

Housing benefit: time for reform

Housing benefit is currently under scrutiny as part of the Government's comprehensive reviews of departmental spending. A study by Professor Peter Kemp of Glasgow University examined the housing benefit scheme, placing particular emphasis on its relationship with work incentives and with the efficiency of the housing system. The research found that:

f Rising housing benefit spending has been caused by a restructuring rather than an overall increase in subsidies to housing. Since 1988/89, housing benefits received by housing association and private tenants have risen substantially, but at the same time the volume of social housing subsidy and of mortgage tax relief has fallen.

f Problems with the current system are:

- Housing benefit affects the 'poverty trap' through the withdrawal of benefit as other income rises. This 'taxes' away most of the additional income from employment and is inconsistent with the Government's over-riding objective of making sure that 'work pays'.
- Recipients have no incentive to shop around for cheap accommodation, negotiate lower rents, or move to smaller accommodation if their present home is larger than they need.
- Paying housing benefit directly to landlords undermines individual responsibility where tenants have all of their rent met by the scheme.
- Recent changes have largely affected private tenants with deregulated tenancies, whilst for other recipients benefit has remained unchanged.
- There are significant administrative problems for tenants and their landlords, especially in the private rental market.

f Lowering social housing rents would cut the number of housing benefit recipients and reduce benefit dependency, but the flaws in the scheme would still require reform.

f Phased reform is practicable and could include:

- Replacing housing benefit with a housing tax credit based on average local rents, differentiating between private, housing association and local authority tenants.
- Introducing a 'housing allowance scheme' for private tenants to subsidise the gap between actual rent and a minimum rent contribution (financed by increased social security benefit).
- Over time, reforming social housing rents to reflect local capital values, paying housing benefit direct to social housing tenants, introducing a notional rent contribution and eventually a 'housing allowance scheme' similar to that for private tenants.
- Simplifying administrative rules and limiting the need to re-adjust benefit when only minor changes in claimants' circumstances have taken place.

Housing benefits

Housing benefit is a means-tested social security benefit administered by local authorities on behalf of the Department of Social Security. It is paid to low-income *tenants*, including people in work, as well as those who are not in paid employment such as the unemployed, lone parents, elderly, sick and disabled people.

Housing benefit schemes can have either *housing* policy objectives or *social security* policy objectives. They can be used as instruments to enable low-income households to live in better or more adequate housing than they would otherwise choose to do (a housing policy objective). Alternatively, housing benefit can be seen as a means by which households can reduce the amount they spend on housing out of their own pocket; by spending less on housing they can afford to devote more of their budget to other items (an income maintenance objective). In practice, however, housing benefit schemes invariably perform both of these functions, though one or the other is often dominant. One of the problems which has beset housing finance in Britain is the tension between the housing and the income maintenance objectives of housing benefit.

Shifting the costs of housing support

Since 1988/89, housing benefit expenditure has increased in real terms, particularly in respect of rent allowances paid to housing association and private tenants. Between 1988/89 and 1996/97, there was a fivefold increase in rent allowance expenditure compared with a twofold increase in rent rebate expenditure paid to council tenants. The number of recipients has also gone up, rising from 4.1 million in 1988 to 4.6 million in 1997.

Assistance in the form of benefits and subsidies

Total assistance with housing costs, however, also involves subsidies to reduce the cost of providing social housing as well as benefit payments and tax relief to mortgage payers. This total assistance has remained broadly constant in real terms in Britain since 1988/89. Furthermore, although the housing benefit caseload has fluctuated over time, the total is slightly lower than it was in the mid-1980s.

Some commentators have argued for a reversal of the shift from direct subsidies to housing providers to personal subsidy. The result would be to reduce social housing rents and thereby the number of recipients of housing benefit and hence benefit dependency. It would also make it easier for working households to extricate themselves from the poverty trap. But even if rents were to be reduced, the housing benefit scheme itself would remain unchanged and its flaws would still be present.

The need for reform

Housing benefit suffers from four major problems: work disincentives, the lack of a 'shopping incentive',

a lack of equity between tenants, and administrative problems.

Work disincentives

Housing benefit plays an important part in the poverty trap because the withdrawal of benefit as other income rises can leave people little better-off from taking a job or getting more pay. A system that taxes away almost all of the marginal benefit from employment is not consistent with the Government's over-riding objective of making sure that 'work pays'.

Shopping incentives

Housing benefit recipients are fully insulated from changes in their rent, neither gaining nor losing from a rent increase. The scheme therefore gives recipients no incentive to shop around for cheap accommodation, bargain a lower rent with the landlord, or move to smaller accommodation if their present home is larger than they need. In addition, the payment of housing benefit directly to landlords undermines individual responsibility where tenants have all of their rent met by the scheme.

Equity between tenants

The recent changes to housing benefit largely affected private tenants renting on assured and assured shorthold tenancies. Almost by default, two systems of housing benefit are now emerging in a more or less *ad hoc* way, one for recipients living in the deregulated private rental market and one for all other recipients. This development has created a lack of equity between these two groups of tenants.

Administration

Research has found significant variation in the quality of housing benefit administration between different local authorities. The difficulties surrounding housing benefit administration can create significant problems for tenants and their landlords, especially in the private rental market.

Options for reform

Improving work incentives

Work incentives could be improved by reducing the rate of benefit withdrawal as income rises (known as the 'income taper') and by increasing the 'earnings disregard' (the amount that someone can earn without benefits being reduced).

Reducing the income taper or raising the earnings disregard would improve work incentives but also increase the number of people affected by the poverty trap. It would also increase the cost of housing benefit at a time when the Government is trying to reduce it, although the cost of reducing the income taper could be minimised by confining the change to people in work. To some extent, there is a *policy conflict between containing the cost of housing benefit and increasing work incentives*.

A housing tax credit?

For households in work, it would be feasible to replace housing benefit with a housing tax credit. This would help to reinforce the financial benefits of working as against being on benefit and increase the number of low-income working households getting help with their housing costs. But while a housing tax credit would create clear water between benefit and work, it could also make it more difficult for unemployed people to bridge the gap. People would gain from being in work, but moving between benefit and work could become more financially hazardous, especially if the work on offer is only temporary.

If a housing tax credit for people in work were to be introduced, then it would need to be based on the average rent in the local authority of the recipient's place of residence rather than on the national or regional average. For each local authority area, there would need to be a different level of credit for private tenants, housing association tenants and local authority tenants, because rents in these three tenures differ significantly.

Shopping incentives

A shopping incentive could be built into housing benefit by introducing a housing allowance scheme similar to those that operate in many other countries. These 'housing gap' schemes subsidise part of the difference - the gap - between actual rent and a minimum rent contribution. For example, a housing allowance scheme might meet 90 per cent of the difference between a claimant's actual rent and a minimum rent contribution.

In the short term, the proposed housing allowance scheme could be confined to the private rented sector (see below). In order to make the reform feasible, certain changes would need to be made. First, social security benefit rates would need to be raised for those with a liability to pay rent and who are therefore eligible to claim housing benefit. Second, the increase in benefit rates should be calculated as a percentage, not of the national average rent, but of a local 'benchmark rent' in each area. This would be necessary because private sector rents vary significantly between regions and local authority areas. Third, the tenant contribution should be set at a relatively low amount such as 10 per cent. Thus, social security benefit rates for tenants would be increased by 10 per cent of the local 'benchmark rent' and housing benefit would be calculated on 90 per cent of the tenant's actual (eligible) rent. In this way, a small shopping incentive would be introduced into the housing benefit scheme. Because the tenant contribution would be relatively small, the possibility of financial hardship would be minimised.

The 'benchmark rent' should be set at an amount below which it is possible for all housing benefit recipients to find accommodation in their locality. If the benchmark rent is set at too low a level that would create financial hardship and undermine support for

the reform. There may also be a case for raising social security benefit rates by more than the required 10 per cent in order to give tenants more room for manoeuvre.

Improving efficiency and equity in social housing rents

The present flat pricing structure in social housing is an obstacle to reform of housing benefit (and vice versa). Rent differentials between comparable local authority housing and housing association accommodation are also an important obstacle to reform. Both social housing rent structures and housing benefit are in need of reform; but it is equally clear that to reform one and not the other would be self-defeating. What is required is a co-ordinated reform of both of them.

Reform of social housing rent structures

One way forward would be to devise a target rent structure for social housing towards which local authorities and housing associations would gradually move over time in a series of steps. For example, social housing target rents could be set as a percentage of the capital value of the dwelling. Rents would continue to be below market levels but the important point is that capital values would provide a reasonably consistent basis on which to set social housing rents for different properties so as to reflect their size, location and quality. In order to move towards the target rents, the annual rent increases would initially need to be focused on the dwellings with rents *below* the target amounts. The rents of dwellings in excess of the target amounts would remain the same until the target rent catches up with the actual rent. The transition to target rents could take some years to achieve.

At the same time, social housing allocation systems could, where necessary, be reformed to allow for transfers within the stock to take place much more quickly and easily in cases where tenants are living in accommodation larger or smaller than their requirements. Landlords with hard-to-let properties could be encouraged to advertise vacancies for letting at target rents on a first come, first served basis.

Reform of housing benefit for social housing tenants

At the same time as the reform of rent structures is underway, worthwhile *short-term* changes could be made to the housing benefit scheme. First, housing benefit could be paid directly to the recipient and not directly into tenants' rent accounts. An exception would need to be made in a small number of cases where tenants are deemed incapable of taking on the responsibility of paying the rents themselves. Some critics have argued that social housing tenants are too poor to be trusted to pay the rent themselves, but this seems unduly pessimistic.

Second, a *notional* rent contribution could be introduced. For social housing tenants, a standard 'housing addition' could be added to social security

benefit rates. Housing benefit would then be calculated on the full rent minus the housing addition. Thus, social housing tenants would receive the same amount of help towards their rent as at present but part of it would be paid with their social security benefit and the majority with their housing benefit cheque. Social housing tenants would thereby make a contribution to the rent out of their 'own' pocket, but the size of their pocket would be increased to make it possible for them to make that contribution.

In the *longer term* - once these two reforms have had time to bed down - it should be much more feasible to carry over the housing gap scheme from the privately rented sector. Because of the differential in rents between private and social housing, the tenant contribution would be set at a lower level for local authority and housing association tenants than for private tenants.

Improving administration

Administration could be improved by simplifying the rules governing the scheme or limiting the need to constantly re-adjust benefit where only minor changes in claimants' circumstances have taken place. For example, housing benefit could be awarded at a fixed rate for the duration of the benefit period; entitlement would only be adjusted where either income or rent increased or fell by more than a specified trigger amount. Alternatively, housing benefit could be awarded for fixed periods of six months, as is already the case with family credit; it would only be re-calculated if the recipient specifically requested it on the grounds that a major change in circumstances had occurred since the original award. Both of these options would modernise housing benefit administration in line with the realities of the 'flexible' labour market and would cut administration costs, but they would also result in higher housing benefit payments in some cases.

Conclusions

Although the cost of housing benefit has grown considerably in real terms since 1988/89, this has been offset by a reduction in spending on other housing subsidies. In other words, there has been a shift of expenditure within a stable overall total. It is important to remember that this shift has reflected some important developments in housing policy: the replacement of public finance by private finance in new housing association developments and local authority stock transfers; greater value for money in social housing grant; and the deregulation of private rents and the expansion of the privately rented sector.

The downside of this shift in housing support is

that it has brought a greater number of households into 'dependency' on housing benefit and hence within the scope of the poverty trap. This problem is exacerbated by the current design of the housing benefit scheme. Rather than reverse the shift in housing support, a more realistic option would be to change those features of the housing benefit system that encourage dependency and undermine responsibility.

While some of the changes proposed could be introduced immediately, others would need to be implemented in stages to avoid undue financial hardship and to allow the housing market time to adjust without major disruption.

About the study

This study was undertaken by Professor Peter Kemp of the Department of Urban Studies, University of Glasgow. He reviewed the literature and statistics on housing benefit, and held meetings with a number of officials.

How to get further information

The full report, *Housing Benefit: Time for reform* by Peter A Kemp, is published by the Joseph Rowntree Foundation (ISBN 1 85935 044 5, price £11.95 plus £1.50 p&p). It is available from York Publishing Services Ltd, 64 Hallfield Road, Layerthorpe, York YO31 7ZX, Tel: 01904 430033, Fax: 01904 430868.

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