

# Paradoxes in the Provision of Affordable Housing in Britain

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## Introduction

A policy of providing affordable or social housing has grown up in Britain since the mid-nineteen nineties. It is a policy which has grown up on an ad hoc basis. Its logic has never been properly thought through. Like Topsy, it has 'just grown'. But what has 'just grown' is a rickety structure which largely fails to achieve its avowed objective - the provision of housing at a low cost to the less well off. The aim of this paper is to set out the paradoxes and contradictions in current policy.

## The Back Story

For most of the last century 'affordable housing' in the UK was provided by local authorities in the form of what was called 'council housing'. The construction of housing by local government began in the nineteen twenties, implicit in Lloyd George's promise of the construction of 'homes fit for heroes' in the 1919 General Election, the so called 'khaki' election. In the interwar period much of this housing was provide in the form of large housing estates, such as the London County Council's 'cottage estates' consisting mainly of semi-detached and detached housing, modeled on the ideas of the garden city movement.

After the Second World War much of the new council housing was built in inner areas, often through the rebuilding, or 'comprehensive redevelopment' of severely bomb damaged areas such as the East End of London and the clearance of what was regarded as slum housing in these inner areas. Most of this development was in the form of blocks of flats, obviously at a much higher density than the old cottage estates. Indeed building high was encouraged by central government in the form of increased subsidies, on the grounds that this saved land. Though, in practice, it was found that densities were not that much higher, since it was felt that large areas of amenity space should be left between and around the tower blocks.

Very large numbers of homes were provided in this way. In the fifties the then Housing Minister promised that 400,000 homes a year would be built, and this target was achieved in the late fifties, when half of the new homes were built by local authorities.

The policy of building large blocks of flats eventually fell out of favour in the nineteen seventies, and it did so for several reasons, social, architectural, and political. The architectural reasons are exemplified by the collapse of Ronan Point in the early seventies after a small gas explosion; suddenly the construction of tower blocks, often 'system built', no longer seemed such a good idea, particularly when the land savings did not appear to be so great, and the blocks

were not popular with the tenants. The reasons for this, the social reasons, have been set out recently by Lynsey Hanley (2007) in her book Estates, set out, moreover, from an occupant's point of view, not, for once, as the reflections of a visiting sociologist.

And the political reasons are demonstrated in the election of the Thatcher government in 1979, with its distaste for action by government of any kind, and with the promise that the occupants of council housing would be able to buy their homes at a substantial discount. In consequence the construction of new council housing virtually ceased, and what had been constructed in the past was sold off.

But this left an unsatisfactory situation. Housing was becoming increasingly expensive as house prices rose in real terms as fast if not faster than incomes because of the planning constraints on the availability of land. The young and the poor could find little which they could afford either to rent or to buy, and the Conservative governments in power between 1979 and 1997 were unwilling to finance the construction of further council housing by local governments. They were, however, willing to assist an increase in the provision of 'social housing' by Housing Associations.

A solution was found by John Major's government in 1995. From then local authorities could require, as a condition of granting planning permission – called a Section 106 agreement, that a proportion of the homes in any large housing development should be in the form of 'affordable housing', usually in the form of homes sold to a housing association at less than market price. Since then most affordable or social housing has been provided in this way.

### **The First Paradox – A Tax or Not a Tax**

The first thing about the policy which strikes one as problematic is the nature of the 'condition' which is being agreed between the housing developer and local government. It would appear unarguable that the requirement that developers should provide affordable housing is actually a tax on the development of land for private housing. It is, moreover, hypothecated tax, a tax where the proceeds have to be used for a specific purpose. The British Treasury is well known for its opposition to hypothecated taxes. They limit the Treasury's freedom of action. Such taxes when they have existed in the past in the UK have only lasted a short time before the revenue has been diverted into general fund. An example is the motor vehicle duty which began life as a contribution to a Road Fund, but soon became just a tax on the ownership of cars.

But though the cost to the developer of providing affordable housing appears to be a tax, it is not called a tax. Indeed the developer actually agrees to pay it as part of an agreement, although the term 'agreement' does not mean that the contribution is in any way voluntary. Pay up or else you don't get your planning permission is the actual situation.

But maybe the fact that the tax can be represented as an agreement is the factor which finds favour with the Treasury. Because it is an agreed contribution, and because its cost is nowhere calculated, it does not appear in any statistics either of government income or government expenditure. In this way the extent of government involvement is minimized. It is very much taxation by stealth.

But when seen to be a tax, one other peculiarity stands out. If it is a tax on the development of land why should it only be imposed on the development of land for housing? Why should it not also be imposed on the development of land for commercial purposes, for offices, shops or industry? Surely a tax which is imposed only when land is developed for one kind of use, residential development, will discourage that use, making house prices higher and less 'affordable' for everyone else. This is even more striking when it is realised that Governments have usually adopted the reverse position, taxing commercial buildings more than housing. So VAT is imposed on the construction of new commercial buildings but not imposed on the construction of new housing. And the annual property taxes imposed on commercial buildings in the form of Business Rates, have, since 1989 when Domestic Rates were abolished, been much higher than the Council Taxes imposed on residential properties.

### **The Second Paradox – Why is Housing Unaffordable?**

This brings us to the major contradiction in the policy. The attempt to make housing affordable when the whole drift of planning policy for the past fifty years has been to make housing more expensive, i.e. less affordable. It is a story which has been told many times before but it is worth relating it again.

In the nineteen forties plans were drawn up for the future development of Britain's conurbations, for example the Greater London Plan or the Clyde Valley Plan. According to these plans land was allocated for the future development of the towns and cities. The demand for land was predicted on the basis of assumptions that the population would not increase very much and that incomes and car ownership would also not increase very quickly. But the population did increase, as did the number of households as these got smaller, and both incomes and car ownership increased substantially.

The result was an increasing demand for housing and for land for housing – but the land allowed to be used for housing did not increase at anything like the same rate. Instead there was an implicit policy of constraint, first documented by Peter Hall et al in two major volumes on The Containment of Urban England, published in 1973.

The implicit policy of constraint resulted in house prices and land prices rising faster than the price of other goods, sometimes much faster. In her recent report on the supply of housing, for example, Kate Barker (2003) notes that the price of housing in England rose by about 3.5% per annum in real terms over the last thirty years whereas the western European average has been about 1%.

Thus, as a result of government planning policy housing became more expensive and less affordable. Of course it has to be admitted that the price effects of the policy of constraint were not widely recognized, indeed were for some time denied. Thus in 1987, Steve Grigson, writing on behalf of the South East Regional Planning Association, argued that the constraints on the availability of land did not affect the price of housing – that the increase in the price of land and the cost of housing was solely due to increasing demand. The argument was contested by Evans (1988), and the then Department of the Environment commissioned an inquiry by Gerald Eve and Associates and the Dept Land Economy at Cambridge. They reported, in 1992, that the supply side did matter, that constraints on the availability of land, when in conjunction with rising demand, did indeed result in housing costs being higher, higher than they would have been without the constraints on supply.

Thus it can be said that since 1992 the higher levels of government should have been aware that a major reason for high and rising house prices has been the constraints imposed on the availability of land for housing. I write 'should have been aware' since the Department of the Environment received the report in 1992 but did not say that they accepted it. And one may still meet government planners who will state firmly that supply constraints do not affect house prices. (There are none so blind as those who won't see!)

Given, however, that all economists will agree that supply is important, and that limitations on supply result in housing being more expensive, there is at least an implicit contradiction in trying to provide, at the same time as the constraints are in operation, more housing which is cheaper, particularly through section 106 agreements.

In the first place, the constraints on the availability of land tend to be tightest in the south of England where the demand is greatest. The intention of the constraint is presumably to stop more households moving to the south because it is regarded as too crowded. The point is rarely made explicit but was, for a short period in the late eighties, expressed as government policy both by Margaret Thatcher and by Nicholas Ridley, her Secretary of State for the Environment (Evans, 2004).

But if the intention is to discourage migration into the South of England, why then, at the same time, try to encourage it by attempting to provide more housing which is cheaper. And if the total supply of housing is what is to be regarded as limited, it follows that if more affordable housing is to be provided then the supply of other homes becomes even more limited and their cost will be even higher.

The contradiction is most explicit with regard to what is called 'key worker' housing – the provision of low cost housing for occupation by people in occupations which are needed in southern England but whose wages or salaries

are not high enough to allow them to afford to live there. These occupations – teachers, police, nurses, and so on – are almost invariably in the public sector. So while the economics of constraint mean that housing is made expensive in the south to deter people from moving there, so that, in the private sector, wages then tend to be higher which then discourages firms from moving or expanding there, the provision of key worker housing becomes a way of exempting government from the impact of its own policies. The state alone should be allowed to employ people at less than market rates since it can use its powers to save itself from having to pay higher salaries by getting cheap housing to be provided for state employees. The cost, of course, falls on the rest of the population since housing costs are made even higher. But once again this increased cost does not appear in any schedule of taxes. It is literally a form of taxation by stealth, a claim which is often made by the current opposition. Usually the claim is synthetic since it is about actual taxes, in this case the claim would be true.

### **The Third Paradox – Lack of Achievement**

The third paradox is that despite, or perhaps because of, all these problems the policy is not successful in achieving its apparent intention, the construction of affordable housing. Councils may set targets but few of them are achieved.

For example the City of Edinburgh has as its target that twenty five per cent of new housing in larger developments should be in the form of affordable housing. In the six years, 2001/02 to 2006/07 permission was given for the construction of 16,700 new dwellings and 12,200 were completed. In the same period permission was given for the construction of 1,350 affordable homes, and 225 were actually built. Note that 1,350 is substantially less than ten per cent of total permissions, indeed it is rather less than ten per cent. The reasons why the number of completions falls far below the number of permissions may lie in delays in construction and other factors which are not our concern here. But the ratio of affordable completions to affordable permissions is much less than the ratio of total completions to total permissions, and that has to be explained. A major reason is almost certainly that developers are likely to delay the construction of affordable housing, on which they expect to lose money, and to construct the rest of the development first, if possible. The cash flow from the whole project is clearly much more favourable if the affordable housing is built as late as possible so an incentive to delay construction is built into the policy. (With the recent downturn in the property market it has been suggested that the position will have changed, albeit briefly. Developers committed to putting flats which are difficult to sell can improve their cash flow by building the affordable housing earlier since Housing Associations will be more able and willing to pay for the properties on completion than private buyers would be.)

The reasons why the proportion of total affordable housing permissions is less than half the target are likely to be several. The most important is that the target only applies to 'large' housing developments. What is defined as 'large' varies from

local authority to local authority and between ten and twenty five units, but the economic effect remains the same. Developers will find smaller schemes much more profitable than larger since no affordable housing has to be provided. As an implicit tax the affordable housing requirement is a disincentive to building larger schemes. A developer acquiring a site on which a few flats can be constructed has no incentive whatsoever to extend the site to build a few more. After all a developer building ten flats in a London suburb can build ten flats for sale on the market. The fifty per cent rule in London would mean that if the site were doubled in size so that a further ten flats can be built, they would all have to be affordable and would not add to total profits, indeed would reduce them.

Evidence of this attitude is the way householders in London suburbs have been leafleted by developers suggesting that if two neighbours would agree to sell their adjacent houses, then the developer would agree a price and obtain planning permission to demolish their houses and replace them with a small block of flats. But there is no suggestion in these leaflets that three or more houses would be sought or would be better. Because of course the builder has a disincentive to increase the size of the development.

If large green field sites were being built over it would be difficult for developers to avoid providing affordable housing by obtaining planning permission for a lot of small developments and building over a site in stages. But another government policy assists a strategy of avoidance. It is government policy that most new housing, at the least sixty per cent, should be built on green field sites. Many such sites are likely to be small, for example the sites of unprofitable filling stations or public houses, so no affordable housing needs to be provided.

So, since many new housing developments are too small for affordable housing to be required as part of the section 106 agreement, none is provided on these sites. Even if only one third of new housing is provided in this way, the proportion built as affordable housing will fall by a similar percentage.

But there may be other reasons why local authorities may not insist on the full target percentage being provided. Since the Section 106 approach is supposed to result in an agreement rather than a mandatory requirement, some flexibility is seen to be in order, and sometimes local authorities may have, from their point of view, more important policy objectives than the provision of affordable housing.

For example, whilst this is not widely known, a developer can claim that the price paid for the land is so high that providing a large amount of affordable housing would make the whole development unviable and so ask that the amount required should be reduced. And there is in existence a document and computer program called the GLA Affordable Housing and S.106 Toolkit: Guidance Notes (2007-8) which allows a local authority to input data on land prices, the prices which could be obtained for the new homes, tenure mix, etcetera. This allows the authority to check, using its own figures, the developer's assertions and to come

up with a lower figure for affordable housing. To cite an actual example, a development of 400 flats on a brown field site near the centre of the London Borough of Harrow was granted planning permission in May 2008. In that case the requirement stipulated was that 35% of the space (27% of the homes) should be affordable. At the meeting of the Borough's Strategic Development Committee the Labour members (the Borough is Conservative controlled) asked why this was and were told that the reason was that the price paid for the land was so high that to require 50% of the space to be in the form of affordable housing would make the development unprofitable, and it could not then go ahead.

The paradox is that the major part of the site consisted of a library and car park both of which were owned by Harrow Council. And a Harrow Council spokesman is on record as saying that the Borough had to get a high price for their land in order to pay for the refurbishment of the local leisure centre, and that this meant that they had to permit a large number of flats to be built on the site. Basically what happened was that the Borough, or rather its Conservative administration, traded off the provision of affordable housing against the achievement of its objective, improving leisure facilities.

This example is one the author became aware of because he is a resident of L.B .Harrow and happened to be at the meeting at which the application was approved. But it is clear that a policy of allowing a reduction in the provision of affordable housing requirement because the development would otherwise be unprofitable is widespread. The evidence for this view is precisely the fact that, as stated earlier, a test has been developed and formulated as a computer program so that Councils can input the figures and come up with a yes or no answer. Information on the program is available on a website, though use of the program has to be paid for.

It is its availability which is indicative of the availability of such trade offs. Though it has to be said that to an economist the whole procedure of arguing that the cost of acquiring the land was too high to be able to afford the 'implicit' tax seems rather odd. One cannot imagine, say, the Her Majesty's Revenue and Customs would be sympathetic to, say, a jeweller who said that he'd paid too much for the gem and the gold so could they let him off paying the full rate of VAT because otherwise he would only be able to sell the ring at a loss! He would get short shrift because otherwise the tax authorities would face such claims from every business. But if local authorities do reduce the requirements then it only encourages developers to overbid for the land. The very existence of the program is an invitation to tax avoidance. Thus once again we run up against an indication of what a rickety contradictory structure the whole affordable housing policy is.

And it is because of its ad hoc nature that the policy breaks down. Because councils are not behaving like tax collectors and laying down that the requirement

will be enforced, the tax, which is what it is, becomes discussable, variable, almost, in some circumstances, optional.

Nowhere is this made more evident than when, indeed, the requirement is simply not enforced. This can occur if the developer agrees to pay, under the Section 106 agreement, money which allows the local authority to achieve some other objective. Of course it might be argued that that is what was happening in the case set out earlier. But it is laid down that anything which is required to be contributed under a Section 106 agreement must be 'related' to the development, and it would have been difficult to argue in court that the refurbishment of a leisure centre was related to the construction of 400 flats a mile or more away across the borough.

As it happens, however, Harrow can provide an example of such an application. In early 2008 an application was made to for the development of a site adjacent to Harrow on the Hill rail and underground station to build about 400 flats. The site is currently occupied by a College of Further Education, Harrow College. Under the application as negotiated with the Council's planning officers, under the Section 106 agreement the applicant was to pay £5m as a contribution towards the improvement of public transport facilities, primarily at Harrow on the Hill Station. In view of this contribution any requirement that affordable housing should be provided on the site was to be waived. The application was recommended for approval by the officers, but refused by the committee on the grounds, somewhat surprisingly, of its effect on a nearby Conservation Area. Although the application was in fact refused, nevertheless the point remains. In such an application the requirement that affordable housing should be provided may be waived if an equivalent contribution is being made towards other objectives.

The examples outlined above help to explain why so little affordable housing may be provided as a proportion of total housing permissions. The council itself may have other objectives which it finds of more importance than the provision of affordable housing. Developers will wish to obtain planning permission and helping the council to meet its other objectives will increase the probability of obtaining permission, and may be cheaper than providing affordable housing. After all the fifty per cent target was laid down by the then Labour Mayor of Greater London, not by the Conservative administration of Harrow. In many cases it follows that not meeting the target is likely to be in the interests of both developers and councils, and so that the actual provision of affordable housing will fall well short of the target set. And therefore that trying to provide affordable housing through Section 106 agreements is an inefficient way to meet this policy objective.

## **The Fourth Paradox – The Paradox of Location**

And so we come to the paradox of location. There would seem to be a presumption that affordable housing should be provided for those who are in need of it. And such people will generally be found in more deprived areas. But private housing will be built by developers who know their market, and so where the demand for private housing is greatest, where incomes are relatively high and demand is high.

But these are not necessarily the locations where there is a need for cheap, subsidized housing for the poor. That is likely to be in areas where incomes are low and the demand for private housing is low, where the degree of deprivation is high and poverty greatest with the most need for housing support. But in such areas the construction of new private housing is likely to be relatively low, and, where private housing is built, the local authority is in a weak position if it tries to argue that a high proportion of the housing being built should be 'affordable'.

Thus Edinburgh, a relatively prosperous city, may be able to have a policy of requiring 25% of new housing to be affordable, and even then, as we showed earlier, the proportion achieved falls far below this. Glasgow, on the other hand, is a much larger city but with much greater degree of deprivation, but with a low demand for new housing can achieve little.

Of course from a neoclassical economist's viewpoint, there is an argument for encouraging people to move from areas where the demand for labour is low to areas where it is high. But as we noted earlier in this paper there is an implicit contradiction in trying to meet this objective when planning policies seek to prevent the expansion of towns and cities in areas where the demand for labour is high. And this brings us back to the point made at the beginning – the provision of affordable housing through Section 106 agreements, to the extent that it is effective, only serves to reduce the supply of other housing which, because the supply is in this way being further restricted, becomes even less affordable than it otherwise would have been.

## **Conclusions**

We have tried in this paper to demonstrate that the policy of providing affordable housing through Section 106 agreements is ill thought out and full of contradictions, a rickety and incongruous structure. Why has this come about? It has done so because governments, both central and local, have seen that the result of the continuing constraint on the availability of land has been that planning permission is worth money. Governments, both central and local, have therefore sought to gain some advantage from giving planning permission. Developers, also aware that obtaining planning permission is worth money, have

become willing to cede some of that money to government in order to obtain the rest. So in the end, both parties are willing signatories of a 'voluntary' agreement.

Economists should, perhaps, be in favour of such voluntary agreements. But as we have tried to show the system has a number of failings. Firstly, relatively little affordable housing is actually provided in this way because the requirement can be avoided by building small rather than large developments. And because local authorities and developers can subvert the affordable housing requirement in order to achieve other objectives which the local authority sees as more important. Secondly, what housing is provided is provided where the demand for private housing is greatest, not where incomes are low and the need for affordable housing greatest. And, thirdly, the policy of encouraging cheaper housing in areas where demand is greatest and land values highest is in contrast with planning policies which seek to discourage people moving these areas.

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