

Notes on affordable housing definitions for Affordable Housing Review

The key issue is having disaggregated definitions – ie different definitions for different target groups. Recent government policy has been mistaken in having a single definition (for example any housing at a less than 80% of market price or market rent) rather than disaggregated definitions. This approach has made a nonsense of the term 'affordability'. Most critically, affordability must relate to the income of the specific target group for whom a home is provided or intended. There is also a need to distinguish between affordability of home ownership (home owners acquiring an equity) and affordability of rented housing, where renters do not acquire an equity but solely the right to occupy accommodation, often for a time limited period.

We also need to be clear the purposes for which a definition (or definitions) of affordability are to be used – for example:

Rent setting in social housing (local authority or housing association)

Rent control in the private rented sector

Determination of capital subsidy for new social housing

Determination of revenue support to households to afford housing which is otherwise unaffordable

Planning policy ensuring use of development capacity for a specific target group assessed as being in housing need.

A number of changes in government policy have introduced concepts of affordability which do not relate primarily to incomes or relate to only one income cohort.

The Barker review focused solely on access to home ownership, focusing on the ratio of average household incomes to average house-prices, disregarding the fact that 50% of households had incomes below the average. This approach was for many years the key driver of housing supply policy at a national level, with no targets set for different types of sub-market housing.

In the early 2000's, the Housing Corporation moved away from a grant model which took rental affordability into account in determining capital grant levels. This led to increased rents of new development leading to significant increases in revenue support to households through housing benefit.

The target rent system, applying to existing tenancies, also introduced a 25% property value- based component into social housing rents, relative to the 75% income- based component.

National planning policy was revised to remove disaggregated definitions for different types of sub market housing, which meant local authorities were no longer allowed to set separate planning policy targets for social rented homes related to household incomes (irrespective of the findings of Strategic Housing Market Assessments).

In recent decades, two alternative approaches (amongst others) have been proposed;

a) a universal housing allowance paid to all households, with households having the flexibility as to whether to use the allowance for a rental payment, a mortgage payment, or in the case of shared ownership, a combination of the two. In some variations, this would not be means tested, and consequently would be paid to households who did not need financial support. Moreover it would not distinguish between households using the allowance to pay for rights of occupation in rental housing and households using the allowance to acquire property equity.

b) residual income methodology. One version of this (promoted at one time by Prof Peter Ambrose and London Citizens) was to fix individual rents on the basis of the income and expenditure requirements of individual households, rather than in relation to the costs of providing the housing.

In defining affordability, it is important to determine what an occupant should be paying for. For example, should a household acquiring an equity pay a higher proportion of their income on housing costs, than a household renting who does not acquire any equity? In relation to rental housing, should a household pay only for management and maintenance costs or also contribute to the original capital cost of provision, even where the capital costs have already been covered either by subsidy or the rental payments of previous occupants, which will normally be the case in social housing which is more than 30 years old?

These different factors make it essential that we have different definitions of affordability for different household types, both in different income groups, but also in different housing circumstances and tenures. Any definition however requires a judgement not just as to what a household should be paying for but also on what proportion of their income should be spent on housing costs. The latter judgement should reflect some estimate of 'reasonable' housing expenditure relative to expenditure on other items, but also a judgement as to the extent, if any, to which households housing costs should be subsidised, which may also reflect a view on a) whether or not all households have a right to decent housing, and how 'decent' is defined and b) what other costs (for example food and clothing) should be regarded as essential expenditure to be prioritised above housing costs, and which should be regarded as less essential or luxury items.

There is also the difficult balance between capital subsidy for housing provision and revenue subsidy to individual households to assist them with accessing housing which is unaffordable (applying whatever criteria is determined). From a public expenditure cost effectiveness perspective there is a case for arguing that a) subsidy in any form should only be provided to households who cannot 'afford' market housing (whether for sale or market rental), and that b) that capital subsidy for social rental housing should be sufficient to ensure that rental costs are affordable by the majority of households in employment thus reducing the requirement for revenue subsidy to the minority of households not in active employment.

For the purposes of simplicity, I would suggest the following:

- a) that for the lowest income households (for example the lowest quartile) housing costs should not exceed 30% of average incomes for that cohort.
- b) that for middle income households (unable to access market housing) housing costs should not exceed 30% of average households for that cohort
- c) that where a household is acquiring a property equity through property purchase (or part purchase) 40% of average incomes for the relevant cohort is appropriate.

In relation to b) and c) the income cohort will vary regionally and locally according to the proportion of local households who can access market housing. The cohort will therefore be much wider in London than in areas where the average household income to market price ratio is much lower.

This approach was used in the definitions of different types of affordable housing in the original 2004 London Plan and Housing Supplementary Planning Guidance (2005). Such criteria have the advantage of ensuring planning applications for specific development can be assessed against

specific affordability criteria and policy compliance. This process in fact operated for major development schemes in London between 2004 and 2007, using the financial viability appraisal process which incorporated an affordability assessment; ie: an assessment of costs to prospective occupier relative to benchmarks derived from the set affordability criteria. These benchmarks were updated on an annual basis to reflect changes in incomes of the relevant income cohort. The use of such criteria can also ensure that public subsidy, whether direct or indirect, is only utilised where it is necessary to ensure affordability by the income group at whom the housing is targeted.

In relation to access to home ownership, while a measure of income: house-price ratios can assist monitoring of changes in affordability, it does not necessarily track the proportion of households in an area who are not already home owners who can afford to access market homes of different sizes and quality in different locations, which is the important policy issue. As recent experience has demonstrated, subsidising access to home ownership tends to have inflationary impacts. Alternative policy measures such as reducing land costs, construction costs and constraining developer profit margins would have more effective impacts on costs, while policies for managing demand to ensure demand is limited to households intending to effectively occupy (ie neither under-occupying or overcrowding) homes (both new and second-hand) rather than purchase primarily for investment purposes, would also be necessary for there to be a significant increase in market affordability.

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