



Response to “Briefing Note on the Impact of the new Housing Benefit Subsidy Changes for Local Authorities and Housing Associations from April 2011 and opportunities presented for Local Authorities”

1. Take accommodation on licence to prevent or meet homelessness duty
2. Develop a Social Letting Agency

Introduction

As stated in our newsletter, I have rarely been more disappointed or concerned than when I read the above titled ‘briefing note’. Disappointed, because given the title of the paper I expected something more groundbreaking, innovative and business-like from a high profile consultant with a Government background.

Concerned, because if Local Authorities do indeed follow the advice given in the ‘briefing note’ there are a number of huge issues that arise for them. I have clarified these issues below, replicating statements from the original briefing note in italics **and my response in red**.

Overview of the briefing note

The ‘briefing note’ explains to us how the current Housing Benefit subsidy rules can be used to allow Local Authorities to procure more private rented accommodation through the use of licence agreements. These are licence agreements with Landlords as well as with Tenants.

The paper states that by using licence agreements, the Local Authority will be able to incentivise Landlords through the HB subsidy, whilst at the same time taking a small surplus to cover the Local Authorities’ own costs. This is then the start of a completely new and equally disturbing section on how this could develop into a Social Letting Agency.....

Issues for concern

Practical Issues

1. Why would Landlords be interested?

Some quotes from the briefing note include:

“A Council should sensibly set out its licence agreement with a private Landlord to include: a no voids rent clause, make all repairs the responsibility of the Landlord, no fixed lease term, no handback costs”

“(Under this arrangement) the interest in the property remains with the private Landlord and therefore ...the Landlord remains responsible for repairs, maintenance and voids”

“A Local Authority may, as part of the licence, include some minimal management duties by the Local Authority such as monitoring or visiting the property”

The big issue here is, forgetting the legalities for a moment (we’ll come to that later), that the first hurdle for any scheme is to create a ‘product’ that Landlords want to use. What is being offered by a scheme suggested in the briefing note is, slightly more rent (using the subsidy rules) and the Local Authorities bond or deposit.

What is the risk for the Landlord for this additional benefit? The Landlord gets no rent during any void periods yet has no control over the Tenant or the Local Authorities internal processes. So if a Local Authority removes a Tenant (for whatever reason, but lets say a Tenant who stops paying their rent), the Landlord is the one who suffers. The Local Authority must give the Tenant at least 4 weeks notice and obtain a court order to remove them, so this is potentially a long process. However, once removed, the Landlord receives no rent until the Local Authority places someone else in the accommodation!

The Landlord receives no fixed lease term. So what security is there for a Landlord? The Local Authority can hand back the property at anytime without penalty. Great for the Local Authority, but why would you sign up to such an arrangement if you were a Landlord? For a little extra rent? I doubt it!

In my experience Landlords are likely to be concerned if all you are offering is MINIMAL management duties as part of the service you are offering! Bear in mind you are competing against High Street Management Letting Agents, Guaranteed Rent Agents and possibly local leasing schemes. By offering “minimal” management of Housing Benefit Tenants (who, fair or not, are widely regarded by Landlords as more hassle than other Tenants), you not only continue a long tradition of Local Authority revolving door schemes, costing you more in the long term, but you offer nothing like the service that a Landlord can get elsewhere.

So without getting onto the issues with repairs, maintenance and ‘handback costs’, you are already creating a product that is not commercially attractive to Landlords. It offers them nothing more than your current private sector access scheme, in fact it just presents more risk, as they have no direct control over the tenant or your processes.



2. Security of Tenure for Tenants

I seem to remember that most of us got into housing as a way of improving lives for Tenants. In recent years we have looked at Enhanced Housing Options and there are now companies such as Ethical Lettings who look to improve Tenants quality of life, not just 'dumping them in the private sector so we can save some money and tick a box'. I'm afraid that is exactly what licence agreements as outlined in this briefing paper do, they offer the Tenant nothing to improve their life in the longer term.

The briefing paper states;

"As the Local Authority would not have any property rights to the accommodation it cannot offer the occupant anything more than it holds from the Landlord. Therefore the occupation agreement.....will be a non secure tenancy"

"The occupant will be occupying the accommodation under a licence agreement which provides him/her with limited rights"

If the intention here was to create short term accommodation as an alternative to B&B use, then I have no problem with accessing that type of accommodation as part of your overall approach to dealing with homelessness. However the briefing paper is quite clear that what you are doing is using the subsidy rules designed to free up short term private sector accommodation, to procure properties which you then put people in for much longer terms, "with minimal management".

Firstly given the difficulties in persuading some Tenants to use the private sector, why would Tenants agree to be put in such a situation, and secondly, why should we be putting Tenants in this situation anyway. Is this why we got into housing? To use short term subsidy rules to put Tenants into clearly unsustainable private sector accommodation, without a thought to quality of life or future prospects? For a minute forget the message it sends out about how we do business for people in our area, but it's the classic 'revolving door' 'box ticking' approach and is shameful if it's the best sustainable option we can offer to those threatened with homelessness in our area.

At the other end of the scale to this shameful approach, have a look at what the innovative Tenant focused people at companies like Ethical Lettings can offer to Tenants and to Local Authorities;

<http://www.ethical-lettings.com/>

Now isn't that the way forward, sustainably housing people, using 'profits' to develop services that offer Tenants better financial stability, education, training and employment opportunities, and all at a saving to the Local Authority through a long term business plan. It makes the short-termism and opportunistic approach outlined in the briefing paper look even more out-dated and short-sighted.



3. The risk to the Local Authority

Ok, so we have established that if there is a void, the Landlord is the one that doesn't get paid, so no risk to us as a Local Authority there (as long as we don't mind a bit of bad press and damaged Landlord relations!).

But what happens then if the Tenant stops paying their rent or gets into arrears? Who carries the financial exposure in this case? The briefing paper isn't clear on this, but there are only two options and I'm sure it would be clearly stated in the licence agreement between Local Authority and Landlord. Either the Local Authority covers all losses from rent arrears or the Landlord does, there are no other options!

If it's the Landlord, it's a further reason (in case they needed anymore) as to why your scheme is so commercially unviable. They have no control over the choice of tenant, the duration of stay of the tenant or the removal of the tenant, yet they carry the loss for any non payment of rent? Umm, tough sell!

Ok, so the Local Authority carry the loss instead do they? An issue for later is that the briefing paper does not factor in any rent arrears losses to the calculations on how to set up a 'money making' Social Lettings Agency. However, before that we need to consider that if the Local Authority is to carry losses for rent arrears, what is our financial exposure likely to be?, what are our eviction procedures? and how long will this process take in reality (i.e. what is our likely financial exposure per tenancy)?

Only once we have answered these questions can we begin to consider whether developing a Social Letting Agency is the answer to our private sector procurement issues, and if it is, what sort of model will help us reduce the risks (such as financial meltdown due to rent arrears) to the Local Authority.

The financial risk element is a make or break issue for any business. Even if you had a great product, a willing customer base (Landlords in this case) and a sound cash flow forecast, the whole business could fall on this one issue of an acute and under-estimated financial risk. I'm amazed that the briefing paper does not even touch on it!

4. Short-term approach

A classic (and often well founded) criticism of Local Authority approaches to issues. "Only focused on the here and now", "No long-term strategic approach", "Lack of a business-like approach" and so on. Unfortunately this is exactly what this briefing paper advocates:

"....the subsidy rules allow the Council to plan its business until at least March 2013"



Then what!?!?

The paper says nothing about life after this date, but focuses on poor and undetailed financial suggestions, (more of which later), about how a scheme would work whilst the subsidy was in place.

Can you imagine for a moment that you are on Dragons Den with your new scheme as outlined in the briefing note. The Dragons ask you what will happen to your financial plan post-March 2013? It turns out your whole scheme is based upon current favourable (and clearly intended as short term) subsidy rules. Your model simply doesn't work without the subsidy.

Questions: Are you telling your Landlords that the product you currently offer them may end in March 2013? How will you deal with the Tenants and tenancies you have created from now until that date, that will become financially unsustainable from March 2013? What will happen to the scheme you have set up? How will you continue the scheme, or more likely, how will you withdraw from the scheme without huge losses or damaging press and publicity (meaning you'll likely never work with local Landlords in your area again)?

We have said consistently that if you are going to set up a Local Lettings Scheme, it must be on a sound and realistic financial footing. Not just as a sensible business approach, but from a credibility point of view, as well as bearing in mind you are dealing with peoples lives (Tenants) and livelihoods (Landlords).

The scheme as outlined in the briefing paper is classic short-termism and with no back up plan will result in catastrophic failure of your scheme when the subsidy situation changes.

Legal Issues

5. Can you agree a licence between Landlord and Local Authority?

The briefing paper states: "Accommodation will be deemed to be held on a licence as long as the elements of a tenancy aren't met. The elements of a tenancy are IDENTIFIABLE PARTIES AND PREMISES, PAYMENT OF RENT, PERIOD OF TENANCY AND EXCLUSIVE POSSESSION".

The briefing paper goes on to state that it believes a tenancy isn't created because, "a key element is that the Local Authority does not have exclusive possession or control of the property".

It goes on, "Any written agreement should be careful to express that the Local Authority has been granted permission to use the property but does not have exclusive possession. The licence could state that the Local Authority will use the property on a night by night basis.....or state that the Landlord will



provide accommodation without naming the actual properties in advance, stating that the Local Authority will pay rent only when the accommodation is occupied and stating no fixed end date”

Even forgetting the Landlords willingness to work on such an ad-hoc and unprofessional basis, in my mind any court would clearly see that a lease or tenancy arrangement exists, not a licence. This shouldn't present too many Landlord / Local Authority relationship problems though, but does have knock on effects for the Local Authority / Tenant relationship.....

6. Can you agree a licence between Local Authority and Tenant?

Now, if you agree that you can't have a licence between Landlord and Local Authority because conditions for a tenancy exist, then you remove the one thing that the briefing paper depends upon for the relationship between Local Authority and Tenant;

“The Local Authority cannot offer to the occupant anything more than it holds from the Landlord. Therefore the occupation agreement provided to the Tenant will not be a non-secure tenancy (as it would be under a lease).....but would be a licence agreement providing the Tenant with limited rights”

Even if you think that the Local Authority could issue a licence to the Tenant, a Tenant could argue strongly that all the elements of a tenancy, lets remind ourselves, IDENTIFIABLE PARTIES AND PREMISES, PAYMENT OF RENT, PERIOD OF TENANCY AND EXCLUSIVE POSSESSION exist.

A matter for the courts once would suggest. My view is at absolute odds with the briefing paper in that not one, but ALL of the key elements of a tenancy clearly exist. This would strengthen Tenants rights and make eviction for rent arrears much more difficult (exposing your scheme to even higher financial risk).

Developing a Social Letting Agency

7. Engaging Landlords

It was quite a shock to me to read the section on why Landlords would be likely to work on such a scheme. Having developed Local Letting Agencies (LLAs) from scratch and undertaken a dozen LLA viability studies, what the briefing note states is completely at odds with what Landlords tell us every day when we are working with them. Here are some examples from the briefing paper as to why Landlords will work on this type of scheme;

“A free management service.....which could be charged for as confidence grows”

No comment on the services you'll need to provide to consider charging, how your teams skillset matches these new services, or indeed how you would



convince Landlords to pay after a free period. Again classic standard consultancy advice, without any practical solutions as to how you would do it locally

“Long term lets which minimize voids”

Aaah, so we are actually using these properties as long term lets then? Even more likely that a Tenant could legally challenge that they have a tenancy. But more importantly in this section, “long term lets” isn’t what you have been selling to the Landlord on this scheme. The briefing paper told you to use expressions such as “on a night by night basis” “not exclusive possession” and so on. So why would a Landlord have any belief that you are entering a long-term relationship?

“A scheme far more attractive than direct placements in the PRS which will be subject to LHA changes and cuts”

Umm? A scheme ‘far more attractive’, yet that only works on a subsidy in place to March 2013? Attractive for whom? Landlords regularly talk to us about how frustrated they get with Agents who change agreed guaranteed rents, withdraw services or simply go to the wall because they didn’t operate commercially.

The thing with a LLA that has a financial model based on the LHA rates and offers a well thought out and commercially attractive product, is that it is a business model and as such you can tinker with the figures and see how it affects your model and income. This is why I always make the point that there shouldn’t be a “one size fits all” LLA model. In some places a LLA model simply might not have the local market conditions to work or there may be issues that mean a different approach or model need to be looked at. Either way, an attractive scheme and/or sensible LLA business model needs to be far more strategic and well thought out than an opportunistic grab at some private sector properties.

8. Using the Subsidy to ‘make money’

The briefing paper makes up some figures to demonstrate how the subsidy could work. Even if those figures are conveniently attractive, that’s not my issue. There will be areas of the country where the figures do make this an attractive option for the Local Authority. My problem is with the final bullet point in the worked example that leaves a nice excess of “£65 per week to cover staffing and administrative costs”.

Firstly, it may well cover staffing and administrative costs, but shouldn’t we work out what they will be for the scheme before saying that £65 a week per property will cover it?

Secondly, and this is really worrying, but not unexpected if you haven’t been involved in setting up a LLA.....are they the only costs then???

I’ve already talked about allowing for rent arrears in your financial model (particularly if you are going to bear the whole risk), but what about



marketing of your new scheme, website set up, training for staff, out of hours cover (or will Landlords have to wait until 9am Monday if there is a problem?), a data management system (or are you going to use that good old excel spreadsheet to manage properties and deal with rent accounts etc.), what about your budget for legal costs (just in case you need to evict a non paying tenant!) or referencing and on and on it goes. Suddenly “£65 per week to cover staffing and administrative costs” doesn’t seem quite as comprehensive an assessment as it should be. I’m not saying its not enough (if you are making the figures up it should be enough!), what I am saying is that it shows an incredible lack of knowledge about the true costs of establishing and running a successful LLA or private sector scheme.

9. The really frightening figures

The briefing paper goes on to consider “what might be the cost of setting up a Social Lettings Agency?”. Some shockingly inadequate analysis takes place;

“There is the cost of creating the SLA in relation to overheads, staffing, premises etc. Set up costs of say £50,000 - £100,000 may be needed”

Where to start with this statement! The point of doing a business plan and financial model is to work out what these costs actually are. In reality they are likely to be far more than the figures randomly quoted above, in particular if you are considering premises (not that these are always needed). I’ll say it again. Without doing this exercise properly you can’t even guess-timate the likely set up costs, where savings could be made and where existing resources can be used.

“There may only need to be an initial ‘spend to save’ outlay as running costs after the first year would be derived from rents charged.....and management fees from Landlords. It may well be possible to obtain enough income by the end of year 1 to cover these costs”

In all the LLA set ups and viability studies we have done, (and we have done these both in large London Boroughs and smaller District Councils), we have yet to undertake a financial model where ‘running costs after year one are covered by income’. A ridiculous statement. As already stated, all LLAs are different, but like most business start ups, struggle to make a surplus that covers running costs until year 3. Speak to any LLA that is out there, (whether we have helped them or not) and they will tell you the same.

The briefing paper goes on to demonstrate how much income could be made;

“Accommodation held on licence – 100 properties with excess on rent of say £30 a week = £156,000.....Total possible income end of year 1 £150,000, rising to £250,000+ by the end of year 2”

What the author of the briefing paper seems to have forgotten is that for these ‘end of year 1’ figures to be accurate, you would have to create and have running 100 tenancies on day 1 of your LLA. Another basic mistake!



In reality if you are looking to create 100 tenancies in a year, then that is approximately 8 a month. A new business or scheme is likely to take some time to get up to that speed, so you can usually expect less than that as your average for the first six months. So on the basis that your 100 tenancies would be created evenly throughout the year, and that tenancy creation at the start would be less than your average thereafter, your income is more likely to be around £55,000 in year 1. A far cry from the £156,000 quoted.

Just to add, the briefing paper makes no financial allowance for tenancies which might end (either through failure or for other reasons). I'm assuming then in the briefing paper, all tenancies (sorry, licences) last forever, providing income forever??

Conclusions

The big concern for me is that there are Local Authorities out there who are struggling to procure properties at the level they need in order to be able to offer decent and sustainable private sector options to people. So, any briefing paper by a high profile consultant may be taken on faith as 'the answer'. This is an understandable reaction, but one which may lead you down a road fraught with problems.

Yes you need to procure more properties.

Yes you need to do it within existing resources.

Yes you need a sensible, well researched and developed scheme (or LLA) to help you achieve this.

And yes, you may need your Organisation to understand that even if you are highly successful, it could be 2 or 3 years before you start breaking even, and that there are risks involved.

The briefing paper outlines an opportunistic (which is not always a bad thing), unsustainable and under researched method of trying to achieve these goals.

We have designed LLA as previously stated. LLAs that are sustainable. LLAs that work on the local LHA rates and offer Landlords a commercially attractive option when they consider how and with who they might let their properties with. And whether you decide to use us to help you develop a LLA, or assess the viability of a LLA in your area, the things you must remember are;

- There is no 'quick and easy' solution to procuring more private sector properties in your area
- There is no 'one size fits all' LLA that can be taken off a shelf and made to work in your area
- You need to have a 'product' that is Landlord focused and therefore ideally, developed in consultation with Landlords. They are your initial customers and without them you can't provide decent options for Tenants.



- Do some financial modeling for your scheme, make sure you quantify known costs for years 1-3, (staffing etc..) and estimate sensible unknown costs (rent arrears losses etc.)
- Do some self-analysis. What parts of your current scheme need to adapt? Which need to be replaced? What do we need to add to our 'product'? What skills do we need?
- What risks are you prepared to take? Guaranteed rent? Is there a way to reduce your risk, such as working with another organization?

And finally, perhaps look at working with people and organisations who know about how to procure properties and create sustainable, cost effective schemes with you, one of which I've already mentioned above.

Best of luck!

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