debt rather than reinvest⁴.

Post-1988, large scale voluntary transfer (LSVT) afforded a refinancing of existing housing debt and often also funded a major repairs programme, initially privately funded but later with more subsidy or debt forgiveness under the New Labour governments. Based on performance gateway access, arms-length management organisations provided alternative ways of running council housing investment and management programmes on a fixed term basis offering additional public funding. Arms Length Management Organisations (ALMOs) in a sense also opened the mind to other forms of arrangements such as local housing companies, which we return to below. In 2012, English councils social rental housing funded by the Housing Revenue Account entered into a new self-financing arrangement involving a series of deals and promises that allowed greater freedoms in return for a number of commitments by councils and pledges by government (CIPFA/CIH, 2016). Additional debt (£12 billion) was taken on and scope for investment clearly depended on risks being supported by securing income levels. This ‘autonomy’ has been to an extent undermined by government restricting rents, and the additional housing management costs associated with the growth in income recovery (ie to reduce lost rent through arrears) in the wake of welfare reform.

In the housing association sector, the mixed funding model was established in 1988, making important reforms to the previous system which had some odd incentives and inefficient features (Hills, 1990). The new system was premised on a strong regulatory environment within which associations would fund development of social housing out of an up-front capital grant for an archetype property with the remaining development costs to be met by a private mortgage loan. The required rent, which should be affordable to a low to moderate income households in work, should meet the loan repayment plus assumptions for M&M and was also supposed to create a sinking fund for long term repairs. The scale and impact of this model therefore turned on two critical parameters and a couple of implicit assumptions. The parameters were: the average grant rate per unit and the size of the overall annual programme. The assumptions were: first that there was an appetite to lend from the private sector to housing associations and second that the housing benefit system would take the strain as the housing association client group shifted inexorably to a narrower and more

⁴ Council house sales on new build also became a disincentive to build new homes for councils since they have never in practice been able to recycle receipts one for one for new build, and many have been discouraged to build if the unit is only to rapidly leave the sector via the RTB.

disadvantaged group with a similar proportion of households in receipt of benefit as for council housing.

For most of the succeeding twenty years this model continued to generate tens of thousands of new social housing units per annum, though it came under pressure as the new millennium wore on because of other housing policy pressures (e.g. the use of the decent homes standard to shake out council housing and shift existing social housing into the housing association sector via increasingly subsidised [or debt forgiven] LSVT, and the desire to reduce grant per unit through a range of measures such as the use of reserves, S106 agreements [Crook, et al, 2016] and cross-subsidy from for-sale products). The world financial crisis and subsequent recession fatally damaged the grant-funded programme which, apart from the coalition government's Affordable Homes Programme (low grant, higher affordable rents and cross subsidy from re-let homes also now operating at the affordable end), has produced an outcome that has seen a much more commercial and affordable approach to new build. This has been led by associations with financial capacity⁵, land and the wherewithal (e.g. security) to build a mix of for-sale and affordable homes (e.g. shared equity and affordable rent), some again supported by local S106 affordable housing agreements. The volume of social housing now being built has shifted into a new low scale equilibrium.

Social housing does not exist in a vacuum but rather is part of a complex, interdependent emergent housing system which has feedback loops and other dynamic properties (Gibb, 2018). The growth of private renting offers challenges and opportunities for social landlords. At the same time, many would-be purchasers cannot access home ownership. Austerity and welfare reform also shift focus to income management, rent arrears and uncertainty about future income (Hickman, et al, 2018). Equally, asset demand for housing encourages new development by private interests, which through planning practice change in the last 10 years has altered opportunities for what S106 can be used for especially in high demand redevelopments in London. This new context, the regulatory backdrop (Marsh, 2018) and the aforementioned reduced subsidy and programmes is making it more common for developing associations to shift their build focus towards mixed and more affordable, but also market level, segments. The hybridisation of social housing is the product of many factors but it raises

⁵ There has also been a significant shift away from long term mortgage finance to the use of capital market funding subject to variable market circumstances and appetite to lend over time.

several questions regarding the purpose of social housing and sector diversification (e.g. Gibb, et al, 2016; Crook and Kemp, 2018; Chartered Institute of Housing, 2018).

Narrowing options but lessons nearby

The options appear to have narrowed considerably. Yet, a different perspective on the experience of the last few years is that of a social entrepreneurial outpouring of ideas and models of new social and affordable housing delivery as both councils and the third sector try to find ways, large and small, to develop in a challenging environment. We will discuss these models in more depth below but the sector is now increasingly familiar with community land trusts, empty home initiatives, land use conversion, local housing companies, funding models like social real estate investment trusts (REITs) and other sale and leaseback arrangements. Apart from bottom-up ideas emanating from specific providers and their partners, there has also been interest within government with the greater use of guarantees and contingent liabilities, as well as incentive mechanisms such as the new homes bonus. Apart from these sorts of activity, many are writing and reporting on other new ways to build and deliver social and affordable housing.

It is also worth looking a little closer to home. For the last two parliaments, the Scottish Government has been pursuing a social and affordable supply strategy which aims to deliver 50,000 units in the current parliament (after delivering a 30,000 target for the last one) made up of 70% social housing funded by capital grants to housing associations and local authorities. The right to buy has been abolished, there are no external borrowing caps for councils who can receive deep capital grants to build. As a result, council housing is emerging at scale in Scotland alongside the larger housing association programme, plus there is a growing grant-funded mid-market or affordable rent programme for key workers as well as shared equity models. This is a £3bn programme over the life of the Parliament and customises the traditional models that used to operate in England. It is geared up to meet 5/6 of the consensus level of national affordable housing need (i.e. a target of 50,000 units and need assessed at 60,000 units). In part, this is simply the consequence of a political decision over the use of scarce resources⁶.

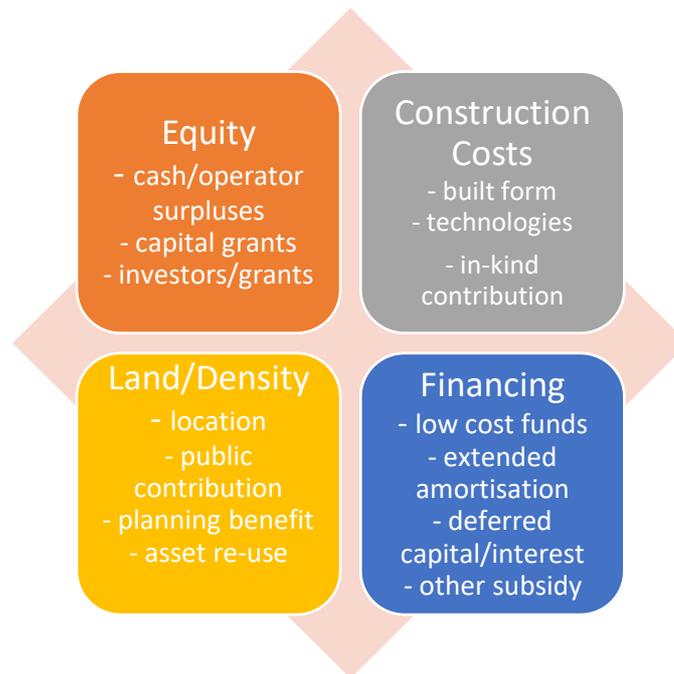
⁶ For more on the Scottish affordable housing supply programme see: Gibb, 2015; 2017; Stephens, 2017. A separate paper on Scottish social housing is being prepared for the SHWG by CaCHE.

Financial realities

Before we look at alternative models and ideas, we need to go back to basics and ask what fundamentally are we trying to achieve and what are the essential parameters involved in developing below market housing? *Shaping Housing Futures* is a tri-national knowledge exchange programme on housing policy in the UK, Canada and Australia. At the first workshop of the programme in Glasgow in 2016, Derek Ballantyne, now chair of the Canadian Housing and Mortgage Corporation, presented a useful analysis of the fundamentals of funding non-market housing (Ballantyne, 2016; Gibb, forthcoming). Below his key points are summarised – these are completely universal and a helpful backdrop to this paper’s subject matter.

Ballantyne argues that there are four elements (housing equity; construction costs; the land element, including density; and, financing) that determine the cost of housing production, and therefore the unit’s ultimate affordability (the quadrants of figure 1). Most affordable or social housing models would normally achieve sub-market pricing through applying one or more of these four factors. Under each of these quadrants, there are further sub-elements, a mixture of private sector led or public led mechanisms that can assist delivery of affordable housing. But, however one approaches the question, somewhere there will be an opportunity cost and therefore a required subsidy of some form (grant, revenue, personal subsidy, land, guarantees, in-kind support, etc.) required to deliver below market cost provision either in terms of production delivery or at the point of consumption (or both). This may be explicit or implicit but it is nonetheless a genuine cost borne by an individual, an incorporated entity or via an arm of the state (and hence by taxpayers). The market will not provide the below market outcome without some element of financial support, unless it is forced to through a negotiated agreement (e.g. planning obligations).

Figure 1 Housing Finance: The Essential Elements (based on Ballantyne, 2016)



Ballantyne goes on to suggest that a variety of mechanisms can be used to reduce the cost of building housing. The effectiveness of these measures will vary over time. Most financial models focus on equity, land and financing. Construction costs are in general more difficult to reduce and materials and labour do not (typically) vary sufficiently in cost terms across regions within a jurisdiction. New construction technologies have improved housing quality but according to Ballantyne have not yet reduced housing delivery costs significantly (but nonetheless do have an impact on housing operations costs – particularly in energy consumption and production). Returning to the other three quadrants, past and current financial models in the countries examined by Ballantyne include one or more of the following elements of cost reduction:

- Low cost land / public provision of land
- Capital grants for land acquisition and / or construction
- Planning and permit concessions
- Equity (including grants, project delivery support, low cost equity investment and other forms of partnership)
- Low cost financing (construction financing and long-term debt)
- Tax concessions (construction, financing and investment)
- State backed guarantees or contingent liabilities.

Ballantyne's analysis raises two further important points. First, the search for financial innovation in non-market housing models (e.g. Gibb, et al, 2013) is unlikely to uncover radical new untapped opportunities because there is actually only a limited number of fundamental ways with which to deliver below market housing through different matching and choices relating to figure 1 above. The models we already know and those that are discussed in subsequent sections – all can be reduced to the elements of figure 1 and its sub-elements. We know that the different stakeholders have to co-operate around the irreducible fact that private sector participation, including construction interests, requires a given rate of return for the risk confronted. It is about putting together the specific mechanisms available, the incentives to work in local contexts and institutional settings that allow specific projects to be realised. There will be good reasons to prefer a subset of approaches over another and there will also be specific constraints (e.g. vested interests) that seek to preclude specific alternative subsets of models (e.g. involving the redistribution of land value uplift). The point here is that the underlying approaches have a finite set of options that make them deliver below market housing costs and that somehow the real cost of the concession that makes it happen has to be borne (there is no free lunch).

Inevitably, politics and current priorities determine the resources available but thereafter those resources need to be used effectively in whatever way they are co-ordinated. In the UK, we can distinguish between the overall capital spend programme for social housing (the key political decision) as opposed to the more technocratic micro decision about how that funding would be allocated according to grant rates and allocations across different programmes. It is true that there are successful idiosyncratic national examples of affordable housing funding such as in France, Austria or in the USA, but barriers to their speedy translation to other settings are considerable and often insurmountable (Milligan, et al, 2009; Gibb and Hayton, 2017). The key point is that an expansion of new affordable supply always requires the political clout that will divert or allocate scarce public resources to it (or away from it). There is no escaping the political context of priority shaping and opportunity cost across programmes and sectors.

The second point is related – the bullet point list of elements (previous page) all have public financing implications directly or indirectly. Scarce public resources must be well used in order to maximise their impact. While governments may not always recognise the very existence of

some of our current tax concessions⁷, we can hardly support redistributive and progressive reforms to the housing sector that purport to increase efficiency if we do not at the same time recognise the continuing need to maximise public value for money.

There are important implications from this analysis for the rest of this paper. First, there is little to be gained by acting as if there is a blank canvas to work from. Rather, there are path dependencies like the continuing priority of supporting home ownership as well as policies that appear to be ruled out, such as significant grant-funding models operating at scale. We need to focus on feasible policies that can deliver programmes that work with the grain of the market and satisfy these political parameters (though they still have to be well designed and possess sufficient resilience).

Second, not only is the size of the programme and its component parts important, so is the way the programme is allocated across regions. Most would argue that the present system is opaque, politicised and not obviously allocated according to agreed measures of unmet need. There needs to both a baseline agreed estimated level of affordable housing need and a regional calculation that sums to the national one. The allocation of resources across space should be transparent and defensible.

Third, the end of grant-funding for social housing in England may be upon us (and in its place a myriad of schemes both locally-originating and government-led), but what will this mean for the political economy of social housing? Some have argued that this is reminiscent of the deal done in the Netherlands in the 1990s when government retreated from its previous funding and partnership roles. This will change the role between landlords and the regulator but may also further weaken the position of social providers relative to the state in England.

Fourth, affordable development will require more reliance on pro-cyclical cross subsidy from market activity. It may be able to reduce costs through guarantees and by pooling. It will also draw more on providers with strong balance sheets, low debt assets and, in the council sector, where there is strong prudential capacity to borrow and manage new debt. The policy may become less about funding directly and more about incentivising greater and more effective use of sweat equity and partnerships with private equity. Where rationed public resources are contributing to new affordable investment, the clamour will be to stretch those resources and

⁷ E.g. acknowledging that not taxing real capital gains on the first home of home owners is a deviation from an asset taxation benchmark of neutrality see O'Sullivan and Gibb, 2012.

to maximise their effectiveness, for instance, linking them to affordable need as in the government's focus on cash difference between market and social rents.

Options – evidence

In this section we consider evidence from the UK and abroad in terms of efforts to innovate and develop new affordable housing models. The section draws on previous reviews carried out by the author (Gibb, et al, 2013; Gibb and Hayton, 2017). In looking to other countries to identify possible affordable models that could translate to the UK context, we need to take a robust approach to the challenges of comparative research and the limits to policy transfer arising from significant institutional and other differences across nations. These challenges are well-known (e.g. Stephens, 2011; Gibb, et al, 2013), involving differences in national housing systems, legal arrangements, historical trajectories, policy settings and broader approaches to social policy. We must always remember that different contexts (like a strong welfare state in a Nordic setting) or institutions (e.g. mutual guarantees in the Netherlands housing associations sector) may constrain the transfer of a given policy to the UK.

In research for the Joseph Rowntree Foundation, Gibb et al (2013) found examples of tax credit, public funding or guarantees innovation in affordable models in countries like Australia and the USA, as well as creative ways of using contingent liabilities, surpluses and well-designed benefit systems in different parts of Europe. Five wider themes could also be identified, not all consistent with each other:

- An enthusiasm for state-backed guarantees though these need to fit with existing policies and match the risks associated with the contingencies involved.
- Support for subsidy systems based on contestable supply & partnership between for profit and non-profit providers, often operating with *blended* subsidies from different tiers of government. Partnership might involve management and/or leasing roles for non-profit providers but sometimes they shared development risk. Questions remained about the governance of charitable entities in such models.
- At the same time, European examples often involved 'collaborative solidarity' with non-profit providers operating as clubs building up funds to bail members out when required and with or without support from government (e.g. Netherlands and Denmark). It has been suggested that the strategic partnerships recently set up by Homes England to target investment resources to a small number of larger

associations is an example of the state moving on from competitive bidding to a more durable and collaborative working model.

- The essential policy choice to deliver more housing at lower subsidy or fewer units at a deeper subsidy. This makes sub-national spending distributions and choice of models (which may be more or less favourable in different regional market conditions) all the more pointed.
- The key will remain in ‘sweating’ existing assets which will skew development to larger providers with the right balance sheet mix of low debt assets, but without external subsidy, this will not generate much general needs social housing.

Czischke (2013) considers how social innovation might be used to improve housing in Europe. The innovation enablers took several forms: an openness to experimentation, opportunities for exchange and cross-learning, cultural factors, resident participation and innovative leaders. One interesting example of such innovation is using “payment by result” or outcome-based social impact funding to underpin homelessness reduction in England – investors are paid a return on their investment as and when the delivery agency can provide evidence of achieving agreed targets (scorecards) relating to their objectives. In an international review of what works in approaches to affordable rental housing, Rowley et al, 2016, draw several relevant conclusions (pp.4-5):

- Institutional finance and funding can be supported by a government guaranteed finance intermediary (including low income housing tax credits), a specialised housing finance aggregator to help smaller providers access long term finance and supporting the maturing of the market in order to create an environment where tax credits and other targeted concessions can support institutional investment in affordable housing.
- Diversity of product delivery – there are different ways to expand affordable supply, not just adding new units via development but through conversion of existing stock, re-using empty homes and developing a range of affordable housing at different price points below market levels.
- Defining affordable rent and incorporating efficient or well-designed housing assistance . Reforms of demand-side assistance are required to help lower income households access affordable housing in high demand areas - how these are designed, their incentive structures and wider consequences are all important to how affordable housing supply evolves. In Norway, Nordvik and Sorvoll (2014) make a case for supporting the positive long run social investment impacts of the

housing allowance to help secure and maintain affordable housing for low income households. The authors take more of a life time or actuarial approach to benefits and costs associated with subsidy rather than just immediate cash costs and neo-liberal views concerning incentives⁸. The present UK system of housing benefit is not the only game in town.

Rowley et al point out that especially in the early 2000s in England, affordable planning obligations changed the spatial distribution of new social housing cumulatively because of where new private housing was being built. There is considerable interest internationally (and not uncritically) in various forms of inclusionary zoning, affordable housing quotas as other forms of planning-led affordable supply mechanisms (Austin, et al, 2014; De Kam, et al, 2014; Nordhal, 2014; Morrison and Burgess, 2014; Scally and Tighe, 2015; Kontokosta, 2015; Korsu, 2016). Bryant (2006) looking at Australia argues that infrastructure charges can actually reduce affordability by bidding up house prices depending on how the charges are designed. The efficacy of these sorts of policies are an empirical matter – as Austin et al note, specific policies depend on local property rights, culture, attitudes to social mix and the incentives facing the different players.

We can synthesise the evidence from research on S106 planning agreements and affordable housing. Gurran and Bramley (2016) identify essential conditions for effective agreements, including: a degree of consensual fundamental legitimization; an operational definition of affordable housing; robust evidence of need; and, setting target levels for local areas (quotas). Thinking about the wider lessons, Gibb (2017) concludes:

1. It does not happen overnight - there was a relatively long bedding-in period of S106 and the social construction of the legitimization of the policy for all stakeholders.
2. The evidence from England is that genuine scale in completions of affordable housing through this mechanism is perfectly possible.
3. The importance of the evidence infrastructure (detailed needs and land supply numbers) within which the site-specific planning agreements have to nest within.

⁸ This harks back to debates about lower HAG rates leading to long term higher HB bills as a result of higher rents.

4. Note also the vulnerability of the policy to top-down short-term reform pressures (e.g. since 2010 in England) which can change the composition, tenure and affordable share of the completions achieved⁹.

In the UK, Scally and Gibb (2015) contrast English policies under the coalition government (2010-15) with those developed in Wales and Scotland that sought to deliver targeted levels of social housing as well as a range of affordable programmes such as mid-market rents¹⁰. UK evidence is also instructive about the challenges and possibilities of shifting local authorities from provision to enabling roles (or indeed to both). Clearly, they continue to play a key role in land planning, in partnership working, by working with local housing companies (discussed further below – see Hackett, 2017; Morphet and Clifford, 2017) and in making deals around planning obligations (Shelter, 2008; Outer London Commission, 2015) and this is especially true in London (Holman et al, 2015).

Returning to Gibb and Hayton (2017), what lessons emerge from the detailed European national case studies they examine (including Finland, Ireland, France, Spain and Austria)?

- Many national housing systems have displayed considerable vulnerability to wider economic and financial shocks. If the aim is sustainable increases in affordable housing we need to build robustness and resilience into our funding and delivery models. At the same time, evidence of how housing systems work, interact and how different elements are interdependent, is critical to making good policy design decisions about housing need, new supply, location and market segmentation. We must re-emphasise the importance of prevention – ‘Housing First’ approaches and other homelessness reduction processes have a part to play and help with tenancy sustainment and arrears reduction is essential.
- Long term stability is required of subsidy (funding levels), regulatory, social security and planning systems – it is in that context that one thinks about instruments and mechanisms e.g. direct subsidy, finance subsidy, guarantees, tax breaks, inclusionary zoning, benefit design.

⁹ For instance, the use of financial viability to reduce or even eliminate affordable housing in such agreements.

¹⁰ Mid Market Rents involves significant capital grants, starting rents close to the relevant local housing allowance, and properties targeted at key workers. In Scotland this affordable rent model operates under the new (indefinite length) 2016 tenancies.

- We should work with the grain of markets – housing, labour and finance markets - and not lose sight of the difficulty in achieving effective interventions by public agencies. We should test and understand the consequences of intervention in markets before proceeding further. In the long term we need to combat speculative forces (including those created or supported by inefficient tax distortions in land and housing markets). Intervention must be based on sound principles including tackling market failures, and the consideration of housing’s place in macro-prudential discussions of mortgage lending stances should also be recognised.
- Affordability needs wider scrutiny and analysis, and the interconnectedness with non-housing phenomena must be identified and explained e.g. insecure and low wage problems in the labour market can undermine housing-led reforms.

The next section looks at recent or contemporary ideas and new social or affordable housing policies considered or piloted in England in the recent period.

Options – policy & model ideas and action

In this section we take a selective and non-exhaustive overview of recent proposals to develop a range of affordable housing models or provide mechanisms to unlock them from the constraints they face (see, also the overview of different models recently produced for TCPA by Smith and Henderson, 2017). The discussion is organised around three headings: overcoming land barriers, financing innovation, and subsidy.

Proposals to overcome land barriers

The cost and availability of land, land value uplift, planning interventions and taxation of land are widely recognised as key factors in promoting or inhibiting more low-cost housing (McFarlane, 2017; Murphy, 2018; New Economics Foundation, 2018). Here we focus on a cluster of approaches that all seek to remedy the land value capture question. We also look further at community land trusts.

Land is an expensive and volatile element of housing costs and is widely viewed as problematic (for good reason – see McFarlane, 2017; New Economics Foundation, 2018). Solutions have been widely proposed to address the inefficient allocation of land resources, hoarding, banking, the excess of surplus public land, capturing more of the societal benefit associated with land value uplift and related questions to help provide more cheap land for

affordable housing purposes. We briefly introduce some of these ideas below but note the strong institutional, electoral and vested interests arrayed against many of them. Land reform is inherently political and re-distributional.

- Surplus public land is often viewed as both a potential solution or at least contribution to affordable land supply, as well as often currently being a problem (New Economics Foundation, 2018; Murphy, 2018). Part of the issue is the duty to maximise land receipts at sale, which is also really about a failure to remove silos and join up different parts of the public sector in the public interest. This has led to a range of proposals to seek to overcome these barriers. One is a form of nationalisation (NEF discuss a peoples' land bank). Many commentators discuss more extensive or greater confidence in the use (or threat) of compulsory purchase orders or, as the Scottish Land Commission suggests, a compulsory sales order – to help land assembly. More creative partnership ideas might also work in specific circumstances for instance making the public sector land owner an equity partner, providing them with access to income streams or simply offering them a ground rent based on leasing. Different market and ownership contexts suggest the need for a range of tools.
- Land value capture mechanisms have risen to prominence in recent years (McFarlane, 2017; Aubrey, 2018) in terms of seeking to return elements of the uplift to the wider community and to pay for infrastructure, as well as to fundamentally change the economics of land and property¹¹. Aubrey (2018) argues that the compensation associated with the granting of planning permission has to revert to its original use-oriented principles; others argue, reminiscent of new town planning, for the introduction of an affordable housing land use class. There is also debate around strengthening the scope for local S106 affordable housing agreements, reducing the private developer's recourse to viability arguments that have in the past diluted the affordable element¹², and also as regards the advantages conveyed to both purpose-built student housing and Build to Rent investors that allows them to bid more for land.
- Land value taxation (McFarlane, 2017) is a long-standing principle much loved by economists and land reformers alike. An efficient tax, it is a targeted way of supporting

¹¹ The Letwin Review recommendations, published alongside the October 29 2018 Budget, make positive proposals to Government to use, inter alia, planning mechanisms like S106 agreements on larger sites in high demand areas, to enable more affordable housing (and greater tenure diversity).

¹² A more robust affordable homes element to planning agreements around new housing development appears now to be the case going forward in London.

infrastructure and redistributing unearned land value gains. While it faces technical and particularly political challenges, it remains popular in certain quarters (including both the Green Party and the Liberal Democrats).

- Development agencies that sit between local and national government, are independent and can chart a long-term vision outside of the electoral cycle – are a possible contributing solution to addressing land market failures (Homes for Scotland, 2018). Drawing on new town development corporation ideas, but also bodies such as English Partnerships, such vehicles could dominate the strategic land market but also support SME builders, regeneration projects and affordable solutions. However, they need to convince that they would add-value, and be nimble and unbureaucratic. Homes England could clearly play such a role, at least in part.

Community Land Trusts represent one specific way of addressing the land value uplift affordability problem (as well seeking to promote ethical and other normative attributes). While some of the literature is evaluative (Young Foundation, 2011; Moore and McKee, 2012), international commentators have also identified it as an important disruptor with scalable properties (e.g. Friends of Europe, 2017) and it is also part of a wider class of proposals that seek to separate out build costs from land and infrastructure.

Financing innovations

We have stressed already that there are limited ways open to financial designers to come up with genuinely innovative ways to overcome the issues raised by the quadrants diagram discussed earlier and the constraints facing the organising of new housing supply at sub-market or concessionary levels. Here we look at three contemporary or recurring approaches: local housing companies led by local authorities; the recurring case made for some form of social or affordable REIT and a cluster of ideas around pure financing ideas such as bond aggregators and state-backed housing banks.

Morphet and Clifford (2017) found that in the summer of 2017 more than 9 in 10 local authorities were directly involved in the provision of housing, be that direct Housing Revenue Account (HRA) provision, using the general fund, joint ventures or the provision of land and other resources for new housing. As we have seen, more than 150 local authorities in England (Hackett, 2017) are involved with Local Housing Companies. Enabling legislation in 2003 and in the 2011 Localism Act has paved the way for local authorities to set up wholly-owned companies financed from general funds and thereby overcome constraints on them to allow

them to provide housing and intervene to address specific needs issues. As we have seen, these companies provide a range of housing niches: starter homes, affordable rent, market rent, housing for temporary accommodation solutions, housing for older people and in some cases social housing.

Local Housing Companies can, in different places, deliver each of these segments to scale (relative to local need). These options depend on the interpretation of local requirements and gaps in provision but also from the mix of local opportunities i.e. funding, land and the governance arrangements that allow these companies to prosper. Because there are many variables at play, England has a wide range of these companies in terms of their structure, governance and provision segmentation. Interestingly, Morphet and Clifford argue in their recommendations section (p.6) that the UK government should consider moving to the International Financial Reporting Standards (IFRS) accounting standards in order to allow councils possessing HRA stock to revalue them at market rates and thereby borrow against their value. This is something that housing associations are already very familiar with. As Hackett (2017) indicates, these are commercially-oriented arms-length bodies and they demonstrate that social, affordable and other market failure responses can be addressed by such vehicles when they are organised for a social or public interest purpose. This provides a *triple-dividend* of extra housing, financial returns and capacity to help shape local places. Hackett estimates that 2 in 5 units are affordable, less than half of those 'social'. The financial surpluses generated are also being used to cross subsidise other activities to provide social and affordable housing.

For many years there has been interest in developing real investment trusts (REITs) which would be a vehicle to invest and partner in additional affordable or social housing. This has, internationally, proven difficult to do. There are only a small number of projects in places like the United States and Singapore. The UK Government showed interest in such models though the Treasury did retreat from this position (Gibb, et al, 2013). Nonetheless, hardly a week passes without new investment models described as social REITs coming forward. Certainly, institutional and other large investors are looking for housing to invest in but one needs to be careful as to what these models actually signify. For instance, the original wave of REIT growth in the UK was in part about tax efficient re-organisation of existing property companies and some of the 'social REIT' models proposed were really sale and leaseback models that would generate affordable housing which would be managed by housing association partners. While there is some evidence at the margin that there are examples of new REIT offers which may create equity partnership in new affordable housing, the main lesson of US REITs is that they

can take a long time (i.e. decades) to develop as a sector but they remain stubbornly market rent rather than sub-market or affordable in scope and scale (presumably due to the tension between tax transparency for investors on the one hand and the limited scope to provide further subsidy on the other).

The UK has a well-developed financial aggregator (The Housing Finance Corporation or THFC) but interest remains in new aggregators, some from the private sector (Council on Federal Financial Relations, 2016). A recurring theme is also state-backed or state-owned investment banks. Capital Economics (2014) argues that state backed loans could generate cheaper long-term finance for affordable housing though it is not necessary for the guarantees to be organised around a specific housing investment bank, as recent experience in both England and Scotland has shown. Is there a compelling deeper case for a housing investment bank?

Subsidy

We have discussed the fluctuating fortunes of capital grants, spending programmes and shallow subsidy. Here we look at three other approaches. First, personal subsidy is likely to remain critical to the housing of low-income households. How can it be better designed and organised to support affordable and social models (touching on the definition of affordability for new models)? Second, we consider the scope for designing models based on various forms of revenue subsidy including state-backed guarantees and outcome agreement frameworks for social investors. Third, we explore pump-priming self-financing programmes that can support affordable housing for instance the use of revolving funds to help provide cheap serviced land.

Personal housing subsidy, demand-side assistance to help with housing costs for low income households, is the largest single part of the housing budget. In many respect demand-side personal subsidies have won the political battle with supply or capital-based subsidies (if not the conceptual or analytical contest). Despite the pressures placed on it since 2010 and subsequent welfare retrenchment, housing benefit, in all its forms, remains a fundamental way of making housing affordable and giving social and affordable developers (and investors) confidence. In addition to the negative impacts of cuts, caps and restructuring, there is also the lost opportunity of a better designed system. The UK continues to have a very odd

approach to personal housing subsidies when viewed comparatively¹³. Should we not be looking more closely at tenure-neutral housing allowances based on more rational and just principles alongside complementary reforms to rents?

One simple but attractive model which recycles public finances is a revolving funds approach. This might be at scale through an English Partnerships' style land assembly vehicle which funds its operations through sales. It might be a shared equity model which returns the state equity on resale. It might be a local land fund to support development, be that on actual sites or as concessionary loans. Indeed, the revolving fund may combine some of these features through intergovernmental financial transactions: the UK Government provides funds to the Scottish Parliament (financial transactions) which are to be repaid after 10 or 20 years – hence it makes sense to direct these funds to repayable investments (the Scottish government has for instance directed some of these funds to lower priced new build help to buy investments). The key with these types of model is the upfront pump-priming cost to establish the fund and subsequently the efficient delivery and management of the fund.

A final opportunity that might be worth further consideration is revenue subsidy (broadly conceived to include specific forms of state-backed guarantees or contingent liabilities, outcome-based social impact bonds, as well as, potentially, profit-sharing private finance models). HRA revenue subsidy was a political football which was used as a control mechanism by central government. Future models would have to be strongly designed and incentive compatible in such a way that parties were not exposed to risks of annual political or financial change. This is in part about writing (and pricing) good contracts. The chief hurdle may of course be to convince governments to move toward long term revenue commitments which is precisely why 'payment by results' social investor models, state-backed guarantees or variants of local authority PFI repayments may be increasingly acceptable.

¹³ In part because traditionally cash benefit need within our social security system has been designed around an after-housing-costs minimum level of income – so that housing benefit meets all additional reasonable rent payments until it reaches its ceiling and other relevant caps.

Conclusion

Policy implications

The central point of Ballantyne's analysis is that designing different ways to deliver low cost or affordable housing requires some combination of a finite range of key elements. Because of the role of private sector interests, somewhere there needs to be subsidy, concession or intervention that has public finance or redistributive implications. Partnership with the private sector, in the form of equity contributions, etc. requires competitive returns. Similarly, cross subsidy to more affordable provision requires market levels of sales.

There are several implications. First, the political willingness to prioritise public resources for housing programmes, as opposed to other social and economic policies, is critical. Second, in such a rationed environment (made worse by the political realities that remain with us ten years after the Global Financial Crisis), policy design has to be efficient, smart and durable, offering good value for public money in terms of outcomes as much as inputs and costs. Third, necessity generates invention and entrepreneurialism. In England, there is considerable ongoing diversity and experimentation - but it is rather unexpectedly taking place in the local authority sector in the form of diverse local housing company activity. At the same time, higher level design debate in areas such as land market reform is also underway. This indicates that entities like local authorities, subject to local contexts, institutional and other resourcing factors, can shape different models of provision and develop a wide range of housing partnerships. Relatively few of these will, however, generate traditional social housing.

There are then both ideas and working models worth taking notice of. We seem to be moving further away than ever from the notion of a conventional dominant model of social and affordable housing provision and instead fracturing into more and more local sensitive models, some of which build on and customise templates of good practice. The exception to this is to be found in other parts of the UK where the political commitment to affordable supply, for the moment, provides for a small set of dominant and comparatively traditional, grant-funded models. Innovation is taking place in England, clearly, but it is shaped by the political financial settlement, the opportunities created by enabling rules, laws and regulations, as well as the local market context. The capacity to make a difference also clearly depends on how serious and costly to rectify are key local market failures stemming from high land prices and inadequate land availability.

Gibb and Hayton (2017) focus on long term durable arrangements that are resilient and less vulnerable to external shock. Affordable models should be designed to be sensitive to their wider systemic interdependency to the rest of the housing system (e.g. affordable rental products competing in the private rented sector or recyclable funds dependent on a resale market), and design ideas should work with and not against the grain of the market.

Ways forward

The paper has attempted to stimulate a debate about what might be possible in the context of national and more local constraints on resources for new social and affordable housing. In that context, what might we expect to see?

First, the continued concentration of new affordable development by a smaller body of large associations, in part as a result of previous concentration regionally, also because of their asset base and ability to operate pro-cyclically and increasingly because of strategic partnership policy initiated by Homes England. The blending of subsidy, discussed in terms of other countries by Gibb, et al, (2013) is increasingly a feature of the system, as could be the expanded use of contingent state-backed guarantees.

Second, the recent removal of council housing borrowing caps in England and Wales, while valuable to unlocking borrowing power, may herald not so much a new mass council housing building programme, as to generate a parallel and perhaps more modest development of council housing alongside the continuing diversification and growth of local housing companies, the latter able to utilise their land, statutory powers, borrowing and revenue-generation capacity in ways greater than the traditional council housing model.

Third, the growing interest in land value capture seems to be irresistible, garnering widespread political support and now proposed (implicitly) in the recommendations of the Letwin Review for more diverse tenure and price points across large scale developments in areas of high demand.

Fourth, there is a case to explore revenue instruments once more and in particular guarantees, profit sharing and ideas like ground rents to equity partners providing land or infrastructure.

Finally, government should once and for all recognise the importance of personal demand-side subsidies to affordable housing and the trade-offs between shallower subsidy, rent levels and benefit costs. Rethinking the design of incentivised, rational and more just housing

allowances could be a new cornerstone from which to build subsidy and affordable finance systems from.

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