Affordable Rental
Issues for consideration in developing a land-based scheme

1. Current position

The following is the summary position with policy on Affordable Rental, as contained in the *Rebuilding Ireland* 2nd quarterly progress report, published in February 2017:

- It has been decided not to proceed with the Affordable Rental Scheme as originally conceived and outlined in the Rebuilding Ireland Action Plan.
- As set out in the Strategy for the Rental Sector published in December 2016, the commitment to introduce affordable rental is to be progressed through kick-starting supply in rent pressure zones. Lands held by local authorities in rent pressure zones are to be brought to market on a competitive tendering basis, with a view to leveraging the value of the land to deliver the optimum number of units for rent, targeting middle income households, in mixed tenure developments.
- The cost of providing rental units is to be permanently reduced by lowering the initial investment and development costs for providers - AHB or private - allowing the rental units to be made available at below market prices without the need for ongoing rental subsidies.
- The local authorities concerned will identify a number of sites with the potential for up to 1,000 units of accommodation and will move forward, as soon as possible, to issue calls for proposals from parties interested in developing projects. As speed of delivery will be critically important, appropriate licence arrangements, incorporating clear timescales for delivery, will be a key feature of the process.
- This programme is being co-ordinated with the dedicated measures in Rebuilding Ireland to accelerate housing output from the Major Urban Housing Delivery Sites, including support from the Local Infrastructure Housing Activation Fund (LIHAF) where necessary.

2. Issues arising with the original scheme

- The initiative to develop an affordable rental scheme arose from recommendations made to the Social Housing Proposals Clearing House Group. The announcement was made by the Minister for Public Expenditure and Reform in October 2015.
- The scheme as initially conceived was expected to work on the basis of tenants paying the majority of the rental cost from their own resources, with the State helping to meet the shortfall through a subsidy payment to the accommodation provider.
- The measure was being designed as a supply-side measure to increase the availability of affordable rental accommodation.

- It took D/HPCLG almost 12 months to design a workable scheme. Technical assistance was provided from the National Development Finance Agency, the Housing Agency, the Housing Finance Agency, NewERA and the Department of Finance Statistics Unit. The original scheme was not considered acceptable for various reasons. A number are now summarised.
- There was a concern that it would lead to a sense of expectation and entitlement amongst a broader group. There was a view articulated in policy discussions with other key Departments that these expectations could not be fulfilled with a scheme that could deliver some 2,000 units, based on the available funding of €10m per annum.
- From the early development work on the scheme there was a difference of view between D/PER and D/HPCLG on the potential target group. D/PER appeared to see the scheme as part of the social housing sphere, with eligibility limits set accordingly. The D/HPCLG position was that the scheme needed to target a different group with a housing need – variously titled the 'working poor', 'squeezed middle' or 'key workers'. Data analysis indicated that a significant group of people on moderate incomes were no longer in a position to afford to buy a home, and were also paying unaffordable rents. This group were outside the margins of eligibility for social housing, but in danger of falling into this category.
- The scheme was mainly a supply-side measure. In order to work in being attractive to investors in delivering supply, the tenant had to be in a position to afford to pay 70% of market rent. With data showing that most social housing tenants had a social welfare payment as their primary income-source, the affordable rental scheme would not have worked for this cohort.
- The following were the proposed income thresholds for eligibility, based on the analysis of data for incomes and rents in the Dublin region.

Net income (gross income in brackets)	1 bed apartment	2 bed apartment	3 bed unit
Minimum	€34,913 (€35,500)	€35,575 (€39,000)	€38,238 (€42,600)
Maximum	€42,000 (€48,000)	€46,000 (€53,600)	€50,000 (€59,200)

- Inputs and observations which were received from D/PER in August 2016 were the subject of an 11-page response from D/HPCLH. Subsequently, a combined observations paper was received from D/PER and IGEES in November 2016. This contained policy criticisms and technical comments on the draft Business Case. The technical comments (reckoned to be from IGEES) were considered to be constructive and could have been accommodated without major difficulty. The more policy-focused comments were not amenable to being addressed without undermining the viability of the scheme. Many of these comments had already been raised and addressed in the August 2016 exchange with D/PER.

- There was a criticism that the level of subsidy was too generous. However, modelling indicated that the terms of the scheme, while potentially attractive to investors, were realistic compared to alternative property-based investment options. The attractiveness could be considered marginal, and not generous. This was a key point of difference in interpretation.
- In terms of the day-to-day operation of the scheme, D/HPCLG saw the provider of the units playing a key role. Considerations here were the supply-side nature of the scheme, the allocation of risk to the provider, and the importance of keeping the transaction off-balance sheet. D/PER made the case for more active local authority involvement in allocation and management.

3. Considerations in designing a new scheme

Similar issues as were present with the original subsidy-based scheme will still need to be addressed. Firstly, some critical questions arise:

- Will a local authority have responsibility for setting its own terms for an affordable rental scheme?
- Will a local authority be in a position to design its own scheme (and be able to access the necessary technical resources)?
- What would be the role of the developer in determining the terms of any scheme at a particular location?
- Can and should the Department guide or prescribe the design of any scheme?
- Will the approval of D/PER be necessary?

The new land-based scheme envisages the subsidy to deliver affordable rental properties being provided through discounted land. The cost of this subsidy and its value to the developer will still need to be monetised. It will have to be converted into a cash equivalent to ensure that the value of the land is being sufficiently captured for the benefit of the local authority. The value of this land will then need to be fully reflected in discounted or 'affordable' rents over some defined period. As with the earlier scheme, a number of questions again arise:

Income eligibility

- What are to be the income thresholds for eligibility?
- How are the income thresholds to be determined?

Rents

- How are the rents to be set (with reference to the market rent in an area, or through some other means)?
- How much does the tenant pay?
- What is the value of the discount? (a 30% reduction on market rent was proposed in the direct-subsidy model).

Administration

- How do prospective tenants apply?
- Who assesses the eligibility of occupants (local authority, AHB, provider/developer)?
- Who collects the rent?
- How do occupants leave the scheme on becoming no longer eligible?
- What criteria other than income are applied in selecting tenants?

There are many more design considerations which were identified in the Business Case for the subsidy-based scheme which would need to be addressed in a land-based approach. Leaving aside design considerations for the moment, a simplified illustration of how a land-based subsidy model of affordable rental might work is described below.

4. Simple illustrative model

This model looks at how the value of a notional site might be captured through the delivery of social housing and units for affordable rental.

> *There is a site valued at €2million in Dublin City which is offered to a developer on condition that social housing and affordable rental units are provided to the local authority. Private housing is also to be included which gives a profit margin to the developer. This arrangement would notionally provide for 5 social housing units, 10 units for affordable rental and 10 units for private sale, as follows:*
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> - *€1m of the value is recovered through the provision of 5 social housing units, based on an equivalent delivery cost of €200,000 each.*

- *€1m is recovered through 10 affordable rental properties to be let by the developer. The market rent for a two-bed unit in the area is €1,388 per month, or €16,656 per annum. The value of a discount of 30% on this annual rent is €5,000. The household will pay the discounted rent of €11,656 per annum. The cost of the €5,000 annual discount over a 20 year period (not accounting for inflation) is €100,000 per unit. This benefit amounting to €1m is captured in the deal, but passed on to the tenants through discounted rents over the 20 year period.*
- *The developer builds a further 10 properties on the site for private sale.*

With this model, the developer is responsible for renting the affordable properties as the landlord and retains ultimate ownership. An issue to consider is whether the local authority or an AHB could fulfil this role. Neither of these bodies is currently active in the 'affordable' rental space. The Government accounting implications of any arrangement would also be a consideration here.

5. Discussion with D/PER on designing a new scheme (24th February 2017)

At a meeting on 24th February 2017 the high level principles and issues that might be associated with a new form of affordable rental scheme based on the provision of a land subsidy was discussed with officials in DPER. The areas discussed and key conclusions arising from that discussion were as follows –

- A key consideration for D/PER is how the scheme would be paid for as there is presently no budget available for the scheme. There are two options in this regard –
    - If the scheme is to be funded from the Exchequer then the Department would have to make a case for additional funding in this regard as part of the capital review that is currently ongoing,
    - If there is no Exchequer cost proposed by the scheme i.e. the local authorities are bearing the cost, then there is no requirement for D/PER approval as long as what is done does not impact on the government balance sheet.
- In the circumstance that local authorities 'go it alone' on the scheme (i.e. there is no recourse to the Exchequer) there will still be a requirement for them to comply with the public spending code and show value for money.
- The treatment of land value and how the land might be provided to a developer in any such arrangement to provide affordable rental properties should also comply with the terms of the spending code in that regard.

- Provisions for the disposal of land should be consistent with Department of Public Expenditure and Reform circular 17/2016, *Policy for Property Acquisition and for Disposal of Surplus Property*.
- D/PER confirmed that at official level there is agreement that the proposed income thresholds for eligibility, based on the Departments previous analysis of data for incomes and rents in the Dublin region, can be used to provide guidance to local authorities in respect of the household income groups at which such affordable properties should be aimed. These proposed income thresholds are set out in the table included in section 2 of this note.
- Related to this, consideration will need to be given to whether local authorities should be able to vary the level of land subsidy provided. A lower level of subsidy could be provided which would consequently vary the proportion of market rent that the tenant will be obliged to pay. For example, rather than a 30% rent reduction being applied, the subsidy could be less than this, say between 15% and 30%. It was agreed that should this approach be implemented there should be a minimum land subsidy agreed as a threshold below which there is little value for the State in taking on the administrative burden of providing this type of arrangement especially where there is consequently little beneficial impact on the tenant.

6. What can be considered as 'affordable'

Using the widely accepted measure in housing policy, 'affordability' has been understood as a situation where rent constitutes 30% or less of income. Once the proportion of a household's net income used to meet rental costs moves above 30%, this can have a negative impact on their quality of life. In the worst case scenario this can lead to people having to move home. It can also push households towards applying for social housing. A key aim of the Scheme is to bridge the gap between what a prospective tenant can afford and the market rent in a given area. Therefore the Scheme will need to require that an applicant household has to be able to meet the majority of the cost of the market rent in an area. In the modelling completed previously the effect of the subsidy was pitched at a level so as to bring the proportion of a households income expended on rent to around or below 30%; therefore, this ratio of rent to income is the reference point around which eligibility was to be assessed. In addition, the subsidy should work for people within a range of incomes, and not just at the maximum threshold. Consequently, an income band, rather than a fixed cut-off point was decided as more appropriate way to assess eligibility.

Housing Funding Mechanisms,

03 March 2017.