Inquiry into British housing 1984–1991

Chaired by HRH The Duke of Edinburgh

What has happened since?

An Inquiry into British Housing was mounted in 1984 to mark the centenary of the Royal Commission on Housing for the Working Classes, and also the Golden Jubilee of the National Federation of Housing Associations. HRH The Duke of Edinburgh, then President of the National Federation, took the chair. The Inquiry's brief was 'to consider inadequacies in the availability and condition of housing in Britain, and to make recommendations to remedy the deficiencies identified'.

The Inquiry report was published in 1985. In the years following publication, the Joseph Rowntree Foundation (JRF) agreed to invest £2m in a programme of research to consider its recommendations in more depth. The Inquiry reconvened in 1990 to look at the evidence, again with The Duke of Edinburgh in the chair. A second report was published in July 1991. Twenty years on from the start of the Inquiry, this paper considers the progress achieved toward implementation of its key recommendations.

The Inquiry recommended removing the inefficiency and inequity of an indiscriminate subsidy (which favoured affluent home-owners more than those on modest incomes and costed almost twice as much as Housing Benefit for people on low incomes). By starting the withdrawal of MITR in line with expected falls in interest rates, home-owners would not be worse off. The Inquiry warned of the ways in which MITR inflated house prices and subsequently boosted equity withdrawal and consumer spending. It also noted that the substantial savings to the Exchequer from ending MITR would easily finance the costs of the Inquiry's other recommendations.

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RECOMMENDATION 1

The phased withdrawal of mortgage interest tax relief (MITR)

Success?

This recommendation in the Inquiry's First Report in 1985 made headline news. And despite its immediate dismissal by the Prime Minister of the day – and the constant pressure on government in the 1980s to increase the ceiling for MITR – it is now the case that MITR has been entirely abolished. The process was made relatively painless by coinciding with falling interest rates.

MITR's phased abolition has already boosted Treasury finances by over £30 billion. Even with interest rates at much lower levels than 20 years ago, abolition of MITR is still saving £3 billion every year – a sum which would be considerably higher if the ceiling for tax relief had been increased in line with house prices.

The Inquiry into British Housing was not responsible on its own for the phasing out of MITR. However, by generating a national debate on a taboo subject, spelling out the inadequacies of this form of subsidy, and repeating these messages over a period of years, a climate of opinion was created in which governments have been able to achieve this change, step by step. As a result:

- a more level playing field exists between owning and renting, and the private rented sector has expanded considerably;
- resources have been freed up for the Exchequer to reallocate to higher priorities than subsidising better-off owners;
- abolition of MITR was a critical factor underpinning the prolonged period of non-inflationary economic growth experienced by the UK since the mid-1990s.

> "Some subsidies are not available to the poor at all. Mortgage interest tax relief is intended to help homebuyers, but it is obviously only available to those who can get a mortgage in the first place. Within the limits of the fixed ceiling, the bigger the mortgage, the greater the relief; and, until 1991, the basic rate tax payer has received a good deal less relief on the same mortgage than a top-rate tax payer…. Many experts are convinced that this relief has the effect of increasing demand and therefore raising house prices – and is consequently counter-productive."
> HRH The Duke of Edinburgh, Preface to the Inquiry's Second Report

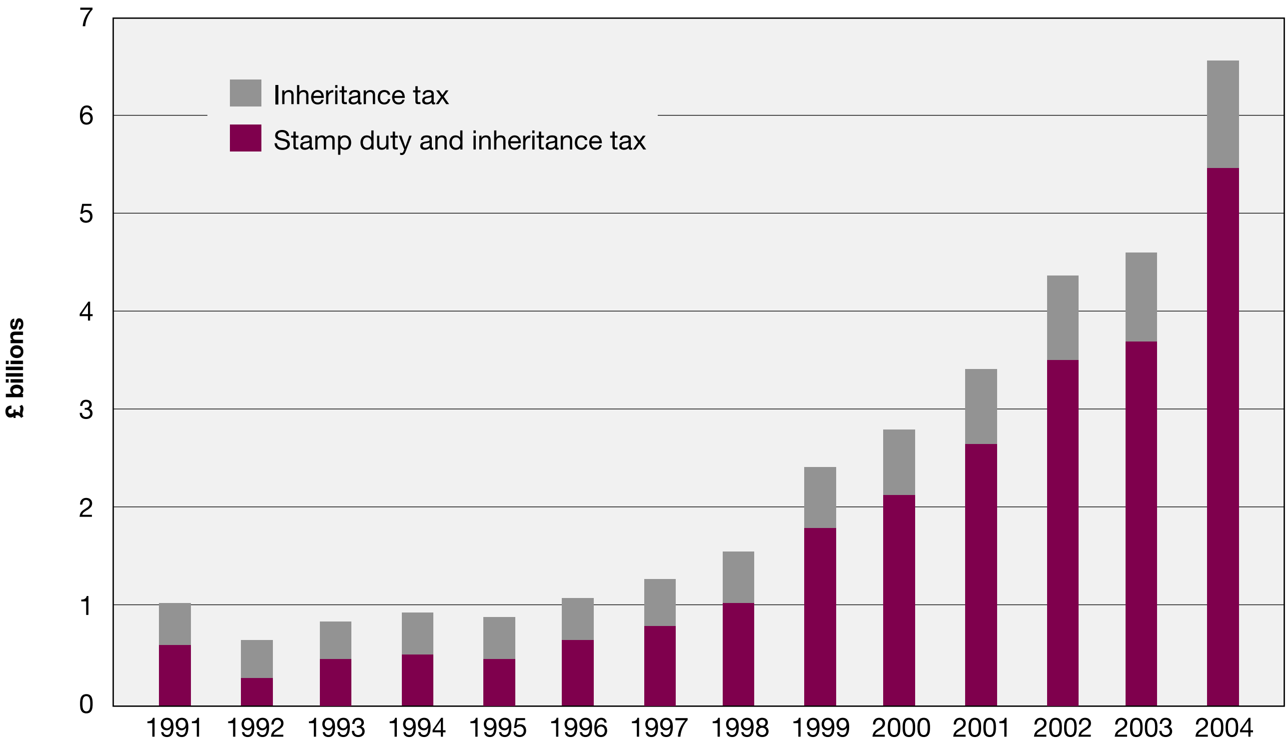
Next steps

Despite the moderating influence of the phased MITR abolition, house prices have risen sharply in recent years. This is partly as a consequence of continued economic growth and low interest rates. But prices – particularly in London and the south of England – have also been inflated by the failure of new house building to keep pace with household growth over the decades since the Inquiry's first report.

These house price rises have reopened debates about the continuing tax advantages for home-ownership in the form of capital gains tax (CGT) relief. However, it remains unlikely that CGT would produce very much here. 'Roll-over' relief would mean those trading up would not pay the tax. Those having to pay would be the people achieving gains when trading down, including those moving into smaller homes from under-occupied property, or going into residential care.

In any event, it may be noted that there has been an increased tax yield from the private housing market through stamp duty, and the element of inheritance tax that is related to residential wealth. There is scope for further reforms to these taxes to make them more efficient, but in the mean time they are now bringing in to the Treasury some £6.5 billion a year (in addition to the annual savings from abolition of MITR) (Figure 1).

Figure 1
Rising tax yield from private housing.



Source: *UK Housing Review 2005/06.*

More important to easing housing problems, and eventually to easing the pressures on house prices, are efforts to narrow the gap between supply and demand; this paper returns to that theme below.

RECOMMENDATION 2

The conversion of all housing subsidies into a needs-related housing allowance

The Inquiry intended that part of the extra revenue received by the government as a result of phasing out MITR would go to creating a new needs-related housing allowance: this would enable person-based subsidies to go not just to tenants requiring help with their rent (Housing Benefit) but to home-owners unable to keep up mortgage payments and to poorer home-owners whose property required urgent repairs and maintenance.

The Inquiry estimated that funding this housing allowance would absorb only a small part of the additional revenue gleaned by the Exchequer from ending MITR. Allocating about £1 billion to supplement the cost of Housing Benefit would have provided sufficient resources to improve the current arrangements and extend support to home-owners by:

- changes to Housing Benefit to help reduce the poverty trap that still results from benefit being withdrawn rapidly as incomes rise;
- restoring Housing Benefit to single people who lost entitlements at the beginning of the 1990s;
- extending the entitlement to those older tenants who cannot obtain Housing Benefit because they have modest capital resources which remove their eligibility;
- providing help for home-owners who encounter financial problems – for example through losing their jobs – and need assistance with mortgage repayments to prevent the loss of their homes;
- providing support toward the cost of urgent repairs and maintenance for (often elderly) owners without sufficient income.

Success?

Help for tenants

There have been as many steps backwards as forwards in Housing Benefit over the last two decades. Recently some modest improvements have been made, including a less restrictive approach to modest household savings and transitional help for households moving into employment. But overall – despite the cost of HB falling because of lower rates of unemployment – the arrangements remain highly unsatisfactory.

Restrictions on the levels of eligible rents introduced in 1996 added to the complexity of the scheme, and discouraged private landlords from letting to claimants, particularly young people. Administratively cumbersome anti-fraud measures also led to a sharp deterioration in the – already highly inefficient – administration of the scheme in many areas. More recently, a succession of reforms designed to improve administrative performance have borne fruit. But more work on this front is still required.

The government has recently piloted 'local housing allowances' for tenants in the private sector, based on average rental costs in each area, with the allowance generally being paid to the claimant, rather than direct to the landlord. The early indications are that this simplified option, which it is now planned to roll out nationally, should be reasonably successful. It has led to a very substantial increase in the proportion of low-income tenants opening bank accounts. And more tenants have sustained tenancies in the private sector with the support of these new allowances, despite fears that landlords would be less likely to let to claimants because of the change to the payment arrangements.

Low-income home-owners

No government since 1985 has attempted to provide a tenure-neutral housing allowance for people needing help with housing costs. Those with mortgages who are in work receive no help, yet low income remains a key source of the mortgage payment difficulties that lead to homelessness.

In this context the JRF launched a new Inquiry into home-ownership last year, and this has now concluded its deliberations. It welcomed the fact that in a benign economic environment repossessions have fallen to low levels. However, the Inquiry also found that the safety net for home-owners in financial difficulties is now less effective than it was in the early 1990s, when repossessions shot up to 75,000 in a single year.

In 1995 the State safety net for home-owners – income support for mortgage interest (ISMI) – was rendered less effective for new claimants. Home-owner households are now required to wait for nine months before they receive any State help with their mortgage costs. A private sector insurance-based safety net was favoured: a voluntary scheme of mortgage payment protection insurance (MPPI). However, a decade later, the take-up of this private insurance has remained very low.

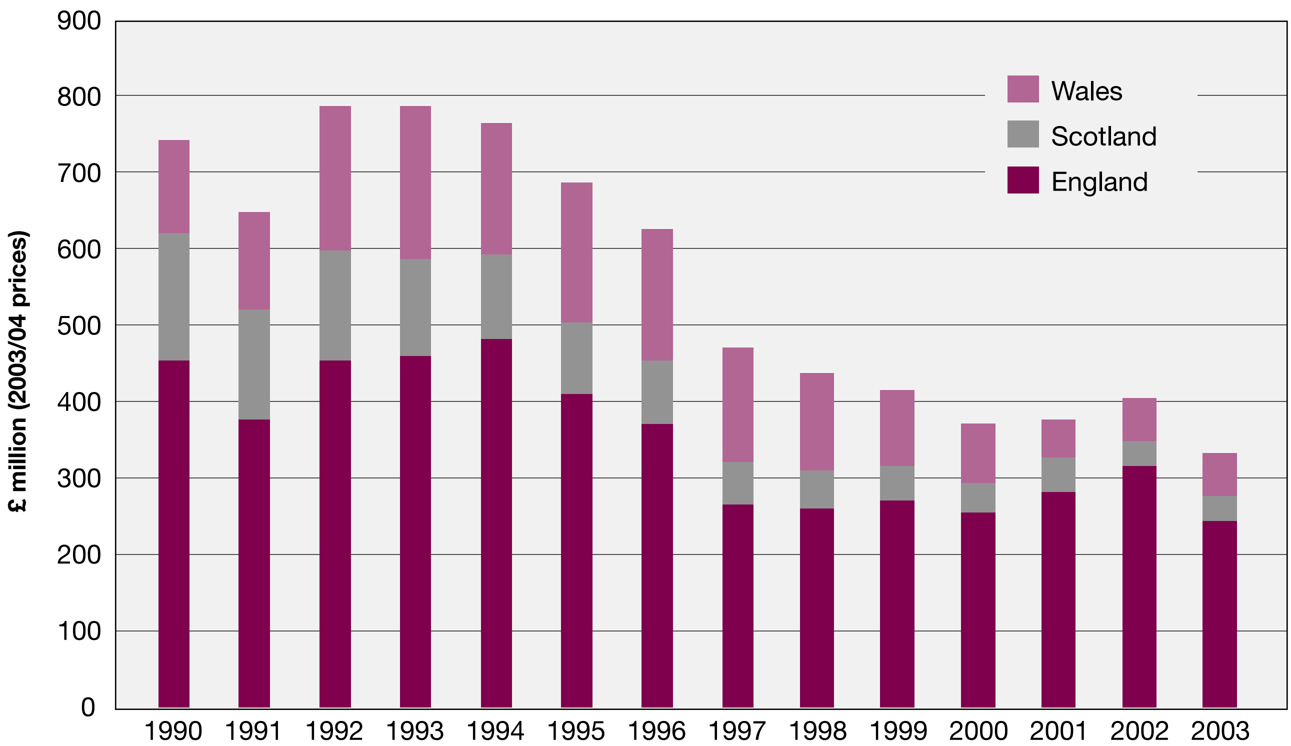
And even amongst those who have taken out insurance, the cover is variable, with fewer households with unemployment rather than health cover, while other risks such as relationship breakdown or reduced earnings are beyond the scope of even the best MPPI policies. The Inquiry found that the gaps in the safety net are now more extensive than they were before 1995: in the event of a severe economic downturn there is a risk of a very substantial rise in repossessions, with the costs that this would entail for the wider housing market and economy, as well as for the households themselves.

While in the short run some reforms are possible to ameliorate the limitations of the current arrangements, in the medium term the Home-Ownership Inquiry argued that consideration should also be given to more radical reforms. This would include further work to develop a proposal for a new 'Sustainable Home-Ownership Partnership' to provide a comprehensive scheme, funded by government, lenders and borrowers, to replace both ISMI and MPPI. The other major reform endorsed by the Inquiry was for further consideration to be given to the proposal for a housing tax credit, linked to the existing tax credit scheme.

Help with maintenance

Meanwhile, there is no sign of extension of support to assist poorer home-owners who are unable to afford urgently needed repairs. Indeed, the position changed for the worse

Figure 2
The decline in home improvement grants.



Source: *UK Housing Review 2005/06*.
Note: Improvement grants excluding disabled facilities grants.

> "Rents and mortgage payments are the most obvious costs of housing. But I have the impression that a need for, and the cost of, maintenance tends to be underestimated. The main fabric of a well-built house may last for centuries, but only if it is never allowed to deteriorate.…People who remain in the same house into their old age are particularly prone to save on maintenance, and when they cannot put if off any longer they are vulnerable to unscrupulous contractors.…Any scheme to help people with inadequate means to house themselves must include some provision for maintenance."
> HRH The Duke of Edinburgh, Preface to the Inquiry's Second Report

for the poorest households relying on Income Support, with the loss of the opportunity to claim 'exceptional needs' payments to cover such repairs. Yet it is now the case that 50 per cent of all those living below the 'poverty line' are owner-occupiers.

Despite important work by local Home Improvement Agencies – 'Care and Repair' and 'Staying Put' organisations – there is only very limited financial help available for maintenance and repair work by owners on the lowest incomes. Government funding for improvement grants to low-income home-owners has been halved over the last decade (Figure 2). Local authorities now have the powers to help home-owners in other ways than with grants, but JRF research (University of Birmingham 2005) suggests little action has followed.

Next steps

Looking ahead, there remains the potential for important changes. The successive reforms to the system of tax credits for low-income working households have served to reduce the number of tenant families who are dependent on Housing Benefit (and have reduced the extent of the unemployment trap for low-paid home-owner households as well).

The proposal for a housing tax credit linked to the tax credit system could build on those improvements, and provide improved work incentives in areas with higher housing costs where the tax credit scheme, on its own, is least effective. The costs of a housing tax credit would depend on the detail, but an initial proposal has been costed at around £1 billion – just a fraction of the income the government currently receives from the abolition of mortgage interest tax relief and the taxes on residential property.

RECOMMENDATION 3

The introduction of a nationwide rent-setting system

When the Inquiry first reported in 1985, rent controls were still in force. The Inquiry recommended new arrangements for rent setting based on the capital values of property. This would give a consistent basis for rents both between landlords and within the stock of individual landlords, and it would offer adequate returns to landlords, thereby encouraging investment in the stock.

In its first report, the Inquiry set a marker of a 4 per cent return on value, for the 'fair rents' set by rent officers for private landlords, and for the rents of housing associations and local authorities.

For private renting

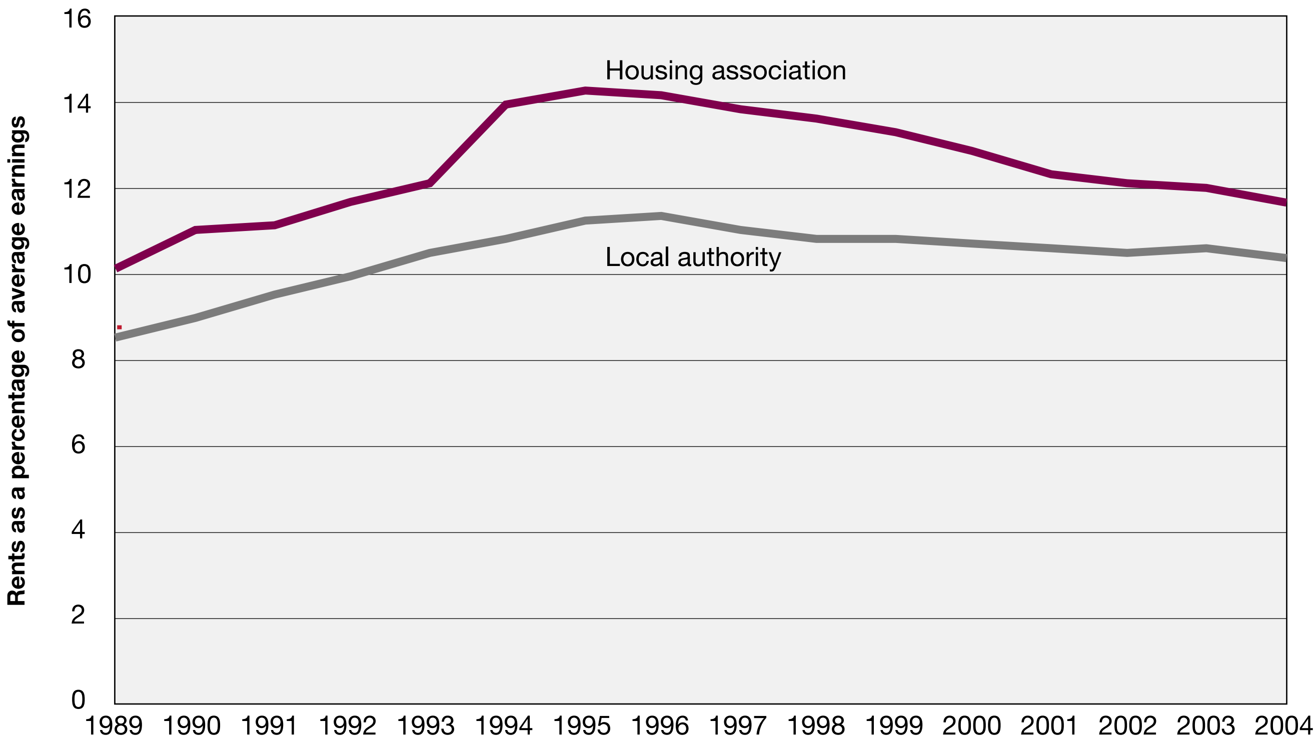
Direct rent controls were removed from the beginning of 1989 for new lettings, assisting the process of letting by the many owners who at that time were unable to sell their properties. The Inquiry felt that, for private sector rents still subject to regulation, and for rents paid through Housing Benefit, their earlier recommendation should stand, i.e. with increases restricted on the basis of 4 per cent capital values. However, to make the 4 per cent return a level acceptable to the market, the Inquiry made the case for tax exemption on these rents where the landlord satisfied some basic regulatory requirements (and became an 'approved landlord'). Freedom from income tax and capital gains tax would greatly increase the total return for the investor. (An open market would remain for landlords operating without tax concessions and without reliance on receipt of Housing Benefit.)

For social housing

The Inquiry was concerned that rapidly rising rents for social housing, even if Housing Benefit could pay them, increased the disincentives for tenants to work. It was also clear that for tenants of housing associations and local authorities, a consistent measure for rents was needed. This would be achieved by basing rents on value, since this reflects all of the factors that make up the popularity of one property compared with another. However, the Inquiry recommended the marker should be a return of just 2.5 per cent on capital value for social housing, to keep a limit on rent increases and to recognise the distinction between the subsidised and private sectors.

Figure 3

Rents in England ease and converge relative to average earnings.



Source: *UK Housing Review 2005/06*.

Note: Housing association rents are for assured tenancies.

Success?

For private renting

The deregulation of the private rented sector in 1989 opened the door to a significant expansion of the private rented sector, and it is now a fully functioning part of the UK housing system. Only a very small proportion of private lettings remain subject to regulation. However, no government of any hue has been persuaded of the value of tax concessions to enhance the return to investors/landlords, although consideration is now being given to the introduction of a reformed tax regime for ‘Real Estate Investment Trusts’.

For social housing

In relation to the subsidised sector, further rent increases above the rise in earnings during the early 1990s worsened the position for many tenants, but subsequently rents have been gradually eased back towards more affordable levels (Figure 3). In 2000, government decided to act to achieve a more rational rent regime in a sector with wildly differing rent levels (between areas and between social landlords in the same areas).

A policy of 'rent restructuring' in England is now in place, and is beginning to ensure a more equitable and coherent structure of rents, both within and between the local authority and housing association sectors. Following a three-year review of the policy, the process is set to continue with only minor reforms, in particular to achieve more rapid convergence between the sectors and to accelerate the reduction of some exceptionally high rents in some localities. It is intended that these measures will be more or less fully phased in by 2011/12.

The rent policy does use capital values as one key component in relating the rent of one property to another, as the Inquiry suggested. However, to prevent vast differences between rents of highest property values and lowest values, the policy also uses an affordability criteria based on prevailing local incomes.

In broad terms, housing association rents now provide a 2 per cent return on value (smoothing values over the housing market cycle). The return on value for local authority rents is marginally lower, but this will increase with the accelerated convergence of rents between the two sectors.

RECOMMENDATION 4

New measures

In the 1980s the public and private rented sectors saw substantial decline: a loss of 1.25 million council homes (and growth of only 0.25 million for housing associations), and a bigger drop of over 1.8 million rented homes in the private sector. The Inquiry wanted to reverse these trends, both to ensure sufficient affordable homes for those unable to buy, and, through market renting, to help job mobility and meet the needs of the growing number of single person households – singles who are postponing family commitments until an older age, or who never marry, or who divorce or separate – for whom owner-occupation may not be the answer.

For private renting

As well as recommending the tax concessions for approved landlords (in return for exercising restraints over rent levels), the Inquiry recommended removing tax disincentives to home-owners who wished to let their properties. It was proposed that lettings by owner-occupiers within their own property (even if self-contained) should be entirely free from taxation, either on the income or the capital gain relating to the proportion of the house which is let.

Moreover, owner-occupiers should be excluded from the requirement to declare income from rents on their tax returns (and those sub-letting who were entitled to benefits should not see these reduced to the point where letting is pointless).

For social housing

In 1985 the Inquiry recommended that the approach to the housing functions of local authorities should give greater emphasis to their strategic and co-ordinating role, supporting the efforts of all providers of housing and enforcing standards in all sectors. It was recommended not only that there should be greater tenant participation in management but also that council property should sometimes be transferred to other landlords.

In 1991, the Inquiry's Second Report returned to the theme of transfers of ownership of council housing, 'which should be to more than one owner'. This time the Inquiry introduced the concept of a free-standing housing unit, still within the council but outside the restrictions of public finance, as an alternative to the transfer of stock to a body outside the local authority's remit.

Under the Inquiry's proposals, the new arrangements would mean that costs of Housing Benefit for council tenants would no longer be drawn from surpluses on rents paid by other tenants: rental income would be retained by the landlord for re-investment. And the landlords of local authority stock would be able to borrow freely from the private sector and use most of the proceeds from sales of council housing specifically for housing purposes.

Importantly, the Inquiry also sought 'grant arrangements that facilitate mixed and flexible tenure schemes which avoid the polarisation and segregation of rented housing'. The point was made that if those in 'welfare housing' were clearly identified as being from poorer households, this can stigmatise and disadvantage the residents.

Success?

Since 1991 the total number of rented homes has continued to decline, albeit rather more slowly. While the social housing sector (the combined stock of councils and housing associations) lost nearly 800,000 properties, and now provides some 4.9 million homes, private renting expanded by about 450,000 properties, and now provides just over 2.6 million homes (Figure 4).

Figure 4
There has been an increase in private renting – but few low-income households are finding accommodation in the sector.

Source: *UK Housing Review 2005/06*.
Note: Data is for Great Britain.

Private renting

Since the late 1990s there has been a huge increase in investment in private renting by individuals supported by the 'buy to let' mortgages made available by mainstream mortgage lenders. However, there has not been the large-scale investment by institutional investors – pension funds, insurance companies, etc. – which the Inquiry hoped to see.

Nevertheless, perhaps helped by the more streamlined valuation arrangements for new Real Estate Investment Trusts, the opportunities for this have now increased. There is a level playing field between renting and owning following the removal of mortgage interest tax relief, and the volatility of equity investments on the stock market has made them less attractive.

> "There needs to be a sufficient flexibility in the housing tenure systems to allow movement of people taking up employment opportunities. However desirable home-ownership may be, selling and buying with every move is both cumbersome and expensive."
> HRH The Duke of Edinburgh, Preface to the Inquiry's Second Report

The JRF's residential investments in City-centre Apartments for Single People at Affordable Rents (CASPAR) in the centres of Birmingham and Leeds have demonstrated that good total returns could be achieved in the early 2000s from unsubsidised private letting in comparison with other investments.

Meanwhile, the Inquiry's recommendations for tax-free lettings by home-owners was adopted by government in 1993 (now applicable for rental income up to some £4,250 per annum); and this change included the helpful concession that it is not necessary to declare these sums to the Inland Revenue.

Social housing

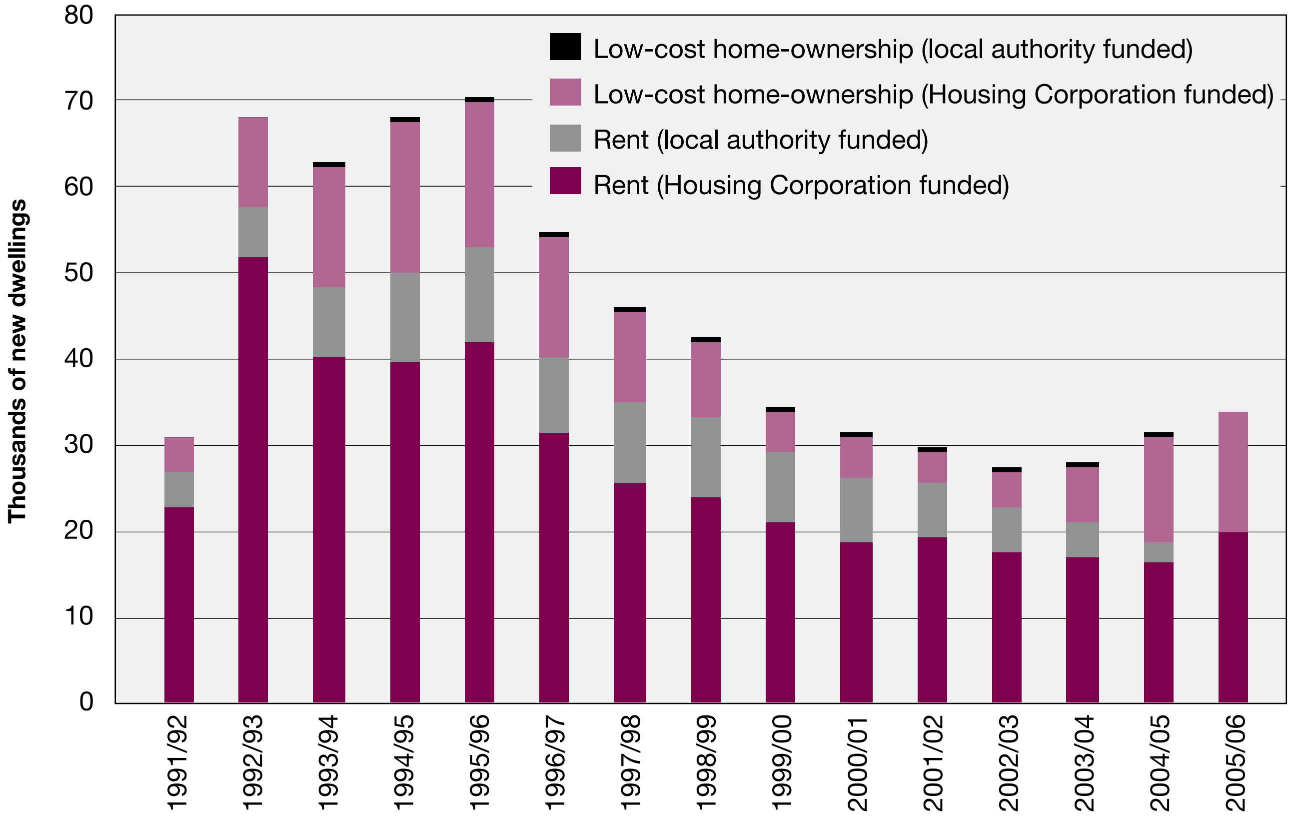
The overall decline in the availability of rented homes is a consequence of the continued depletion of the social sector stock through right-to-buy sales, without an adequate level of investment in replacement housing. Altogether £45 billion has been received from the sale of council housing, the greater part of which has been used by successive governments to offset, rather than supplement, declining programmes of new investment.

Where right-to-buy receipts have been reinvested they have mostly been used mostly to fund (much needed) improvements to the existing stock, not for extra homes. Even if outline government plans to increase investment levels in new social housing in the next few years are realised, this will still leave investment at historically low levels. Housing association output of homes to rent funded by the Housing Corporation and by local authorities has fallen to the lowest level for decades (Figure 5).

The Inquiry's views on transferring local authority stock to new landlords have become policy for all the major political parties. This has led to billions of pounds of private investment already going into the improvement of public sector housing. (In all, housing associations – both new ones created to take over council stock and established ones – have borrowed over £50 billion outside public expenditure constraints since 1989.)

In 2000, the Inquiry's idea of the housing functions of the local authority being at arm's length to the council but outside the restrictions of public finance, was adopted by the government as an alternative to straightforward transfers. This has taken off rapidly and already a third of the council-owned stock in England is now being operated by 'arm's-length management organisations', albeit that they are still subject to some public sector financial controls.

Figure 5
New housing association dwellings.

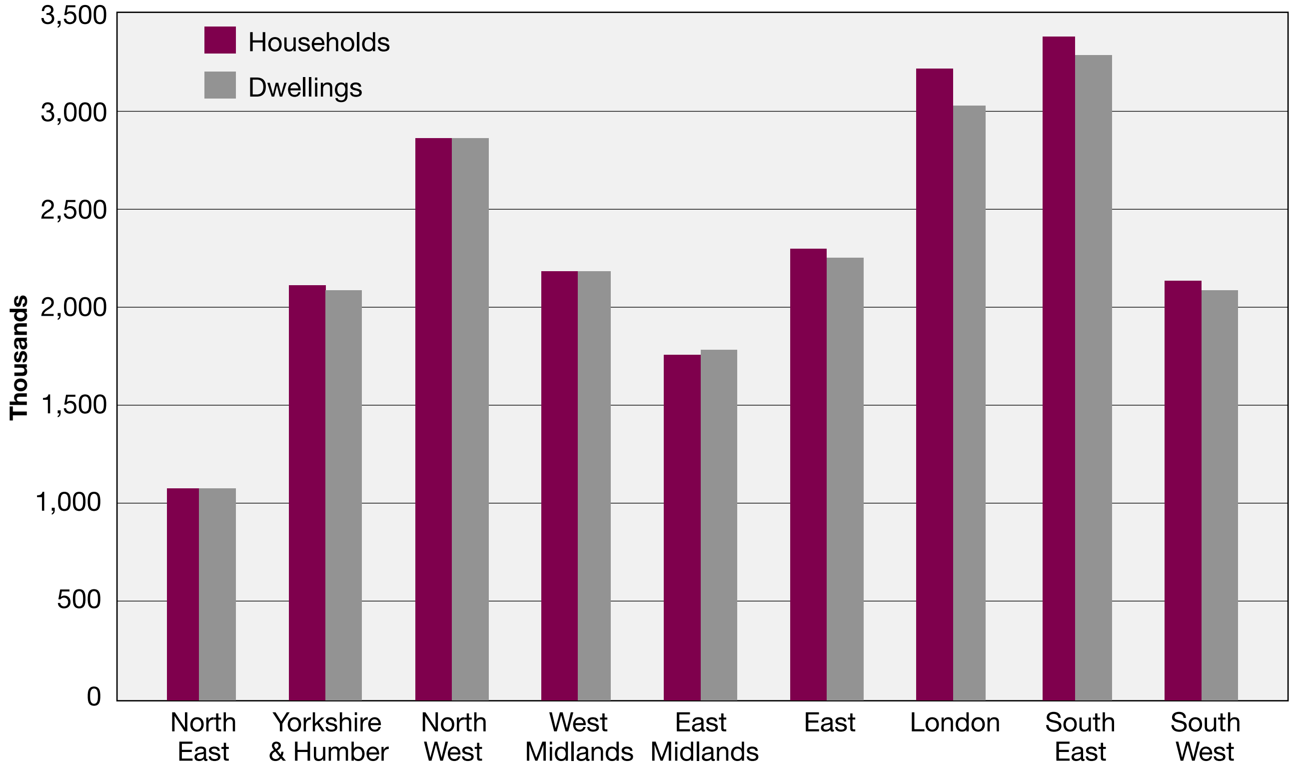


Source: *Housing and Neighbourhood Monitor* (forthcoming, JRF).

More generally, a new financial regime for council housing in England and Wales has ended the arrangement where income from tenants' rents was used to meet the cost of Housing Benefit for other tenants, rather than pay for the services they receive. Nonetheless anomalies remain, the new financial regime is highly complex and redistributive between councils, and, as the Audit Commission concluded in a recent report, it is not conducive to effective management and planning.

Finally, the Inquiry's recommendations that poorer households cease to be segregated in a separate social sector have become central to the housing policy of all political parties. Avoiding the labelling and stigmatising of low-income tenants is accepted as essential not only to enhance the life chances of the tenants but to sustain the value of the new homes. Planning policy now encourages local authorities to require a proportion of newly built homes in private sector developments to be affordable to those not able to buy on the open market; and the funders of social housing – principally the Housing Corporation – are charged with ensuring that new social housing is integrated within a mixed community, containing full ownership, low-cost home-ownership and rented properties.

Figure 6
Regional household dwelling deficits in the south in 2003.



Source: *Housing and Neighbourhood Monitor* (forthcoming, JRF).
Note: 'Dwellings' exclude second homes and a 2 per cent vacancy reserve.

In conclusion

On balance, can it be said that the recommendations from the Inquiry into British Housing have now found their way into public policy and practice? In a number of major respects they have. But there are significant omissions from the current housing agenda.

First, savings from the removal of mortgage interest tax relief have not been applied to the reform of Housing Benefit and the creation of an adequate safety net for home-owners whose financial circumstances take a turn for the worse (or who need to fund urgent repairs that they cannot afford). Recent purchasers with substantial mortgage commitments are more at risk now than their counterparts were two decades ago, should higher unemployment return and/or interest rates rise. And, as well as continuing problems with administration in many areas, the Housing Benefit system remains unduly complex and fails to support work incentives: new reforms are a modest start on the road to major improvements in the system.

Second, shortages of affordable homes in areas of economic growth – particularly London and the South East – have grown over the last two decades (Figure 6). Supply has fallen, with house building at historically low levels. Using planning requirements to create affordable housing, in place of funding social housing directly, is not replacing the need for direct subsidies. An absence of both market and affordable housing means essential public services and growing businesses cannot secure the staff they need. Without major initiatives – perhaps including regional economic policies to redirect growth to less pressurised regions – overcrowding and homelessness is rising again. Those falling between social housing on the one hand and housing for sale on the other are becoming a significant proportion of the whole.

Strong economic growth and falls in unemployment have masked the underlying weaknesses in our housing systems over recent years. More has been done to ensure that housing schemes make use of urban brownfield sites, but this is not sufficient to remove the need for new developments on some 'greenfield' land in many parts of the country. Increased output of new homes is essential not just to match the growth in household numbers, but also to ease house price pressures, which otherwise will mean many of the next generation will be denied access to home-ownership.

Many of the key recommendations in the two reports from the Inquiry into British Housing have been taken on board, to good effect. Important, parallel work is being done to regenerate areas in need of economic and social revival. But underlying housing problems remain nationwide. Without the underpinning of a needs-related housing allowance, large numbers of households are at risk of being impoverished by their housing expenditure, or even becoming homeless. And with cutbacks in the building of social housing, alongside barriers to private house building which heighten scarcity, acute shortages are causing considerable problems, particularly in southern England.

Richard Best
Secretary to the Inquiry
December 2005

Special thanks to Professor Steve Wilcox, University of York.

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