Title: Tenant Fees Bill Impact Assessment **IA No:** **RPC Reference No:** **Lead department or agency:** Ministry of Housing, Communities and Local Government **Other departments or agencies:**	**Impact Assessment (IA)** **Date:** 1 May 2018 **Stage:** Final **Source of intervention:** Domestic **Type of measure:** Primary legislation **Contact for enquiries:** Becky Perks rebecca.perks@communities.gsi.gov.uk

Summary: Intervention and Options

RPC Opinion: GREEN

Cost of Preferred (or more likely) Option				
Total Net Present Value	**Business Net Present Value**	**Net cost to business per year** (EANDCB in 2014 prices)	**One-In, Three-Out**	**Business Impact Target Status**
-£34.50m	-£2615.57m	£340.3m	TBC	TBC

What is the problem under consideration? Why is government intervention necessary?

In 2016-17, there were 4.7 million households in the private rented sector. Letting fees, and high deposits, can represent a significant affordability problem for tenants. Letting fees are not always clearly or consistently explained and are often disproportionate to the value of services provided. Many tenants are unaware of the true costs of renting a property and lack the power to negotiate the level of fees since agents are appointed by landlords. This can restrict movement in the sector and hamper affordability. Intervention is needed to address these market failures. In addition, intervention is necessary to cap deposits to ensure that the financial burden at the outset of a tenancy is fair.

What are the policy objectives and the intended effects?

The policy objective is to ensure that tenants are only required to pay their rent and deposit when securing a property in the private rented sector. The intended effect is to deliver a fairer, more competitive, more affordable and more transparent market. Tenants will be able to see, at a glance, what a given property will cost them in the advertised rent - reducing the problem of asymmetric information when tenants may later discover hidden costs. The party that contracts the service – the landlord – will be responsible for paying for the service, which will help to ensure that the fees charged reflect the real economic value of the services provided and sharpen and increase letting agents' incentives to compete for landlords' business.

What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)

Different options to implement the ban on letting fees have been considered. These included promoting awareness of the existing transparency requirements under the Consumer Rights Act 2015 through to a range of primary legislation options. This resulted in our preferred option of introducing primary legislation to ban all letting fees paid by tenants in connection with a tenancy, with the exception of tenancy and holding deposits, utilities communication services and council tax, and fees arising because of a default or variation requested by the tenant.

Different options on the capping of tenancy deposits have been explored ranging from no cap (the status quo) to caps of 4 weeks' rent to 8 weeks' rent. This resulted in our preferred option of limiting tenancy deposits at 6 weeks' rent.

Will the policy be reviewed? It will not be reviewed. **If applicable, set review date:** N/A

Does implementation go beyond minimum EU requirements?	N/A			
Are any of these organisations in scope?	**Micro** Yes	**Small** Yes	**Medium** Yes	**Large** Yes
What is the CO_2 equivalent change in greenhouse gas emissions? (Million tonnes CO_2 equivalent)	**Traded:** N/A	**Non-traded:** N/A		

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible Minister: Heather Wheeler Date: 1 May 2018

Summary: Analysis & Evidence

Policy Option 1

Description: Ban tenant fees and cap deposits at 6 weeks' rent

FULL ECONOMIC ASSESSMENT

Price Base Year 2017	PV Base Year 2019	Time Period Years 10	Net Benefit (Present Value (PV)) (£m)		
			Low: -12.62	**High** -45.54	**Best Estimate: -**34.50

COSTS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	22.9		138.7	**1208.5**
High	54.1		517.9	**4438.9**
Best Estimate	44.7		303.4	**2619.9**

Description and scale of key monetised costs by 'main affected groups'

The main costs fall on landlords and letting agents as a result of the ban on tenant fees. We estimate in total, in the first year of the policy, the cost to landlords will be £82.9m whilst the cost to letting agents is estimated at £157.1m. This estimate includes pass throughs, for example, by letting agents charging landlords higher fees. We estimate familiarisation costs (as transition costs) in Year 1 totalling £44.7m to both landlords and letting agents. There is an additional cost to landlords from the reduction of deposits estimated at £1.3m which on average start in Year 4.

Other key non-monetised costs by 'main affected groups'

There is a potential negative effect on the closure of letting agents and employment losses, and on third party suppliers to letting agents such as inventory suppliers. However, if it is the most inefficient agents that leave the market, then in turn market efficiency would improve (p22).

BENEFITS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	-		139.9	**1195.9**
High	-		519.0	**4393.4**
Best Estimate	-		304.6	**2585.4**

Description and scale of key monetised benefits by 'main affected groups'

The main benefits fall to tenants who gain from the ban on letting fees, we estimate a benefit of £240.0m based on the ban on letting fees in the first year of the policy - essentially a transfer from landlords and letting agents to tenants, accounting for potential higher rents that will reduce the total benefit to tenants (p31). Tenants will pay an estimated £12.1m less in deposits in Year 1 of which there is an associated benefit of £1.4m. In addition, the £1.3m cost to landlords from Year 4 onwards represents a transfer benefit to tenants.

Other key non-monetised benefits by 'main affected groups'

There are significant non-monetised benefits. 1.4m households moving home in the PRS in Year 1 will benefit from being better able to appraise their choice of home and be more empowered to challenge poor practices. Landlords will benefit from potential lower incidences of rent arrears, and 16,000 letting agent branches may benefit from increased demand from tenants and innovation of business models. Wider society may benefit from a potential lower reduction in temporary accommodation costs and more money being spent in the economy (p20).

Key assumptions/sensitivities/risks | **Discount rate (%) : 3.5**

The headline EANDCB does not include any estimates of pass through. In other words, it is the total estimated annual loss of revenue from tenant fees to landlords and letting agents, and from the deposit cap to landlords, excluding any pass through by landlords and letting agents, for example, by charging tenants higher rent. It is therefore likely to be an overestimate of the cost to business. However, the overall NPV, BNPV, costs and benefits, do include these estimates of pass through.

BUSINESS ASSESSMENT (Option 1)

Direct impact on business (Equivalent Annual) £m:			Score for Business Impact Target (qualifying provisions only) £m:
Costs:	**Benefits:**	**Net:**	
340.3	0.0	-340.3	TBC

1. Policy background and overview[1][2]

The private rented sector (PRS) is an important part of our housing market. It houses 4.7 million households. The sector has more than doubled in size since 2002.[3] This impact assessment addresses the provisions of the Tenant Fees Bill, namely the banning of fees paid by tenants, and the capping of tenant deposits.

There are a number of problems with the status quo which the Tenant Fees Bill will address. These include:

- Information failures – tenants are not always fully aware of the letting fees they will be charged before considering a new tenancy in the private rented sector.
- Lack of competition – there is evidence of excessive charging by letting agents, such as double charging of both landlords and tenants, or charging more than the economic value of services provided.
- Affordability – the level of deposits requested can sometimes be excessive. Large deposits involve tenants paying substantial amounts of money upfront at the outset of a tenancy which can reduce affordability.

Letting agents are engaged by many private landlords to let and manage rental accommodation on their behalf. Good agents provide a valuable service in ensuring that properties are safe, compliant and professionally managed. They help landlords comply with their legal responsibilities and help tenants secure safe and good quality homes.

The duties of letting agents include finding tenants, collecting rent, and responding to queries from tenants, for example in relation to repairs. Letting agents charge fees to landlords for carrying out these duties on their behalf. Letting agents also charge fees to tenants for a variety of reasons, including seeking references, inventory services, and contract negotiations.

However, letting agent fees are not always clearly or consistently explained with the result that many tenants are unaware of the true costs of renting a property. This information failure means tenants are not fully able to appraise the costs and benefits of a potential property and distorts consumer choice. The competitive pressure on tenant fees is very weak as agents are chosen by landlords. Letting agents can therefore impose unfair or excessive fees because tenants have a very limited ability to negotiate or opt-out. This restricts movement in the private rented sector and reduces affordability.

The Government announced at the 2016 Autumn Statement that it would introduce a ban on letting agent fees paid by tenants in England to improve competition in the private rental market and give renters greater clarity and control over what they will pay. The commitment to make renting fairer for tenants was reaffirmed in the Housing White Paper, published February 2017, and the Conservative Party Manifesto.

On 7 April 2017, the Government launched an eight week consultation seeking views on the detail of how a ban should be introduced. The consultation closed on 2 June and 4,724

[1] Note that the central, low, and best estimates provided on the Summary: Analysis and Evidence page differ from those normally presented. The low estimate is based on estimating the low estimate of benefits from the low estimate of costs. In standard impact assessment practice, the low scenario would be based on taking the low estimate of benefits from the high estimate of costs – i.e. the worst case scenario that could occur. However, our low estimates of costs and benefits are dependent on each other, as they are based on the same assumptions of pass through. The low scenario therefore uses low costs and benefits, and the central scenario uses both central costs and benefits, and the high scenario uses high costs and benefits.

[2] The estimated high NPV is lower than the low NPV, primarily as the high NPV scenario is based on the highest potential costs to landlords and letting agents.

[3] English Housing Survey, 2016-17.

responses were received from a range of individuals and representative bodies. 50% of responses were from tenants, 32% were from letting agents, 10% were from landlords and 8% were from other interested stakeholders. More than 9 out of 10 tenants who responded to the Government consultation backed the action to ban letting fees.[4]

The Government published a draft Bill on 1 November 2017 to set out the detailed approach to banning fees paid by tenants, which had been informed by responses to the consultation.[5] The draft Bill was scrutinised by the Housing, Communities and Local Government Select Committee, who provided a number of recommendations.[6] The Department has considered these recommendations and other feedback gained during the pre-legislative process to refine the Tenant Fees Bill to ensure that it fully delivers its objective of delivering a fairer, more transparent and competitive private rented market with a high quality of service.

The Bill also bans landlords from charging tenants letting fees, and bans agents and landlords from requiring tenants to make payments to third parties except in permitted circumstances. We consulted on whether to ban landlords from charging fees to tenants. The majority of responses agreed that this was necessary. It mitigates the risk of tenants being charged agent fees through other routes, avoids creating a situation where landlords are encouraged to self-manage their properties purely on financial grounds and avoids the risk of some tenants being charged fees whilst others are not. Tenants will be able to see what a given property will cost them in the advertised rent level without any additional hidden costs.

In addition to letting fees, many tenants are required to pay a deposit at the outset of a tenancy. Landlords can collect a deposit to mitigate the risk of loss of income should a tenant default on their obligations under the tenancy agreement. Landlords are not required to ask for a deposit but many choose to do so, with 74% of households in the private rented sector having paid a deposit in 2014/15 according to the English Housing Survey.[7]

Legislation introduced in the Housing Act 2004 requires all landlords letting on Assured Shorthold Tenancies to protect their tenants' deposits in a government-approved scheme within 30 days of taking the deposit. The three government approved Tenancy Deposit Schemes in England help ensure that tenants are treated fairly at the end of their tenancy. A deposit can be protected in a custodial scheme, where the deposit is paid to, and held by, the scheme until the end of the tenancy, or in an insurance scheme where the landlord or agent holds the deposit. The three deposit protection schemes are – My Deposits, Deposit Protection Service (DPS), and the Tenancy Deposit Scheme (TDS). Combined, the three schemes currently protect over 3.7 million deposits. Of these, 2.2 million are in insured schemes, and 1.5 million in custodial schemes.

At the end of a tenancy landlords may seek to deduct money from the deposit to cover issues such as unpaid rent, damage to property, lost items, and cleaning costs. However, the deposit is the tenant's money and landlords must therefore provide appropriate evidence where they believe they are entitled to retain any of the deposit. The deposit protection schemes provide an alternative dispute resolution (ADR) service if the landlord and tenant are unable to agree how the deposit should be divided. In the vast majority of cases, landlords and tenants are able to agree how the deposit should be split at the end of a tenancy without arbitration.

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4 https://www.gov.uk/government/consultations/banning-letting-agent-fees-paid-by-tenants

5 https://www.gov.uk/government/publications/draft-tenants-fees-bill

6 https://publications.parliament.uk/pa/cm201719/cmselect/cmcomloc/583/583.pdf

7 English Housing Survey, Private Rented Sector Report, 2014-15
https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/570848/Private_Rented_Sector_Full_Report.pdf

The Government proposes to cap tenancy deposits at 6 weeks' rent. Currently, there is no cap on deposits with the result that tenants can be asked for significant amounts of money that are disproportionate to the landlord's risk. Government intervention to cap deposits is necessary to ensure that the financial burden at the outset of a tenancy is fair, whilst ensuring a reasonable level of security for landlords. 68% of respondents to the Government's consultation agreed that tenancy deposits should be capped.[8] We listened to concerns about capping deposits at 4 weeks' rent. A cap of 6 weeks' rent gives landlords greater flexibility to accept higher risk tenants, such as those with pets, as well addressing concern around tenants leaving without paying their final month's rent

The Bill enables agents and landlords to continue to charge a refundable holding deposit, capped at one week's rent, to a tenant to ensure that there is a financial commitment from a tenant to a given property and to mitigate the risk of landlords self-selecting tenants that they believe to be most likely to pass reference checks. The Bill requires agents and landlords to refund the holding deposit to tenants except in circumstances where the tenant withdraws or does not take all reasonable steps to enter into the tenancy agreement, fails a right to rent check or provides false or misleading information that materially affects their ability to rent the property.

2. Problem under consideration and rationale for intervention

At the outset of a tenancy, tenants are usually required to provide around a month's rent in advance, a deposit as well as letting fees. This can involve substantial amounts of money, and make entering and moving within the private rented sector financially prohibitive. For example, as a guideline of the scale of the money required upfront at the start of a tenancy, the Valuation Office Agency (VOA) report that median monthly rents during October 2016 to September 2017 were £675. In addition, renters pay an average of £200-£300[9] in letting agent fees per tenancy and a deposit of between 4 and 6 weeks' rent.[10] A typical and average tenant may therefore be asked for between £1500 to £1800 upfront at the start of a tenancy.

These fees may be more difficult for households in the private rented sector to manage because evidence suggests they spend more of their household income on housing than other household types. On average, households in the private rented sector spend 34% of their income (including Housing Benefit) on rent. Social renters spend, on average, 28%. Those buying their home with a mortgage spend on average 18% of their household income on mortgage payments[11]. In the private rented sector, more tenants need to borrow money to be able to afford the costs associated with securing a tenancy.[12] The leading cause of homelessness is now attributed to the ending of an Assured Shorthold Tenancy (AST).[13]

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[8] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/656211/Govt_response_to_consultation_on_banning_letting_fees.pdf

[9] Evidence from the consultation and data from the English Housing Survey 2014-15.

[10] English Housing Survey, Private Rented Sector Report, 2014-15
https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/570848/Private_Rented_Sector_Full_Report.pdf

[11] English Housing Survey: Private Rented Sector 2016-17
https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/675942/2016-17_EHS_Headline_Report.pdf

[12] Citizen's Advice Bureau

[13] MHCLG Homelessness Statistics, December 2017
https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/667302/Statutory_Homelessness_and_Prevention_and_Relief_Statistical_Release_Jul_to_Sep_2017.pdf

Tenant fees

Good agents provide a valuable service for their landlords and tenants. However, the fees that are charged to tenants can be significant, difficult to understand, and can be greater than the economic value of the service provided.

The English Housing Survey 2014-15 found that the mean average fee paid by a household in 2014-15 was £223, while the median was £200.[14] There is evidence that letting agent fees paid by tenants have increased significantly in recent years. The English Housing Survey reports that median fees charged by agents increased by 60% between 2009-10 and 2014-15 (14% increase in mean).[15]

The National Approved Letting Scheme found that the average fee charged is £172 with costs ranging from £30 to £500 (inclusive of VAT) and Generation Rent found that the average paid by two tenants is £400 with fees ranging from £40 to £780.[16] Shelter found that one in seven renters pay £500 or more in letting fees.[17] This highlights the large range of fees that tenants can be charged – in addition, they are often not aware of the level of fees at the outset of considering a tenancy.

Tenant responses to the Government's 2017 consultation on banning letting fees found that the average (mean) fee charged at the start of a tenancy is £327 per tenant. Responses from agents put the average (mean) fee at the start of a tenancy at £238 per tenant. In addition to this, some agents said they charge a renewal fee (mean average of £70), an inventory fee (mean average of £117) and a check out fee (mean average of £91).[18]

Given that the majority of tenancies are granted for six or twelve months initially, tenants can expect to pay letting fees regularly either to secure a new tenancy or renew an existing one.[19] These repeated and often significant charges, can have a real and detrimental impact on individual finances, particularly for those tenants who are more vulnerable. It decreases the ability of individuals to access and move around in the private rented sector and makes it harder for those tenants who are trying to save for a deposit to buy their own home.

In the Government's consultation on banning fees, 69% of tenants said that letting fees had affected their ability to move into a new property.[20] Citizens' Advice in their 2015 report 'Still Let Down' found that 64% of tenants experienced problems paying letting agents' fees, and 42% had to borrow money.[21] The English Housing Survey 2014-15 also found that about a third (34%) of private renters said that fees would stop them moving into a new home.[22]

As well as the financial impact on tenants, the wide range in letting agent fees charged, despite the services provided being broadly comparable, suggests that the market is not functioning in accordance with true market forces.

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14 https://www.gov.uk/government/statistics/english-housing-survey-2014-to-2015-private-rented-sector-report

15 https://www.gov.uk/government/statistics/english-housing-survey-2014-to-2015-private-rented-sector-report

16 2016 National Approved Letting Scheme online survey on letting agent fees. Generation Rent's findings are at http://lettingfees.co.uk/stats/

17 https://england.shelter.org.uk/__data/assets/pdf_file/0010/834832/6636_Scottish_letting_fees_report_v9.pdf

18 https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/656211/Govt_response_to_consultation_on_banning_letting_fees.pdf

19 English Housing Survey 2014-15 found that most private renters had an initial tenancy agreement of six or 12 months; 45% had an agreement of 12 months and 36% of six months.

20 1,558 tenants responded to the question 'Have letting agent fees ever affected your ability to move to a new rented property?' https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/656211/Govt_response_to_consultation_on_banning_letting_fees.pdf

21 https://www.citizensadvice.org.uk/about-us/policy/policy-research-topics/housing-policy-research/still-let-down/

22 English Housing Survey, Private Rented Sector Report, 2014-15 https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/570848/Private_Rented_Sector_Full_Report.pdf

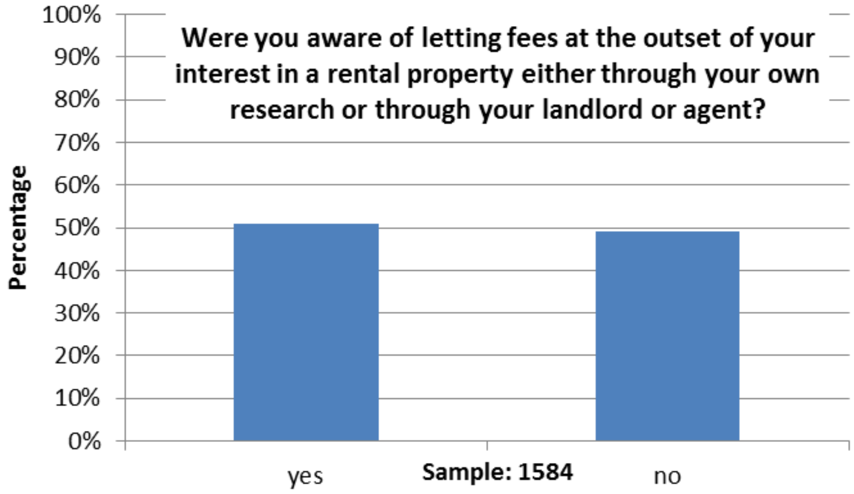
Further, even if all agents were fully compliant with the transparency requirements a tenant would still have little to no ability to negotiate or opt-out of letting fees since the decision to appoint a letting agent sits with the landlord.

Transparency requirements were implemented by the Government in the Consumer Rights Act 2015 to require letting agents to publicise a full tariff of their fees to tenants and landlords prominently in their offices and on their website. The aim of the requirements was to better enable tenants and landlords to compare letting agents and to shop around on the basis of their fees and services. However, as the evidence on the level of fees citied above demonstrates, there is significant variation in the way that agents charge for their services, and some agents still do not clearly displaying their fees. This makes it extremely difficult for both tenants and landlords to understand what services are being charged and to whom, resulting in the competitive process being undermined.

The Government's consultation asked tenants and landlords whether they considered letting agent fees to be clearly and transparently displayed. 15% of tenants thought that they were transparent compared with 69% of landlords.[23] The disparity between landlords' and tenants' views on the transparency of their respective fees suggests that the fees charged to landlords are clearer and easier to understand. This supports the argument that agents seek to primarily market their services to landlords.

The consultation found that only 50% of tenants were aware of fees at the outset of interest in a rental property.

Figure 1: Proportion of tenants aware of letting fees at outset of interest in letting



Source: Banning letting fees paid by tenants consultation, MHCLG

Where prices are transparent and upfront consumers are able to make rational decisions to reward companies that provide superior products for the same price or equivalent products more cheaply. The lack of transparency with regards to letting fees distorts the market. When a tenant settles on a property, they often do not have full information on the level of fees they will pay to secure the tenancy. Consequently, they are not able to fully appraise the costs and benefits of prospective properties to live in.

The Office of Fair Trading, in their 2013 market study, found that tenants focus on the headline advertised price (i.e. the rent), and don't focus on the 'drip' prices that come later in

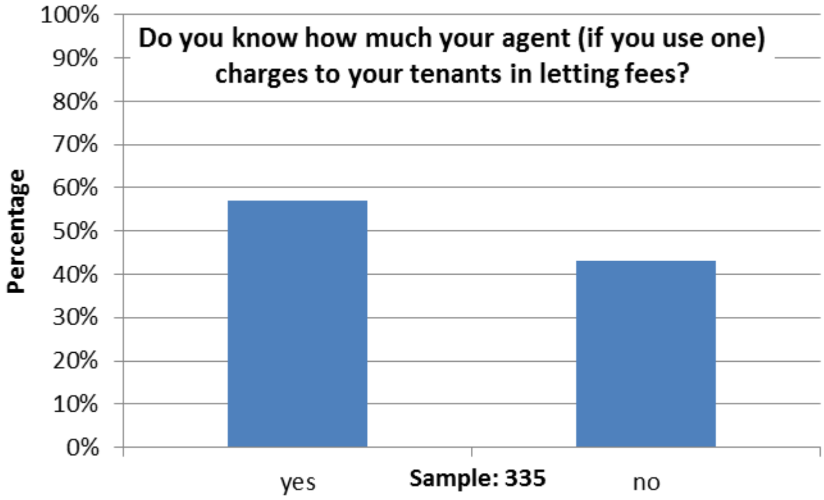
[23] 1,606 tenants responded to the question 'Do you consider that letting agent fees are clearly and transparently displayed?' and 366 landlords responded to the question 'Do you consider that letting agent fees charged to landlords are clearly and transparently displayed?' https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/656211/Govt_response_to_consultation_on_banning_letting_fees.pdf

the process in the form of letting agent fees.[24] Similarly, empirical studies and theoretical models indicate that mandatory hidden fees cause, even trick, people into buying things they would not otherwise.

Further, in highly competitive property markets, such as London and other metropolitan areas, renters have to prioritise the location of the property and the affordability of the rent. Competition for acceptable accommodation is such that renters cannot take time to shop around in the hope of finding a similar property with lower letting agents' fees or let directly by a landlord. Tenants may also be under time pressure to find a new property, if their current tenancy is coming to an end and they are seeking a new property to rent. In reality, once a tenant has chosen a property, they accept the fees that are charged and have to deal with any 'hidden' fees at a later stage.

There is often confusion in the sector between landlords and tenants around who is paying for which letting agent service. 43% of landlords who responded to the Government's consultation on banning letting fees said they do not know the fees that their agent charges to tenants.[25]

Figure 2: Proportion of landlords aware of how much their agent charges tenants



Source: Banning letting fees paid by tenants consultation, MHCLG

Similarly, although landlords are motivated to find the agents with the lowest landlord fees, they have little or no incentive to find agents with low fees for tenants. Indeed, agents can, and do, keep their landlord fees down by charging increased fees to tenants. Landlords can also off-set fees charged by letting agents against tax liabilities whereas tenants do not have the option to do so.

Letting agents are able to use their informational advantage to extract more revenue. Some agents do exploit their role as an intermediary between the tenant and landlord by imposing unfair, excessive or duplicative charges. For example, a reference check can be purchased on the market for £30.[26] However, in response to the Government consultation, tenants said that they were charged on average (mean) £137 and agents said that they charged on average (mean) £97. There is significant variation in the levels charged. Some tenants explained that they had been charged referencing fees ranging from £15 to £625.

[24] http://webarchive.nationalarchives.gov.uk/20140402234354/http://www.oft.gov.uk/shared_oft/markets-work/lettings/oft1479.pdf

[25] Of 335 landlords who responded to the question 'Do you know the how much your agent (if you use one) charges to your tenants in letting fees?' https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/656211/Govt_response_to_consultation_on_banning_letting_fees.pdf

[26] http://www.experian.co.uk/background-checking/private-landlords.html and https://www.nlatenantcheck.org.uk/services.aspx both advertise full tenant reference checks for £30 or less.

In addition to these tenant fees, agents also charge fees to landlords. This indicates, as well as the variation in fees charged to tenants, some agents are benefitting from supernormal profits. Letting agent fees to landlords tend to be based on a percentage of the rent and are often cited as covering referencing, inventories and contract negotiation – the main types of charges levied to tenants. Typical rates of commission charged to landlords are 7-10% for a 'let only' or introductory service and 13-15% for management services. Additionally, it is increasingly common for landlords to be charged further fees for referencing, inventories, negotiation of the tenancy agreement, deposit protection, check-in and check-out and arrangement of works (usually a percentage of the works value).

As with tenant fees, letting agent fees paid by landlords vary from agent to agent. The National Landlords Association Quarter 4 survey, December 2016, asked 360 landlords if they were charged any additional fees by their letting or managing agent, in addition to the commission charged. The results are below:

Table 1: Level of fees charged, and percentage of respondents being charged fees

Type of fee charged	**Percentage of respondents charged fees**	**Average amount charged**
Inventory	33%	£103
Tenancy agreements	29%	£202
Check-in	17%	£142
Referencing	16%	£97
Credit checks	13%	£81
Check out	9%	£87
Protection insurance	8%	£131
Guarantor agreements	5%	£48
Other	13%	£350

In a well-functioning competitive market, supernormal profits either from over charging or double charging would not be earned by a typical firm. They therefore represent a failing in the market and transferring the money to tenants could mean the money is spent more efficiently in the wider economy.

With regards to fees charged by self-managing landlords (i.e. those that do not use an agent), 30% of landlords that responded to the Government's consultation stated that they charge no fees to tenants. Of the remaining respondents that do charge, the average fee at the start of a tenancy is £107. However, as part of their response to the consultation, the Deposit Protection Service (DPS) conducted their own survey and received more than 1,900 responses from landlords. The DPS survey found that 78% of landlords said that they either don't charge any fees or simply just pass on the costs of the referencing/credit checks. The Residential Landlords Association (RLA) stated that most of its members either charge no fees to tenants or charge in the region of £25 per person.

The fact that landlords charge significantly less than agents for similar services again indicates that agents are charging more than the economic value of the services provided. This is particularly apparent with renewal fees where some agents charge a fee at the end of the initial fixed term even if no further fixed term is agreed but the tenancy becomes a rolling statutory periodic one, which simply inherits the terms and conditions of the pre-existing tenancy and requires no additional referencing, contract negotiation or inventory services.

High tenant fees are a problem across England. The table below presents our analysis of regional tenancy fees from English Housing Survey 2014-15 data.[27]

Table 2: Median fees by region, 2014-15

	tenancy fee amount, 2014-15 £		fee as a proportion of weekly household income (including income from all adults) %	
	mean	median	mean	median
North East	-	-	-	-
North West	192	150	66	34
Yorkshire and the Humber	152	145	39	28
East Midlands	176	150	38	29
West Midlands	200	197	46	24
East	227	178	39	33
London	260	243	48	32
South East	284	200	55	35
South West	209	175	52	32
all households	223	200	49	31

Whilst median fees (£) are highest in London, when comparing fees as a proportion of weekly household income, it is apparent that tenancy fees can be high across England. For example, households in Yorkshire and the Humber pay a median of 28% of their weekly household income compared to 32% in London households. The median fee as a proportion of weekly household income is 31% across England. Once comparing fees to household income, there is little evidence that one particular region is disproportionally affected by tenant fees.

In summary, there is a competitive failure in the lettings market, which has four main elements. Firstly, tenants do not know in advance what they are going to be required to pay, secondly tenants do not have power in the market to negotiate or opt out of the fees charged, thirdly the agent charging fees to both landlords and tenants increases the risk of unfair practices in the form of double charging, and finally many of the fees charged are substantially greater than the value of services provided.

Government intervention is necessary to address the asymmetry of information between letting agents and tenants, to reflect that the primary customer of an agent is the landlord, to prevent agents from exploiting their position as an intermediary between the tenant and landlord and to ensure that the fees charged reflect the true economic value of the services provided. This will increase competition, transparency and affordability in the lettings sector to the benefit of all consumers.

Deposit cap

Landlords can collect a deposit at the outset of a tenancy to mitigate the risk of loss of income should a tenant default on their obligations under the tenancy agreement. Landlords are not required to ask for a deposit but many choose to do so, with 74% of households in the private rented sector having paid a deposit in 2014/15 according to the English Housing

[27] The North East figure has been omitted due to a low sample size.

Survey.[28] Analysing deposit protection data suggests the average deposit requested is just under 5 weeks' rent.

Table 3: Average deposits according to Tenancy Deposit Protection Schemes

	March 2012	March 2013	March 2014	March 2015	March 2016	March 2017
Average Deposit	£979	£992	£1,006	£1,039.56	£1,118	£1,161

The average deposits across all 3 tenancy deposit protection schemes was £1,161 in March 2017 – an increase of 18.6% over five years. However, in many cases the amount of deposit taken is much greater.

Description of deposit data

To consider the potential costs and benefits to landlords and tenants from a cap on deposits, we have analysed a sample of data held by one the deposit protection schemes. This contains observations on 549,000 deposits that were repaid in the 12 months to November 2017. We are able to observe the deposit amounts, the amount returned to the landlord, the amount returned to the tenant, and the monthly rent of the tenancy. It represents a valuable data source which can be used for considering the implications of a deposit cap. It may not be representative of the overall tenant and landlord population as it is based on a selection of data from one particular scheme, and refers to custodial deposits only. Therefore the estimates should be treated with some degree of uncertainty as they may not reflect the whole population of private rented sector deposits.[29]

Table 4: Summary statistics of average deposits, custodial data only[30]

	Average deposit (number of weeks' rent)	**% of deposit returned (sum of all deposits returned divided by sum of deposits taken)**
East Midlands	4.53	77%
East of England	5.12	76%
London	5.11	79%
North East	4.44	74%
North West	4.47	74%
South East	5.42	77%
South West	4.86	80%
West Midlands	4.94	77%
Yorkshire and The Humber	4.44	76%
England	**4.88**	**77%**

This data suggests the average deposit in the South East is 5.42 weeks, compared to 4.44 weeks in the North East. At the same time, on average, across all deposits, 74% of deposits

[28] English Housing Survey 2014-15

[29] The data does not contain information on the length of the tenancy and when the tenancy started, therefore it may be a mix of various prices (for example, the tenancy may have started a year ago or around four years ago). However, it represents the most robust data source available for the purposes of this analysis.

[30] MHCLG analysis of custodial data. Not all deposits could be matched to a particular region which may influence these results.

are returned in the North East compared to 77% in the South East. This suggests that landlords are taking higher deposits because they are able to do so rather than to mitigate real financial risk. There is much less variance in the percentage of deposits returned that the level of deposits requested (compared to monthly rents).

Large deposits can have a significant impact on affordability for tenants. A deposit of 8 weeks' rent, for example, in London or the South East, represents a large upfront cost required to secure a tenancy when this money could be more efficiently used in the wider economy. For example, the median rent in London according to VOA data was £1,433 between October 2016 and September 2017.[31] In addition to a month's rent, a deposit of 8 weeks' rent equates to approximately £2,660,[32] before factoring in the impact of tenancy fees. Whilst the financial burden in monetary terms is lower in regions such as the North East, so are median incomes. It is a problem across England.

Data suggests that the amount of deposit taken is not linked to the riskiness of the tenant. Whilst we are limited given available data to fully explore deposit length and risk characteristics of tenants, we have analysed the deposit protection data to explore correlations between the length of deposit, and the amount retained by the landlord. Our analysis of the data mostly suggests that landlords appear to 'bunch' around certain intervals, for example, 4 weeks' or one month's rent, and 6 weeks' rent, rather than a considered approach to evaluate risk and in turn the level to set the deposit.

Further analysis of data from the deposit protection services shows that on average across all regions tenants receive back 77% of their deposit value. This helps to show that deposits have become larger than is necessary to provide sufficient security for landlords. The average length of time private tenants have lived in their current home is 3.9 years.[33] During this time, the tenant's money is held in a deposit protection scheme and cannot be used in other areas of the economy.

As with letting fees, tenants are often forced to accept the terms of the deposit as set out by the landlord otherwise they will risk losing the property. Tenants can therefore be required to pay unreasonable deposits that are incommensurate with the landlord's risk. Tenants have little bargaining power to influence this level of deposit, which is further indication that the lettings market is not functioning in accordance with true market forces.

Tenants, due to having less economic power, have less flexibility to leave poor quality accommodation, which in turn reduces the pressure on landlords to make improvements. Moreover, affordability barriers lead to increased incidences of homelessness – which imposes significant social costs in the form of disrupted lives and the demand on health and other public services, and places a burden on local authorities in terms of temporary accommodation costs.

Government intervention in the form of a cap on tenancy deposits at 6 weeks' rent is necessary to ensure that the level of deposit required by landlords is financially manageable for tenants and commensurate with the landlord's financial risk. This will result in the money being available to tenants to spend, leading to wider economic benefits.

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[31] https://www.gov.uk/government/statistics/private-rental-market-summary-statistics-october-2016-to-september-2017

[32] For example, median weekly rents would be approximately £333 (£1,433/4.3). Multiplying this by 8 weeks suggests a deposit of approximately £2,600, plus a months rent (£1,433), plus tenancy fees.

[33] English Housing Survey, 2016-17

3. Policy objectives and the intended effects

The policy objective and intended effect of the Tenant Fees Bill is to deliver a fairer, more competitive, and more transparent lettings market where tenants have greater clarity and control over what they will pay and where the landlord is the primary customer of the letting agent, and to improve fairness and affordability at the outset by capping tenant deposits at 6 weeks' rent.

The pre-requisite for effective and competitive markets is for consumers to have the ability to shop around for a supplier that provides the quality of service they are seeking at a price they are willing to pay. Under the ban on tenant fees, landlords will cover the costs of contracting an agent and any on-going management that they choose to procure. This will sharpen and increase letting agents' incentives to compete for landlords' business resulting in a more transparent market with lower overall fee levels and a higher quality of service. A ban will also reduce the risk of unfair practices in the form of over or double charging.

We do not expect the full level of tenant fees that are charged currently by letting agents to be passed on to landlords since there is evidence that a number of agents are charging excessive fees and that some agents are double charging landlords and tenants.

Good and innovative letting agents that provide services that represent value for money to landlords will continue to play an important role in the market and will be on a fairer footing to compete for landlords' business since the opportunity for rogue agents to exploit their position as intermediary between landlords and tenants will be greatly reduced. For example, it will no longer be possible for agents to compensate an artificially low rate to landlords by increasing their fees to tenants.

A ban is likely to have a negative impact on agents that are unable to adapt to a market where letting fees to tenants are banned. Such agents may currently rely on overcharging or double charging in order to maintain their profits. Or they may simply be unable to offer the quality of service needed to secure the business of landlords. However, any impact on business in terms of lost profits will equate to a direct saving to tenants and lost profits are likely to represent fees that were not a fair reflection of the service provided in the first place.

With regards to tenants, the policy objective is to improve affordability at the outset of a tenancy and for tenants to see – at a glance – what a given property will cost them in the advertised rent level with no hidden costs. A ban will strengthen the position of the tenant in the lettings market since they will be able to compare properties and negotiate with a landlord/agent on the basis of the rental price of a property alone. The greater transparency under a ban will ensure that tenants are only committing to a property that they know that they can afford.

This, in turn, may reduce incidences of tenants defaulting on rent as well as facilitating better movement into and around the private rented sector. Tenants will have greater power and flexibility to leave poor quality accommodation, which may help to drive up property standards. Moreover, more optimal housing choices and fewer affordability barriers may lead to reduced incidences of homelessness.

The cap on deposits will help to ensure that the amount of deposit requested is more aligned to the landlord's financial risk and help to further assure affordability for tenants at the outset of a tenancy. Capping deposits will also help to deliver wider economic benefits as less money will be held in protection schemes and instead be available to be spent in other areas of the economy.

The Bill enables agents and landlords to charge a holding deposit to a tenant to ensure that there is a financial commitment from a tenant to a given property. The holding deposit provisions will mitigate the risk of tenants speculating on a number of properties, which could result in unnecessary and costly work by agents and landlords. The holding deposit will also help to mitigate the risk of landlords cherry picking those tenants that they perceive to be most likely to pass a reference check. Similarly, enabling a landlord to charge fees related to a variation requested by the tenant or default by the tenant (such as a late payment or lost key) means that landlords will not be unfairly penalised by costs incurred owing to an action by the tenant.

Landlords and agents are prohibited from requiring a tenant to pay for a third party service (except for utilities, communication services and council tax) but the Bill does not prevent tenants from procuring their own services, for example paying for their own reference check or inventory. Some tenants may indeed choose to do so to demonstrate they are financially and legally able to meet the terms of their tenancy and give themselves a competitive edge in the market. There is thus no reason why third parties that offer a valuable service to agents, landlords and tenants would not be able to continue to market and sell these services.

In summary, the intended effect of the Bill is to ensure that the party that contracts the service pays for the service, which is a key characteristic of an effective and fair market.

4. Description of options considered

Ban on tenant fees

Six different options to implement a ban on letting fees paid by tenants have been considered:

1. Do nothing.
2. Promote awareness of the existing transparency requirements under the Consumer Rights Act 2015 and use guidance to encourage agents not to charge tenants fees.
3. Introduce legislation to cap the level of letting fees charged to tenants.
4. Introduce primary legislation to ban letting agents from charging fees to tenants in connection with a tenancy but continue to allow third parties and landlords to charge fees to tenants.
5. Introduce primary legislation to ban all letting fees paid by tenants (i.e. those charged by agents, landlords and third parties) with no exemptions.
6. Introduce primary legislation to ban all letting fees paid by tenants in connection with a tenancy with certain exemptions (Preferred Option)..

Option 1 would not achieve the stated policy objective. Option 1 would result in tenants continuing to pay fees, with the same problems stemming from informational barriers that they do not always know what the level of fees will be upfront. This will continue to distort consumer choice and the letting agents market will remain less competitive.

Regarding option 2, even if awareness were increased substantially tenants would retain their weak competitive position in the lettings market due to the fact that it is the landlord who appoints the agent. Landlords and letting agents would retain an incentive to charge fees and tenants would remain powerless to prevent this. This would likely mean that supernormal profits would continue and guidance alone would be insufficient to tackle this. Regulation is therefore necessary in order to improve competition and give renters greater clarity and control over what they will pay.

Option 3 would also not achieve the stated policy objective. Although a cap would prevent agents from overcharging tenants for the value of services provided, tenants would continue to have very limited ability to negotiate the level of fees charged. A ban ensures that the party that contracts the service pays for the service, which is an indicator of a fair market. A ban is also easier for tenants to understand and enforce.

Option 4 would mean that landlords were still able to charge letting fees to tenants and that agents could require tenants to pay a third party company fees as a condition of a tenancy. This is likely to lead to tenants paying agent fees through other routes, for example an agent could, as a condition of rental, ask that a tenant completes a reference check with a third party partner for a fee. The policy objective is that tenants are not required to pay any letting fees in order to improve transparency and affordability in the sector (although we do not want to prevent tenants from procuring their own services from third party services). Option 4 would therefore not meet the stated policy objective. It may also lead to some landlords choosing to self-manage their properties in order to profit from charging fees to tenants as well as an unfair situation where some tenants (those letting directly from landlords) could be charged fees but others (those letting through an agent) could not.

Option 5 would mean that tenants would not need to provide money to secure the property and therefore there would be no financial commitment from a tenant to a given property. This could lead to tenants speculating on a number of properties, which could result in potentially unnecessary and costly work by agents and landlords. Similarly, requiring the tenant to pay for any default charges that are a direct result of their action means that the landlord or agent is not unfairly penalised by costs that are outside of their control. The Government does not wish to unreasonably increase the risk or financial exposure of individual landlords or agents.

Our preferred legislative option is option 6 since this will achieve the stated policy objectives whilst minimising the costs to business. Tenants will have greater clarity and control over what they will pay, helping to improve transparency and affordability. Under this model, the party that contracts the service will be responsible for the costs for that service. Landlords will cover the costs of contracting an agent and any on-going management that they choose to procure but tenants will remain responsible for any fees that they choose to procure or that arise as a result of a default. This should result in a more transparent market with lower overall fee levels and a higher quality of service. Tenants will benefit from the ban on fees by approximately £240m in the first year of the policy compared to the counterfactual.

Deposit Cap

We have considered options on capping deposits. A trade-off exists - should the deposit cap be set too low then landlords may not be covered adequately for risk to their property, and in turn may be less willing to let their properties to riskier tenants, and a small number of landlords may exit the market altogether. Landlords may also seek to increase rents to compensate for lower deposits. Should the cap be set too high then no change will be enacted, and no improvement in affordability for tenants will result.

Five different options on what level to cap tenant deposits have been considered. These are:

1. No cap on deposits.
2. A cap of 8 weeks' or 2 months' rent.
3. A cap of 6 weeks' rent.

4. A cap of 5 weeks' rent.
5. A cap of 4 weeks'/one month's rent.

Option 1 would not achieve the policy objectives and would fail to protect tenants from unreasonably high deposits. In the Government consultation, we asked whether refundable deposits, payable at the outset of a tenancy, should be capped; 91% of tenants and 68% of all responses said 'yes' to a cap.[34]

We have considered the impact of different levels of cap to consider options 2 to 5. In the Government's consultation, of the 1,474 responses that were received, 45% of respondents said 4 weeks' rent, 25% said 6 week's rent and 17% said 8 weeks' rent. Tenants in particular supported a cap of 4 weeks' rent or less with the majority of landlords opting for a cap of 8 weeks' rent. Full results are in Table 5 below:

Table 5: Preferred level of deposit cap, survey monkey responses to Government consultation on banning letting fees paid by tenants

	2 weeks' rent or less	**One month's rent**	**Six weeks' rent**	**Two months' rent**	**£250 or less**	**£251-£500**	**Over £500**
Tenants (870 responses)	6%	58%	19%	9%	2%	3%	3%
Landlords (135 responses)	4%	21%	32%	39%	2%	1%	1%
Agents (332 responses)	2%	19%	41%	27%	4%	5%	2%
Other (137 responses)	9%	48%	16%	18%	2%	4%	3%
TOTAL (1474 responses)	5%	45%	25%	17%	3%	3%	2%

Table 5 shows that a cap at one months rent was most popular with tenants, compared to two months rent for landlords, and 6 weeks rent with letting agents. A deposit cap tied to the level of rent is preferable to a fixed amount since it will better allow for regional market variations and ensure that the legislation is less likely to require amendment in the future. We have considered the average level of deposits taken.

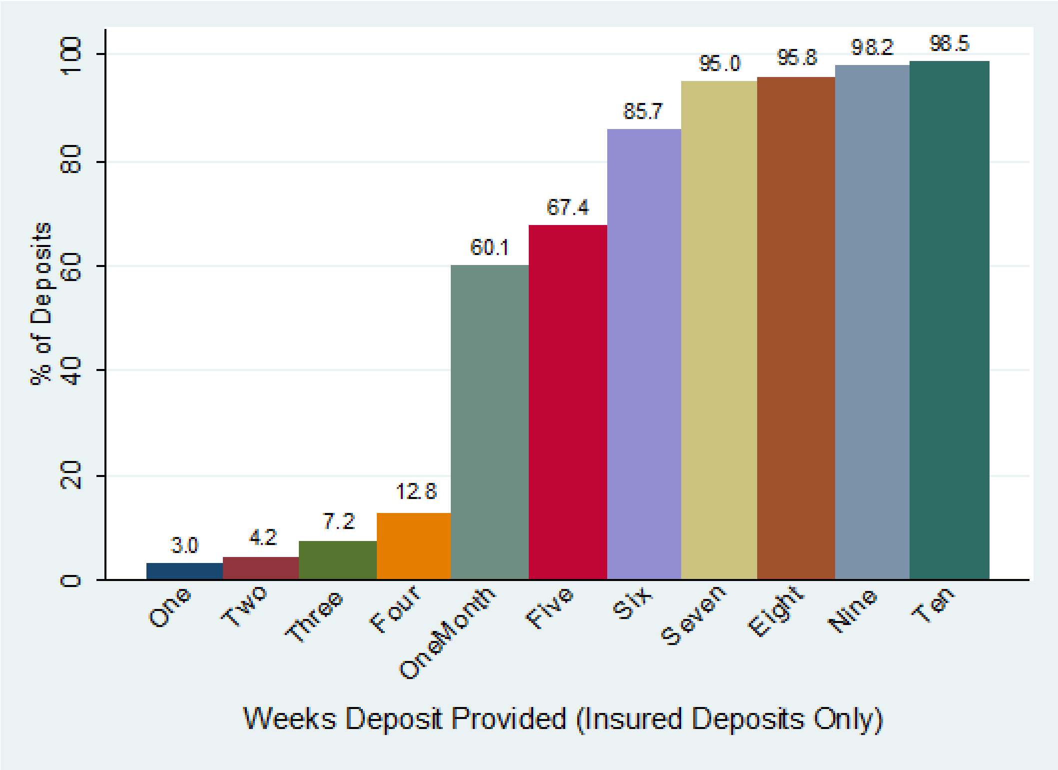
The English Housing Survey (2014/15) reported that 61.8% of households that paid a deposit on their previous tenancy paid four weeks rent/one month or less. The remainder paid more than four weeks rent/one month.

Landlords and letting agents have a choice to protect the deposit in either an insured scheme, where the landlord or letting agents holds the deposit in their own bank account,

[34] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/656211/Govt_response_to_consultation_on_banning_letting_fees.pdf

but if there is a dispute at the end of the tenancy this disputed amount must be transferred into the protection scheme, as opposed to custodial deposits where the deposit is transferred into the deposit protection scheme for the duration of the tenancy. We have also analysed a sample of data held by the deposit protection schemes to further disaggregate the levels of deposit requested. Graph 1 presents analysis of a sample of data from an insured deposit scheme.

Graph 1: Proportion of deposits by number of weeks rent



Graph 1 indicates that for example, 3% of deposits are for 1 week's rent or less, and 4.2% are for 2 weeks' rent or less. This data indicates that although option 2 (capping deposits at 8 weeks' rent) would protect tenants from unreasonably high deposits, it would not significantly help to improve affordability for tenants given approximately 4.2% of deposits are for greater than 8 weeks' rent.

Options 3 to 5 would achieve the stated policy aim of protecting tenants and reducing the financial burden they face at the outset of the tenancy. A cap of 4 and 5 weeks' rent would provide greater protection for tenants than a cap of 6 weeks' rent. For a cap at 4 weeks' rent, a majority of landlords would be required to take a smaller deposit. A cap at 5 weeks' rent would affect approximately 33% of deposits, opposed to approximately 14% of deposits for a cap at 6 weeks rent. A cap of 4 weeks' rent or one month would result in around 40% of deposits being reduced.

We recognise that landlords need some protection for their asset, and that a cap of 4 weeks' or one month's rent may not provide adequate insurance. It could have a detrimental impact on the rental market if landlords begin to exit as a result. Landlords and agents raised concerns that a cap of 4 weeks' rent may result in a behavioural change, encouraging tenants to forgo their final month's rent payment and leave landlords with less flexibility to accept riskier tenants such as those with pets. Whilst it is difficult to assess these impacts, we have rejected Option 5 (a 4 cap of 4 weeks' or one month's rent) on this basis.

Options 3 and 4 may provide a balance between improving affordability for tenants whilst protecting landlords. We have also analysed a sample of data on custodial deposits which contains 549,000 usable observations. From our sample we are able to estimate the share of the deposit returned to the tenant at the end of the tenancy, which we can use to estimate the potential impacts of different levels of deposit cap. These may not be representative of the overall tenant and landlord population as it is based on a selection of data from one particular scheme, therefore the estimates should be treated with some degree of uncertainty as they may not reflect the whole population of private rented sector deposits. The data also contains a higher proportion of longer deposits, compared to analysis of insured data and findings from the English Housing Survey. They are also based on assumptions of the number of new PRS tenancies. They should therefore be treated as indicative estimates only. In the monetisation of costs and benefits, we vary these estimates to account for this uncertainty.

The table below presents estimates using this custodial data.

Table 6: Estimates of the impact of capping deposits at 5 and 6 weeks' rent[35]

	6 week cap	**5 week cap**
Landlords		
A. Estimated % of deposits that will result in reduced end of tenancy claims (adjusted for bias)[36]	1.4%	3.9%
B. Estimated median loss from deposits in Row A	£89	£181
C. Estimated annual loss to landlords in row A from deposit cap, starting on average in year four of the policy (central estimate)[37]	£1.3m	£7.2m
Tenants		
D. Estimated % of deposits that will be reduced	14%	33%
E. Estimated reduction in deposits paid in year one of the policy (saving to tenants)[38]	£12.1m	£64.3m

Our best estimate is that a cap of 6 weeks' rent would result in 1.4% of deposits resulting in a landlord losing money, as a result of the new deposit level not covering the landlord claim at the end of a tenancy. At a cap of 5 weeks' rent, our best estimate is that 3.9% of deposits would result in this scenario. These indicate the estimates of the deposits which are withheld by the landlord at the end of the tenancy, and where the amount withheld is greater than the proposed deposit cap. The true figure of the percentage of deposits affected from the custodial data is slightly higher than these estimates, however, we have adjusted for the

[35] MHCLG analysis of a custodial deposit data and forecasted data on the number of PRS moves.

[36] The true figure we have estimated from the custodial data is 1.8% at 6 weeks and 4.9% at 5 weeks. However, the custodial data is biased with larger than average deposits compared to findings from EHS and a sample of the insured deposits. For example in the custodial dataset, 18.1% deposits are for greater than 6 weeks, compared to 14.3% in the insured dataset. Therefore we adjust the 1.8% estimate by 1.8% * (14.3%/18.1%) = 1.4%, to adjust for some of this bias. In the monetisation of costs and benefits, we vary these estimates to account for this uncertainty around the true figure. In the upper scenario this cost to landlords from a 6 week cap is estimated at £1.6m and £900k in the lower scenario.

[37] [37] Figures varied in the monetisation of costs and benefits as there is uncertainty around the actual growth rate in the PRS and therefore the number of tenancies that will affected.

fact that the custodial data appears to have a higher proportion of longer deposits than the overall deposit population (see footnote below).

Our best estimate is that a cap at 6 weeks' rent would result in a median loss from 1.4% of deposits of £89 per deposit, and a cap of 5 weeks' rent would result in a median loss from 3.9% of deposits of £181. These are average estimates based on the observed median, which therefore approximate the best estimate of losses that will occur to landlords that we are able to estimate with available data. For example, at a cap of 6 weeks' rent, the median loss of £89 means half of the estimated losses are below £89 and half above. According to our analysis of the deposit data this £89 approximately equates to a median of approximately 45% of weekly rent.

Only 1.4% of deposits will result in a loss to the landlord, according to our analysis. However, we have also considered whether there is a small tail of landlords that will lose much more than this median of £89. Our analysis indicates that this is unlikely to happen and would not affect a significant number of landlords. Even considering a higher percentile, 75% (i.e. deposits that result in a loss being greater than 75% of the other estimated losses in the sample), the loss from the deposit cap at 6 weeks would be on average 72% of weekly rent which would affect only 0.3% of all deposits.

Only at the 90% percentile would the loss to landlords begin to have a significant impact. At the 90% percentile (i.e. deposits that result in a loss being greater than 90% of all other losses in the sample), the loss on average would be 260% of weekly rent (i.e. 2.6 times weekly rent) which would only affect 0.14% of deposits, before even considering that not all landlords take a deposit.[39]

Therefore the loss to landlords from the deposit cap at 6 weeks' rent is expected to be small even considering those who lose more than the median of £89 according to our analysis of the deposit data. As this analysis indicates that the estimated median loss of £89 covers most of the loss that landlords will face, it is later used in the monetisation of costs and benefits. Our best estimate is that 98.6% of deposits will result in no loss – i.e. the vast majority of landlords will not be affected by the deposit cap compared to the counterfactual, as the deposit is already more than covering the damages they claim at the end of the tenancy.[40]

We estimate that this will result in a loss to landlords starting predominantly in year 4 of the policy, as whilst initial tenancy agreements tend to be 12 months, on average, tenants live in their current PRS property for 3.9 years. In reality, some tenant households end tenancies before 3.9 years and some afterwards. Hence starting the costs in year 4 represents an average of what will actually happen in the PRS.

Tenants initially gain more from a cap at 5 or 6 weeks' rent. Our best estimate is that in 2019, a cap at 6 weeks' rent would result in approximately £12.1m less being spent on deposits compared to £64.3m for a cap at 5 weeks' rent. For the vast majority of tenants

[39] This calculation is from a very low sample size and should be treated with further caution appropriately.

[40] Note that all these calculations rely on using observations on the deposit amount, and the rent is associated with that deposit. Whilst the deposit values are validated, the observations on rents are collected only for statistical reasons and may be subject to a small number of errors. Furthermore, we are not able to observe the reasons for the landlord claiming the deposit. In some cases, for example, it could be voluntary agreement between the landlord and the tenant that the tenant does not pay the final one or two months rent, in lieu of the deposit. Therefore, our best estimate of 1.4% of deposits resulting in a loss to the landlord may be an overestimate.

that pay a deposit, this releases money that would otherwise be held dormant in a deposit protection scheme.

We recognise that landlords need to use a deposit, to protect their asset and a cap at 5 or 6 weeks' rent would allow landlords greater flexibility with setting this amount and thus improved financial security. A sample of data from the deposit protection services shows that on average, across all deposits, tenants receive back 77%, indicating that deposits at present on the whole do provide sufficient security for landlords.

The Housing, Communities and Local Government Select Committee's scrutinised the draft legislations and noted:

'Security deposits should be capped at the equivalent of five weeks' rent in recognition that finding 6 weeks' worth of rent can cause financial difficulties for tenants. Tenants are required to find large sums of money at the start of a tenancy which can pose a significant financial challenge. By reducing the cap on security deposits, the private rented sector will become more affordable while also protecting landlords from rogue tenants.'[41]

We accept that a deposit of 5 weeks' rent does offer more tenants greater affordability benefits. However, as table 6 demonstrates, a cap of five weeks' rent has a correspondingly greater financial impact on landlords. We estimate that capping deposits at 5 weeks' rent will cost landlords approximately five times more than a cap at six weeks' rent. The deposit is only retained by the landlord in instances where the tenant defaults on their obligations under the tenancy agreement and thus the cost to landlords is money that they are entitled to in order to cover issues such as unpaid rent, damage to property, lost items, and cleaning costs.

We do not want to unfairly impact landlords financially. We anticipate the impact on business of a cap at 6 weeks' rent to be small given that only a minority of rented properties require a deposit greater than 6 weeks' rent, and in turn, a very small number of deposits are disputed or insufficient to cover any breaches under the tenancy agreement. Whilst there could be a behavioural effect where landlords charging less than 6 weeks' rent deposit now move towards the cap, we do not anticipate this to happen on a significant basis as these landlords could already charge a deposit equal to 6 weeks' rent should they wish. We will continue to encourage landlords to consider on a case by case basis the appropriate level of deposit to take.

Our preferred option is therefore option 3 (capping deposits at 6 weeks' rent) since this will achieve the stated policy objective of assuring fairness and affordability for tenants at the outset of a tenancy (i.e. ensuring that they cannot be charged a disproportionately high deposit) whilst enabling landlords to retain the flexibility to secure adequate financial security for their asset.

Where landlords need more than 6 weeks' rent money to cover any damages or unpaid rent they are unlikely to have asked for this money now, and would still be eligible to pursue this money through the courts or direct from the tenant.

Summary of preferred option

Our preferred options will lead to greater competition in the rental market and protect tenants. On average, across the 10 year appraisal period, tenants will benefit on average by £259m per year (once discounted). Letting agents will see a revenue loss averaging £168m

[41] https://publications.parliament.uk/pa/cm201719/cmselect/cmcomloc/583/583.pdf

per year once discounted, and landlords £89m, once accounting for pass throughs. Whilst large in aggregate, this largely reflects the size of the market – the PRS accounts for 4.7 million households (20% of all households), and the costs and benefits should be considered on an individual tenant, landlord, and letting agent basis. The wider market and society will benefit from increased competition and efficiency as a result of the Bill.

The Tenant Fees Bill will ban landlords and their agents from requiring tenants and licensees and persons acting on their behalf or guaranteeing their rent to make any payments in connection with a tenancy with the exception of:

- the rent;
- a refundable tenancy deposit (reserved for any damages or defaults on the part of the tenant) capped at no more than six weeks' rent;
- a refundable holding deposit (to reserve a property) capped at no more than one week's rent;
- certain payments on assignment, novation or variation of a tenancy when requested by the tenant capped at £50, or reasonable costs incurred if higher;
- payments associated with early termination of the tenancy, when requested by the tenant;
- payments in respect of utilities, communication services and council tax; and
- payments in the event of a default of the tenant (such as replacing a lost key or late rent payment fine), capped at the level of the landlord's loss..

The Bill also bans agents and landlords from requiring tenants to make payments to third parties (with the exception of utilities, communication services and council tax payments). This mitigates the risk of tenants being charged agent fees through other routes, avoids creating a situation where landlords are encouraged to self-manage their properties purely on financial grounds and avoids some tenants being charged fees whilst others are not.

The Bill enables agents and landlords to charge a holding deposit to reserve a property while reference checks etc. are carried out. The Bill requires agents and landlords to refund the holding deposit to tenants except in circumstances where the tenant withdraws, fails a right to rent check or provides false or misleading information, which materially affects their suitability to rent the property. Exempting tenant default and variation fees from the ban will also ensure that the landlord or agent is not unfairly penalised by costs that are outside of their control.

The holding deposit provisions are intended to respond to concerns raised during the consultation that tenants are speculating on a number of properties, which could result in potentially unnecessary and costly work by agents and landlords. Similarly, enabling a landlord to charge fees related to a default by the tenant (such as a late payment or lost key) means that a landlord is not unfairly penalised by costs incurred owing to an action of the tenant. Landlords will only be permitted to charge the amount of any loss incurred.

The enforcement of the ban will be carried out by local authorities with a provision for the designation of a Lead Enforcement Authority to provide guidance and support to enforcement authorities regarding the operation and enforcement of the fee ban.

A breach of the fees ban will usually be a civil offence with a financial penalty of £5,000 but if a breach is committed within 5 years of the imposition of a financial penalty or conviction for a previous breach this will be a criminal offence. Local authorities will have discretion to decide whether to prosecute or impose a financial penalty for the offence but guidance on this will be issued. The penalty for the criminal offence, which will be a banning order offence under the Housing and Planning Act 2016, is an unlimited fine.

Local authorities will be able to retain the money raised through civil penalties for future local housing enforcement. The Bill also enables tenants to recover unlawfully charged fees.

Finally, the Bill will make some amendments to the Consumer Rights Act 2015 to apply the letting agent transparency requirements when agents advertise on property portals (e.g. Rightmove, Zoopla), to provide clarity around how many times local authorities can issue a civil penalty for lack of compliance and to state that agents must provide the name of the Client Money Protection scheme of which they are a member. The Bill will also amend the Housing and Planning Act 2016 to state that County Councils will have enforcement responsibility for the requirement on letting agents to belong to a client money protection scheme.

The Bill will improve competition in the lettings sector by capitalising on the stronger market position of landlords, recognising that letting agent services are primarily provided on their behalf and that landlords, unlike tenants, are able to negotiate the letting fees charged. The ban will increase letting agents' incentives to compete for landlords' business by providing lower overall fee levels and good quality of service thus making the sector more competitive, more affordable and of a higher standard.

5. Monetised and non-monetised costs and benefits of preferred option

The impact of the policy will have costs and benefits to various groups – most of these impacts fall on tenants, landlords, and letting agents. The main effects of the Bill have been monetised, there are also significant non-monetised impacts which have been considered and where they have not being monetised these are outlined below.

The table below provides a summary of the cost benefit analysis.

Table 7: Summary of impacts, 2017 prices, central scenario (£ million)

10 year undiscounted cost	**10 year undiscounted benefit**	**Net Benefit**	**Net Present Value**	**EANDCB (2014 prices)**
3078.5	3045.9	-32.6	-34.5	340.3

The table above summarises the cost benefit analysis in the central scenario – i.e. our best estimate of the impacts of the policy. The annex contains further tables with a full profile of costs and benefits across the low, central, and upper scenarios. Both landlords and letting agents are classified as businesses and enter the Equivalent Annual Net Direct Cost to Business (EANDCB) estimates. Cost estimates in table 7 include familiarisation costs.

There is an important distinction between the estimates that form part of the EANDCB figure and all other estimates. The EANDCB is the expected loss to landlords and letting agents from the ban on tenant fees and the cap on deposits, before any pass through. We expect some pass through from the ban on tenant fees with letting agents charging landlords higher fees and some landlords charging tenants higher rent. This pass through is excluded from the EANDCB estimate, as guidance suggests that such costs are indirect costs and cannot be included. The impacts of the pass throughs are included in the wider NPV calculations. The EANDCB figure also does not include pass throughs between businesses – i.e. letting agents passing costs to landlords. This would influence where the EANDCB falls on specific types of businesses but would not change the overall headline figure.

The EANDCB is based on an expected 4 million households staying in the PRS in 2019/20 and we assume all are potentially subject to renewal fees, and 1.4 million moves to or within the PRS (i.e. existing PRS households changing home, or new households to the PRS). We then apply our estimates of the proportion of landlords that use agents (51.5%), the average letting agent tenant fee (£223) and renewal fee (£72), apply the proportion of landlords that charge tenant fees (50%), and apply our best estimate of the average letting fee charged by landlords (£26) and assume no renewal fees from landlords[42]. We then add the estimated losses to landlords from the deposit cap. We also assume the PRS grows 5% per annum based on the historical growth rate of the PRS, inflating the loss to businesses and the benefits to tenants.

Over a full 10 years, the net present value of the policy is estimated at -£34.5m. The policy primarily implies a redistribution from letting agents and landlords to tenants – a transfer of costs or benefits from one group to another, with the negative NPV primarily resulting from familiarisation and enforcement costs. However, there are wider productivity benefits by increasing efficiency and fairness in the lettings sector (by reducing the ability of letting agents to overcharge and double charge landlords and tenants) and by reallocating resources to more productive industries. It is not possible to robustly monetise these benefits but they are outlined below and likely mean the Bill is beneficial for the market and society overall.

Detail of monetisation in NPV estimates

We have monetised the following benefits for the following groups:

- Tenants – impact of paying no letting fees. Benefits from reduction in paid deposits. Benefits from reduced deductions from deposits, representing a cost to landlords.
- Landlords – higher rent as a result of a reduction in letting fees.
- Letting agents – higher fees to landlords to compensate for lost tenant fees.

We have monetised the following costs for the following groups:

- Tenants – impact of paying higher rent as a result of a reduction in letting fees. Assuming that rents were to increase, it would become much simpler for tenants to understand and compare rental costs. It would also be easier for tenants to manage these regular and expected costs rather than high upfront and often hidden charges that fees represent. More than one third of tenants who responded to the Government's consultation on banning letting fees believed that rents would rise, but a quarter of that group explicitly said that a rise in rents was preferable to upfront fees as it would be more affordable and transparent.
- Landlords – impact of being charged higher letting agent fees, loss of revenue from the ban of charging letting fees where a landlord charges them, reduction in deposit protection, and familiarisation costs of understanding and adjusting to new regulations.
- Letting agents – familiarisation costs of understanding and adjusting to regulations, loss of revenue from the ban on letting fees.
- Government – expected costs of enforcement.

In addition, there are other benefits and costs that we have not monetised. In terms of benefits, these include:

42 Evidence from landlord associations and from the consultation suggest a wide range of landlords that charge fees, and what levels they charge. We consider this information together to come to a central estimate of £26, we assume no renewal fees from landlords in the absence of further data.

- Tenants – less costly for tenants to move from current home, and more transparent pricing allowing for better decision making. Tenants would be required to find less money at the outset of a tenancy. This may lead to reduced instances of financial difficulty and tenants would also be financially more capable of re-locating and leaving a bad or unsuitable rental. This may serve to increase pressure on landlords to improve property standards. There are also wider economy and social benefits arising from improved tenant mobility.

  A ban on tenant fees may also help to promote longer term tenancies where these are wanted since there would be no financial incentive for an agent in offering short terms tenancies that need frequent renewal. This would serve to provide tenants with greater security, which would particularly benefit families with children who are increasingly represented in the private rented sector and who can have schooling services disrupted by the need to secure a new rental property. Between 2006-07 and 2016-17, the number of households with dependent children in the private rented sector increased by around 966,000. There are approximately 1.8 million households in the private rented sector with dependent children.[43]

  We have not monetised these benefits given the difficulty in estimating the welfare gain from more optimal decision making on the choice of property. Tenants will benefit from being able to fully appraise upfront the respective cost and benefits of potential homes to rent, rather than discovering hidden fees too late into the process, which if they had known, may influence their choice of home.

  In addition, as we believe the profits resulting from tenant fees to letting agents arise because of the market failing, and therefore these profits are above what would be earned in a market operating in good and effective competition. These profits are argued to be supernormal profits, and in turn, may be more efficiently spent in the economy by tenants.

- Landlords – potential lower incidence of rent arrears.

  We have not monetised this benefit given the uncertainty of the impact on rent arrears. The English Housing Survey reports that 9% of private renters were either currently in arrears or had been in the last 12 months, a figure unchanged since 2011-12.[44] Whilst tenant fees can involve significant sums of money being required at the outset of the tenancy, in comparison to monthly and annual rents they are small and so this impact is likely to be minor. For example, the mean tenant fee is estimated at £223 in 2014-15 English Housing Survey compared to annual rents of £8,100 during October 2016 to September 2017.[45]

- Letting agents – more competitive market for those operating competitive and innovative business models. Further, some responses to the Government's consultation, particularly from tenants, pointed out that banning fees may improve the image of the letting industry, and thus relationships between tenants and agents, by removing some of the concerns that tenants currently have over the costs charged for services provided.[46] This could lead to an increase in business for letting agents, which in turn

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[43] English Housing survey, Headline Report, 2016-17 https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/675942/2016-17_EHS_Headline_Report.pdf

[44] English Housing survey, Headline Report, 2016-17 https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/675942/2016-17_EHS_Headline_Report.pdf

[45] Private Rental Market Summary Statistics, October 2016 to September 2017 https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/667109/PRMS_Statistical_Release_171214_.pdf

[46] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/656211/Govt_response_to_consultation_on_banning_letting_fees.pdf

could lead to greater professionalisation of the lettings sector if landlords recognise that tenants are more likely to rent a property through an agent.

This has not been monetised as it is difficult to assess before the implementation of the policy how letting agents will innovate and offer better services, and the monetised benefit that would result from this.

- Third Party suppliers to the lettings market – more competitive market for those operating competitive and innovative business models.

  This has not been monetised as it is difficult to assess before the implementation of the policy how third party suppliers will innovate and offer better services, and the monetised benefit that would result from this.

- Society – reduced homeless acceptances leading to a potential reduction in temporary accommodation costs, and a more productive allocation of resources due to efficiency gains in competition.

  This has not been monetised as there is significant uncertainty on the reduction of homeless acceptances that will result. On 30th September 2017, 79,190 households were in temporary accommodation. In addition, between 1st July and 30th September 2017 local authorities accepted 15,290 households as being statutorily homeless.[47]

In terms of un-monetised costs, these include:

- Landlords – potential loss of interest on deposits. A landlord has a choice to protect the deposit in a custodial scheme, where all of the deposit is transferred and held by one of the deposit protection providers, or an insured scheme, where the landlord holds the deposit. If there if a dispute at the end of the tenancy, the disputed amount must be transferred to the deposit scheme. In the latter case, as the landlord holds the deposit, there is a potential small loss of interest that would be earned on that deposit by keeping it in a bank account. This cost is minimal – on average £1.63 per deposit for landlords that end up taking a lower deposit and uses an insured deposit scheme.[48] As the cost is minimal, we have not monetised it as part of the NPV and EANDCB calculations,

- Letting agents – closure of letting agent branches and employment losses. We are not able to reliably forecast the loss of employment from the ban on tenant fees. Those agents losing business are likely to be those most reliant on supernormal profits, benefiting from market failures, and in turn who are not able to adapt their business models effectively. If it is the most inefficient agents that leave the market, then in turn market efficiency would improve. Conversely, it is possible that the lower cost of signing tenancies through a letting agent may lead to increased demand by tenants for properties managed by letting agents. A number of responses to the consultation, particularly from tenants, pointed out that banning fees may improve the image of the letting industry and thus the relationships between tenants and agents, and removed some of the concerns that tenants currently have over the costs charged. This, in turn, could lead to an increase in business for letting agents.

[47] Statutory homelessness and prevention and relief, Q3 2017
https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/667302/Statutory_Homelessness_and_Prevention_and_Relief_Statistical_Release_Jul_to_Sep_2017.pdf

[48] For example, there will be approximately 1.4m new tenancies signed in Year 1, 74% will pay a deposit, of which 14.3% will pay a reduced deposit. The loss to landlords from interest payments only includes landlords who use an insurance based scheme, not a custodial one (approximately 59% of deposits). A tenant lives in their PRS property on average for 3.9 years which indicates that interest may be accrued on average for 4 years. Assuming it does so at the Bank of England base rate of 0.5% and is compounded, the total loss to the overall landlord population is estimated to average £1.63 per deposit when considering median reductions in rent from the deposit cap., which will affect approximately 86,000 of the 1.4m new tenancies signed in year 1.

- Third party suppliers to letting agents (e.g. inventory providers) – downward pressure on prices from a more competitive letting agent sector and reduction in business.

These are further summarised in the tables below.

Summary of benefits and cost

Table 8: Categories of benefits analysed

Group that benefits fall to	Type of benefit	Included in cost-benefit analysis or described qualitatively
Tenants	No letting fees	Monetised
	Benefits from reduction in deposits paid, representing access to money at the start of a tenancy than at the end	Monetised
	Less costly for tenants to move from current accommodation, for example, empowering them to leave poor quality accommodation	Non-monetised
	Increased likelihood of a longer, more secure tenancy due to reduced financial incentive for an agent in offering short terms tenancies that need frequent renewal	Non-monetised
	More transparent pricing allowing better decision making and allocation of lettings	Non-monetised
	Improvement in affordability from deposit cap, allowing for a broader choice of homes to rent.	Non-monetised
Landlords	Higher rent	Monetised
	Lower incidence of arrears	Non-monetised
Letting agents	Higher landlord fees to compensate for lost tenant fees	Monetised
	More competitive market for those operating competitive business models	Non-monetised
Third party suppliers, such as reference companies & inventory providers	More competitive market for those operating competitive business models	Non-monetised
Society	Reduced homelessness acceptances leading to reduction in temporary accommodation costs	Non-monetised
	More productive allocation of societal resources due to efficiency gains from competition	Non-monetised

Table 9: Categories of costs analysed

Group that costs fall to	Type of cost	Included in cost-benefit analysis or described qualitatively
Landlords	Higher letting agent fees (letting agent charging landlords higher fees)	Monetised
	Loss in revenue to landlords from the ban on charging letting fees	Monetised
	Familiarisation costs of understanding and adjusting to regulations	Monetised
	Potential loss in risk protection from damages or non-payment of rent as a result deposit cap (transfer benefit to tenants)	Monetised
	Potential loss of interest on deposits	Non-monetised
Letting agents	Familiarisation costs of understanding and adjusting to regulations	Monetised
	Loss in revenue from the ban on charging letting fees and from landlords choosing not to use agents	Monetised
	Closure of letting agent branches and employment losses	Non-monetised
Third party suppliers, such as reference companies & inventory providers	Downward pressure on prices from more competitive letting agents.	Non-monetised
Tenants	Higher rent	Monetised
Government and LAs	Enforcement costs	Monetised

An appraisal period of 10 years is used as per standard practice for impact assessments, from 2019-20.

The policy is assessed against a 'Do Nothing' – the counterfactual. In this scenario the regulation to ban letting fees to tenants is not introduced and tenancy deposits are not capped. This counterfactual is used as the baseline for the cost-benefit analysis.

Costs and benefits are estimated based on assumptions around the number of expected tenancy moves / renewals in the PRS, the number of letting agents and landlords. Whilst the EANDCB figure does not include pass through from letting agents to landlords and from landlords to tenants, the estimates below do in order to form an estimate of the 3 main groups – letting agents, landlords, and tenants[49]. Where there is uncertainty around an

[49] All estimates, excluding the EANDCB figure only, include our estimated levels of pass through. These need to be considered in order to consider the impact on different groups, letting agents, tenants, and landlords. For example, in the central scenario, we assume 50% of the loss to letting agents from the tenant fees ban is passed through to landlords, and 50% of the total landlord burden is passed on to tenants. These are outlined in further detail in this section.

assumption, upper and lower bound scenarios have been included. The cost benefit analysis is presented in 2017 prices and discounted from the year of implementation in line with the Green Book.

Table 10 summarises the analysis by considering the Net Benefit to four groups. Households in the private sector will see an average annual benefit of £258.6m (discounted) over a 10 year appraisal period. This will result in annual savings of between £26 and £70 per household from the tenant fees ban alone, with larger savings for households that use letting agents and/or that move or renew tenancies frequently. There are additional benefits to tenants who now pay lower deposits as a result of the cap. Greater competitive pressure in the lettings market will ensure that landlords and letting agents will be unable to fully pass on the costs to PRS households. Table 10 presents the estimates of net benefits taking into account direct and indirect costs, and the pass through of revenue losses. For example, they take into account our estimates of how much the loss to letting agents from the ban in tenant fees will be passed through via higher charges to landlords. These rates of pass through are further outlined in the analysis below.

The majority of costs result from a transfer to households from letting agents and landlords. The impact on letting agents, over a 10 year appraisal period and discounted to present values is estimated to average -£167.8m. For landlords the impact is estimated at -£89.3m. Government is estimated to impacted by enforcement costs.

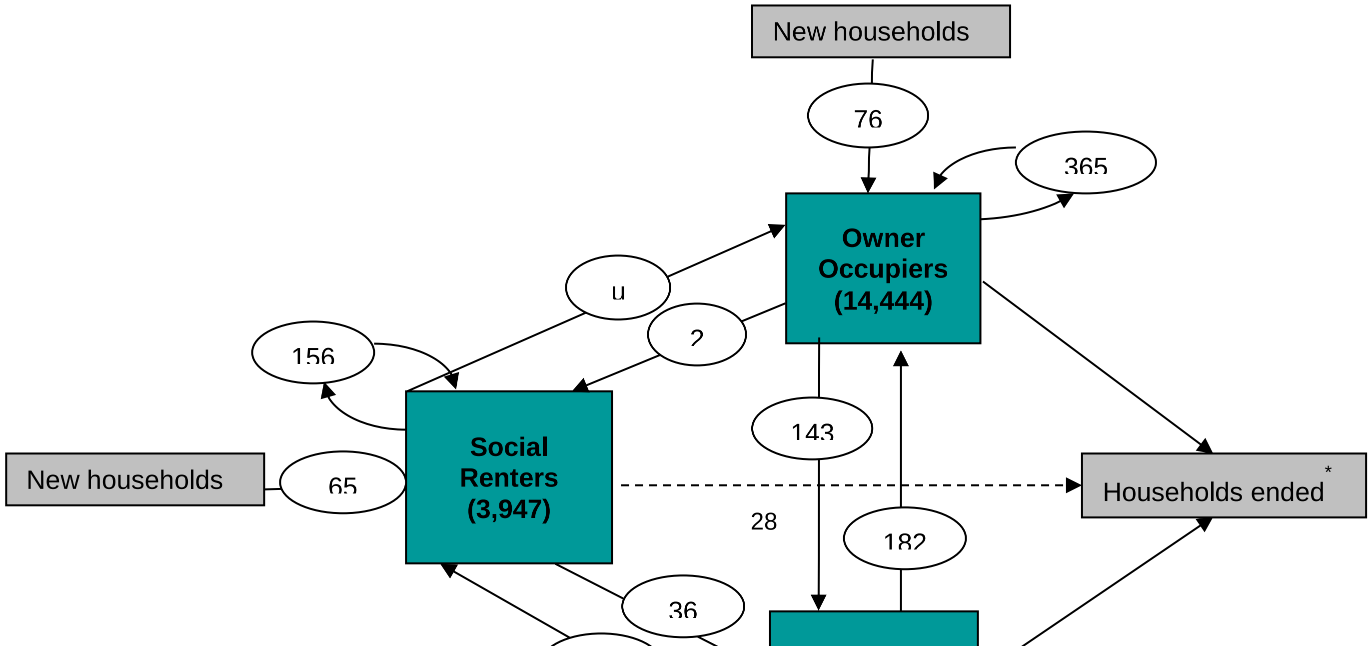
Table 10: 10 year annual average of net benefit by group, central scenario, excluding familiarisation costs

Policy	**Impact on letting agents**	**Impact on landlords**	**Impact on tenants**	**Impact on Government**
Discounted	-£167.8m	-£89.3m	+£258.6m	-£0.4m

Analysis

In 2016-17, there were 860,000 moves within the PRS (for example, from one privately rented home to another). There were an additional 149,000 new PRS households created, 36,000 social renters moving to the PRS, and 143,000 owner occupiers moving to the PRS. This totals to 1,188,000 moves in to or within the PRS.

Figure 3: Household moves (thousands) by tenure, 2016-17



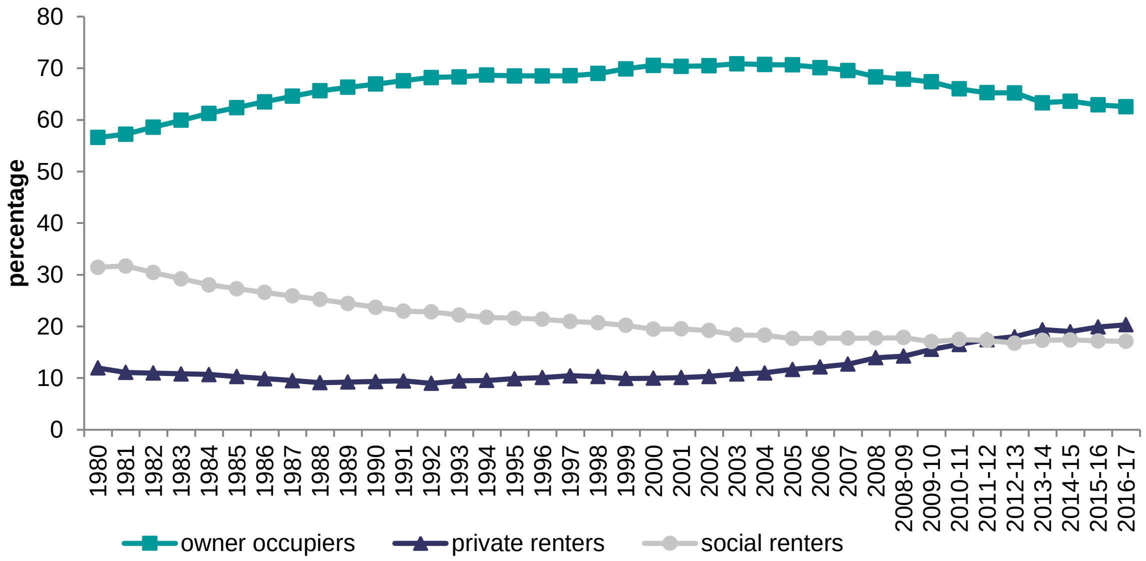
Given the growth in the PRS over the past 10 years, we assume that there will be 1.4m moves to or within the PRS by the expected time of implementation in 2019-20, based on the PRS growing by 5% per annum.[50] This is based on the historical growth rate of the PRS since 2008-09 and the relative stability of the ratio of moves to the size of the PRS stock, illustrated in the table below. In the upper scenario, we assume a 6% growth rate, inflating the cost to letting agents and landlords, and 2.5% in the lower scenario.

Table 11: Growth in PRS households from 2008-09 to 2016-17

Year	Private renters	% Growth rate
2008-09	3,067	
2009-10	3,355	9.38
2010-11	3,617	7.81
2011-12	3,843	6.26
2012-13	3,956	2.93
2013-14	4,377	10.64
2014-15	4,278	-2.26
2015-16	4,528	5.84
2016-17	4,692	3.62

Figure 4: Trends in household tenure, 1980 to 2015-16

[50] This analysis relates to the number of households in the PRS only and should not be used to estimate likely numbers of households in the social rented or owner occupied sectors.



Source: English Housing Survey

In order to consider the impact of the policy from the year of implementation, we adjust the number of moves in and to the PRS, and the number of PRS households, from 2016-17 English Housing Survey data to 2019/20, by applying 3 times the average annual historical growth rate of the PRS (5%).

Below we provide a summary of the monetised costs and benefits on each of the 3 groups – letting agents, tenants, and landlords. The overall estimates depend on assumptions made on the level of pass through – i.e. the extent to which the loss to landlords is passed on to tenants through higher rents, and for example the extent to which losses to letting agents is passed on to landlords.

Letting agents

Not all landlords use letting agents. The Council of Mortgage Lenders (now integrated into a new trade association, UK Finance) Private Landlord survey reported that 63% of landlords involve letting agents in letting and / or managing properties,[51] while the report by Capital Economics, commissioned by ARLA Propertymark, estimated that 40% of landlords use letting agents.[52] For our central case, we take the average between both values: 52%.

The level of fees charged to tenants varies significantly, but for the purposes of this analysis we employ the mean fee charged to households reported in the English Housing Survey (EHS) in 2014/15 - £223. The EHS data represents the most robust estimate and is based on survey data that is a National Statistic. We uprate this to 2017 prices by using the HMT deflator to account for the growth in prices. In the sensitivity analysis, we vary this fee by 25% to account for the range of fees provided by the consultation.

For PRS households that do not move and use letting agents, they may be charged renewal fees. The analysis assumes renewal fees are £72 on average, which is the midpoint between MHCLG desk research that found that the average renewal fee was £75, following a review of 50 letting agents' pricing practices, and analysis from Generation Rent that estimated renewal fees average £68. The estimate is corroborated by evidence from the consultation, where the median estimate provided by agents was £60, while tenants estimated £100.

[51] The Profile of UK Landlords, 2016 https://www.cml.org.uk/news/press-releases/cml-research-survey-of-uk-landlords/

[52] ARLA Propertymark http://www.arla.co.uk/lobbying/housing-research/

By combining the number of PRS households that use letting agents to move and/or renew tenancies with the average cost of each fee, we estimate that letting agents will be deprived of revenue from the loss of tenancy and renewal fees from tenants. This revenue loss, however, as the analysis below shows, is likely to be offset to some extent by an increase in fees to landlords.

> *Gross revenue loss to letting agents = (Proportion of landlords that use agents)*{(No. of PRS household moves)* (letting tenant fee) + (No. of PRS renewals)*(renewal fee)}*[53]

This is the estimate of the gross revenue loss. Some of this revenue loss will be passed on to landlords. We assume 50% pass through to landlords for the reasons outlined below in the cost to Landlords section (see next section, Landlords – Ban on tenant fees).The net revenue loss to landlords is illustrated by the formula below.

> *Net revenue loss to letting agents = (1- pass-through rate to landlords)*(gross revenue loss to letting agents)*[54]

We assume no costs to letting agents from the deposit cap and assume these costs fall to the property owners – landlords.

Landlords

Ban on tenant fees

The majority of landlords own only one letting, but the majority of the dwelling stock is owned by landlords with more than one property (CML Private Landlord Survey 2016).[55] Based on the 2010 Private Landlords survey, we estimate that the average landlord owns 2 PRS lettings. However, this is not evenly distributed – with 78% of landlords only owning one dwelling, but representing 40% of the total stock. In the central scenario, we estimate there are approximately 2.75 million landlords based on the expected growth in the PRS if it continues to grow at its historical growth rate.

It's likely that letting agents will recoup some of the revenue from tenant fees by passing them on to landlords via higher fees. The consultation responses showed that agents and landlords believe that one of the key impacts of the ban would be higher fees to landlords, with circa 40% of agents and landlords raising this issue. This is supported by research from the National Landlord Association that shows 79% of landlords believe their fees will increase as a result of a ban.[56] An increase in fees to landlords may have a number of overlapping effects:

a) Some landlords may increase rents to cover the increase in fees;
b) Some landlords may pay the increased fees in full without passing it on in higher rents;
c) Some landlords may stop using their letting agent;
d) Some landlords may attempt to renegotiate with their letting agent;
e) Some landlords may search for a more competitive letting agent;
f) Some landlords may withdraw from the market, though this is likely to be small.

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[53] 52% * 1.4m moves * £223, plus 51.5% * 4m renewals * £76 = £314.4m once inflated to 2017 prices.

[54] (1 – 0.5)* £314m = £157m.

[55] The Profile of UK Landlords, 2016 https://www.cml.org.uk/news/press-releases/cml-research-survey-of-uk-landlords/

[56] https://www.landlords.org.uk/index.php/agents/press/releases/landlords-stand-agents-in-wake-tenant-fees-ban

It is highly likely that at least a proportion of the lost revenue will be passed on to landlords. Letting agents play a role in matching households to homes, carrying out checks, and drawing up contracts. Landlords will continue to demand and be willing to pay for these activities.

However, it is very unlikely that the fees will be passed on to landlords in full due to greater competition between letting agents to hold on to and attract business from landlords. Currently, tenants are unable to exert sufficient competitive pressure on letting agents, as the choice of a letting agent is primarily one by the landlord and not the tenant. Some agents are also double charging both tenants and landlords or over charging. Under the fees ban, the charges levied by letting agents should be a fairer reflection of the economic value of the services provided given that letting agents will solely be selling their services to their primary customer, the landlord.

We expect that landlords using letting agents will see their fees rise by an amount equivalent to 50% of what their letting agent was charging their tenant. This is in line with a report from Capital Economics prepared for ARLA Propertymark, which argued that the pass-through rate is likely to be 50-100 per cent.[57]

Letting agents will continue to need a revenue source from letting privately rented homes and given the size of the private rented sector, households will continue to demand the services of letting agents. Letting agents play a crucial role in the management of properties, organising viewings, and providing a source of tenants to landlords. That intuitively suggests that letting agents will continue to survive, and if tenants do not provide the revenue for these services then it must be landlords instead.

We are limited in arriving at a precise estimate of pass through of the loss of letting agents to landlords. However, 50% represents the most sensible scenario taking in the available evidence. On the one hand, there is evidence of excess profits due to ineffective competition, on the other, the services of letting agents will continue to be demanded and some group of the population will need to pay a fee at least equal to normal levels of economic profit so letting agents continue to trade in the rental market.

Taking that information, we expect a 50% rate of pass through, indeed a general average and approximation suggests around 50% of the fees charged to tenants can be considered to be commensurate to the expected resource cost and normal profit, for example, by considering the level of charges letting agents charge tenants compared to landlords. A reference check can be found on the open market for £30 but tenants reported a mean charge of £137 in response the consultation. Even considering normal levels of profit and costs of time for letting agents staff to conduct the check, fees such as these are approximately twice as much as the prices on the open market, even when factoring in a few hours of labour to conduct such checks.

Hence, some but not all of the fees will be passed on because:

- There is evidence of supernormal profits, and the ban on fees will result in more competitive pressure on letting agents as tenants will be able to see, in a given advertised rent, how much the property will cost them. Evidence from the consultation indicates around half of tenants didn't know the level of fee they will be charged.

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[57] http://www.arla.co.uk/media/1045728/letting-the-market-down-assessing-the-economic-impacts-of-the-proposed-ban-on-letting-agents-fees.pdf

- Landlords, who may be charged higher fees, will be better incentivised to ‘shop around’ and exert their bargaining power.
- This evidence of supernormal profits stems from this problem of asymmetric information highlighted above, but other issues exist with the market also. For example, there is evidence of letting agents double charging landlords and tenants. Landlords or tenants have little incentive to exert competitive pressure to reduce this problem as they are unlikely to know it is happening and primarily care about the fee they are themselves charged.

The regulation will also ban landlords, as well as letting agents, from charging tenant fees. The responses from the consultation indicate that c.50% of self-managing landlords do not charge fees. For those that do charge, these fees tend not to be as high as those charged by letting agents. Considering the range of responses to the consultation, fees from landlords are likely to range between £1 and £50. Taking both as lower and upper sensitivities, we use £26 as a central case. This is about a tenth of the average fees charged by letting agents.

We recognise that letting agents have higher staff and overhead costs, hence justifying some of the higher cost of tenant fees by letting agents. However, as the level of fees charged by landlords is significantly lower than those by letting agents, in the central scenario we assume that 50% of the cost to letting agents is passed to landlords, which is the lower bound estimate of the ARLA Propertymark report. Given the uncertainty of the true pass through that will result, we vary this from 40% pass through to landlords in the upper scenario and 60% in the low scenario. A precise figure is not possible with available data, but this represents the most sensible assumption for the reasons outlined above.

Gross cost to landlords = (Revenue loss to letting agents that is passed on to landlords through higher fees) + (No. of PRS household moves into or within PRS)(1 – proportion of landlords that use agents)*(proportion of landlords charging fees)*(landlord tenant fee)*[58]

The above formula suggests the gross cost to landlords is the proportion of the loss to letting agents that is passed through to landlords via higher fees, and the loss of fees to the landlord population where they charge tenant fees themselves.

Therefore landlords will see an increase in letting fees from letting agents and will be unable to charge fees to tenants, in turn, there is also the pass through from landlords to tenants to consider from this effect In both scenarios, landlords may attempt to shift the cost burden to tenants via higher rents. Some will be able to pass the cost through in full, others will be unable to do so, with the majority in between. We do not expect that the full level of letting agent costs will be passed on to landlords because:

a. A significant proportion of landlords currently self-manage and do not charge fees. This sector of the market may limit the ability for other landlords to increase rent.
b. Landlords will be better incentivised to choose and find the most cost efficient letting agents.
c. There is limited capacity for tenants to absorb extra housing costs. The English Housing Survey shows that households in the PRS pay a significantly higher proportion of income on housing costs than those in other tenures. However, this proportion has mostly stayed stable over the past number of years.

[58] £157m + (1.4m * (1- 52%) * 50%* £26) = £166m.

Figure 5: Mortgage/rent as a proportion of household income (including and excluding housing benefit), by tenure, 2016-17[59]

The ARLA report citied earlier suggests 90% of letting agents expect rents to rise. 41% of landlords stated they would increase rents for new tenants if their cash flow position worsened. This report argued that due to the nature of competition in the rental market (closer to monopolistic competition, with a number of landlords and letting agents bidding for the same customer, than a monopoly market), that the pass through rate from landlords to tenants is likely to be around 50%.[60] It is difficult to observe and predict the level of pass through prior to the ban. In the absence of firm evidence as to the intentions of landlords, and considering the limited ability of PRS households to absorb extra rent, as well as the evidence available, we assume that 50% will be passed on. The higher rent will reduce the net costs to landlords. The majority of respondents to the consultation – including letting agents, landlords and tenants – believed that rents would rise as a result of the ban. In the upper scenario, we assume 60% is passed on – therefore reducing the costs to landlords, and in the low scenario 40%. There is uncertainty around this number which we are not able to address given the limited evidence available – 50% represents our best estimate based on the justifications above.

Net cost to landlords from ban on tenant fees = (1 – pass-through rate to tenants)(Gross cost to landlords)*[61]

It is also likely that some landlords may decide not to use letting agents. According to the consultation, 76% of landlords said that an increase in fees from letting agents would affect their decision to use an agent in the future. A survey carried out by the Deposit Protection Scheme, found that 13% of landlords would stop using agents if fees increased.[62]

As landlords spend time undertaking tasks in lieu of their letting agent – we would expect them to increase rents as compensation. However, in the absence of robust evidence as to

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[59] English Housing Survey, 2016-17.

[60] http://www.arla.co.uk/media/1045728/letting-the-market-down-assessing-the-economic-impacts-of-the-proposed-ban-on-letting-agents-fees.pdf

[61] £166m * 0.5 = £83m.

[62] As part of their consultation response, the Deposit Protection Scheme surveyed 1,928 landlords. Of the landlords currently using agents, 13.3% said that they would stop using agents if fees increased.

the extent landlords would choose to self-manage, we have not quantified this effect. A reduction in landlords using agents would decrease the costs to landlords and increase the cost to agents.

Cap on deposits

Our best estimate is that a cap at 6 weeks' rent will result in 1.4% of deposits resulting in a loss to the landlord. In the upper and lower scenarios, we vary this estimate by 15% to account for the uncertainty of the true figure. The estimated median loss to these landlords from our analysis of a sample of custodial data is £89 per deposit.

These costs will only arise for a small minority of landlords where the deposit does not cover all the landlords' costs at the end of the tenancy (for example unpaid rent, or damages to the property). The English Housing Survey (2016-17) reports that the average time a tenant has been living in their current property as 3.9 years. Therefore we assume that on average, this cost to landlords begins in Year 4, once tenancies that benefited from the cap in Year 1 begin to end.

The cost is estimated at £1.3m starting in Year 4, increasing from then on in as we assume that the PRS grows by 5% annually. This cost will occur to landlords when tenancies that benefit from the deposit cap begin to end (3.9 years on average). For simplification, we therefore begin to count these costs from year four onwards. In reality, some tenant households end tenancies before 3.9 years and some afterwards, but the average is 3.9 years so for the purposes of simplification, this cost enters the NPV from year 4 onwards which is the point which the average tenancy will end. They then continue annually in the NPV calculation, increasing due to the assumed growth in the PRS. In the upper scenario this cost is estimated at £1.6m and £900k in the lower scenario. This represents the reduction in the deposits claimed by landlords compared to the counterfactual.

*Net cost to landlords from deposit cap = Estimated tenancies ending in Year 4, from tenancies signed in Year 1 * proportion of landlords charging deposit * proportion of deposits resulting in a loss * median estimated loss*[63]

This net cost to landlords from the deposit cap continues from Y4 to Y10 in the 10 year appraisal period, increasing every year from Y4 onwards due to the assumed growth in the PRS. We assume no pass through in terms of rents to tenants from the deposit cap. In reality, this cost to landlords may be an over estimate as it is based on a sample of custodial data that may not be representative of the overall tenant population, and landlords would be fully entitled to continue to pursue tenants for any shortfall including court action should they wish. This cost to landlords represents a transfer to tenants, described below.

Tenants

Ban on tenant fees

Tenants will save from no longer paying letting agent and landlord fees, with a proportion of the saving offset by higher rents. In the consultation, more than a third of tenants said they expect rents would rise, but a quarter of that group explicitly said that that an increase in rents would be preferable to upfront fees as it would be more affordable and transparent.[64]

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[63] 1.4m * 74% * 1.4% * £89 = £1.3m once rounded.

[64] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/656211/Govt_response_to_consultation_on_banning_letting_fees.pdf

That said, we expect that the savings in fees will outweigh any increase in rent due to landlords exerting competitive pressures on letting agents and the limited ability for landlords to increase rents in compensation. In aggregate, we expect that the average household in the PRS will save between £26 and £70 annually over the 10 year period from the ban on letting fees alone.

The monetised benefit will be equivalent to the annual net costs to letting agents and landlords, accounting for the higher rent tenants will face.

> *Net benefit to tenants = (Net cost to landlords from tenant fees ban) + (net cost to letting agents from tenant fees ban)*[65]

As the net benefit to tenants is estimated from the above calculation, it therefore relies on our estimates of pass through. These rates of pass through have been described and justified in the above analysis.

The estimates of pass through do not affect the estimated EANDCB, which is based on no pass through.

Cap on deposits

The benefits of the deposit cap are estimated as the benefits from the reduction in deposits paid, and the transfer of the costs to landlords where the deposit no longer covers damages or unpaid rent, to tenants. The former represents the movement of money from the future to the present day, a benefit starting in the first year of the policy. The latter represents an actual reduction in expenditure by tenants from deductions to their deposit by landlords, and increased expenditure for landlords, starting in year 4 of the policy and continuing thereafter.

In the central scenario, we estimate that there will be a reduction of £12.1m paid in deposits in Year 1 of the policy. This assumes there is no behavioural impact where landlords charging less than 6 weeks now increase the deposits they request towards the cap. To avoid double counting the cost to landlords from lower deductions of deposits, we subtract the estimated £1.3m cost to landlords estimated in Year 4. This totals £10.9m. Tenants have lived in their current PRS property on average for 3.9 years. The value of this £10.9m to tenants, after applying a discount rate of 3.5%, would be £9.5m in 4 years time. Therefore the net benefit estimated in Year 1 of the policy is £1.4m, increasing each year due to the assumed growth in the PRS.

*Benefit to tenants from the deposit cap = (Estimated PRS moves * % of tenants paying a deposit * % of tenants whose deposit is reduced * Estimated median reduction in deposit – estimated cost to landlords in Year 4) - value of this calculation in 3.9 years time.*[66]

In addition, the £1.3m cost to landlords assumed to occur from Year 4 onwards represents a transfer to tenants. Rather than just the movement of money from the future to the present day, it represents an actual reduction in expenditure for tenants (through a deduction in their deposit), and an increased one to landlords. Therefore this cost to landlords from Year 4 onwards also appears as a benefit to tenants in the NPV calculation. It continues from Y4 to

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[65] £82.9m + £157.1m = £240m.

[66] 1.4m * 74% * 14% * £83 = £12.1m once rounded. The transfer benefit starting in Year 4 is then subtracted to give £10.9m . The value of this money is present day terms, had it being received 4 years later, is £9.5m. The net benefit in Year 1 is £10.9m - £9.5m = £1.4m, increasing annually due to the assumed growth in the PRS. In reality, the benefit is higher if a tenant, after 3.9 years, moves to another PRS property and therefore recycles the deposit.

Y10 in the 10 year appraisal period, increasing every year due to the assumed growth in the PRS.

Summary

Table 12: Costs and benefits to each group in 2019-20 (Year 1) only, by scenario, excluding familiarisation costs[67]

		Central	Upper	Lower
Letting agents	Costs (revenue loss no letting fees)	£314.2m	£456.5m	£192.0m
	Benefits (revenue gain from higher landlord fees)	£157.1m	£182.6m	£115.2m
	Net cost	£157.1m	£273.9m	£76.8m
Landlords	Costs (revenue loss from no letting fees & higher landlord fees)	£165.8m	£195.7m	£115.6m
	Benefits (higher rent)	£82.9m	£78.3m	£69.3m
	Net cost	£82.9m	£117.4m	£46.2m
Tenants	Costs (higher rent)	£82.9m	£78.3m	£69.3m
	Benefits (No letting fees)	£322.9m	£469.6m	£192.3m
	Benefit from reduction in deposits	£1.4m	£1.4m	£1.3m
	Net benefit	£241.3m	£392.7m	£124.3m

Table 12 presents the results of the impacts that have been monetised. In the central scenario, letting agents are estimated to have a direct cost of £314.2m in 2019-20 as a result of no longer being able to charge tenant fees – this is a revenue loss. Our modelling then suggests that there are estimated to be £157.1m in benefits from a revenue gain from charging landlords higher fees. The net cost to all letting agents is therefore estimated at £157.1m, in the first year of implementation. With 16,000 estimated letting agents branches, that is an approximate cost averaging £10,000 per letting agent branch in Year 1.

In the central scenario, landlords are expected to lose in total £165.8m in 2019-20 – this is an annual cost and also increases per year due to the expected growth in the PRS. This

[67] All figures rounded.

loss stems the impact of no longer being able to charge letting fees themselves directly, and from letting agents passing on a proportion of their own burden to landlords. However, there is then an estimated benefit of £82.9m from the benefits of expected higher rent. Consequently, the net cost to landlords is estimated at £82.9m. With 2.75m landlords estimated in the central scenario, that suggests an average cost to landlords of £31 in Year 1.

The aggregate net costs to landlords and letting agents are estimated to directly transfer to tenants. Tenants therefore see a net benefit of £240m in 2019-20 from the letting fees ban alone, and an estimated benefit of £1.4m from the reduction in deposits paid. The total net benefit estimated to tenants in Year 1 of the policy is £241.3m in the central scenario (once rounded).

The cost to landlords, which is a transfer benefit to tenants, from the deposit cap does not appear in the above table as we have assumed on average it will start in Year 4 of the policy as described in the above analysis. The above table (Table 12) illustrates the costs and benefits in the first year of the policy only.

By way of summary, the key effects monetised are, and presented in the NPV calculations over a 10 year appraisal period:

- The ban on letting fees for new tenancies and those renewed, taking into account estimates of pass through by landlords being charged higher fees, and tenants being charged higher rent.
- The deposit cap, of which two main effects are monetised, whilst similar they are different estimates. This pertains to i. some tenants paying a lower deposit, and ii. some landlords in a small number of instances, when they take greater than 6 weeks deposit and go on to retain greater than 6 weeks deposit, experiencing a cost from a reduction in the claim they make on deposits. The former (i.) is treated as a net welfare gain to tenants with no costs to landlords and starts from Year 1, the latter (ii.) is treated as a cost to landlords which is treated as a transfer to tenants and starts from Year 4, continuing to Year 10.

Familiarisation costs

Fees make up a significant proportion of revenue for letting agents. Consultation responses indicated that fees makes up about 10-40% of revenue, with 20% being the most common response.[68] This is supported by the Capital Economics report commissioned by ARLA Propertymark, which estimates that 20% of letting agents' revenue comes from fees.[69] Therefore, letting agents will need to spend time familiarising with the regulations, adapting their business model and renegotiating contracts with landlords.

Contracts drawn up between letting agents, landlords and tenants to reflect the Bill will not be an additional burden as the process would have occurred in the counter-factual, hence, in many cases they do not represent an additional cost. Extra costs will arise only when the Bill prompts a renegotiation of an existing contract. It is likely that the vast majority of agents will renegotiate contracts with landlords on a tenancy by tenancy basis. In addition, much of the industry is already aware of the background of the policy and proposed measures.

[68] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/656211/Govt_response_to_consultation_on_banning_letting_fees.pdf
[69] http://www.arla.co.uk/media/1045728/letting-the-market-down-assessing-the-economic-impacts-of-the-proposed-ban-on-letting-agents-fees.pdf

There are approximately 16,000 letting agent branches in England. The ARLA report estimates the letting agent industry employees 58,000 workers, which suggests an indicative average of 3.6 employees per letting agent branch.[70] The average number of properties managed by a letting agent is approximately 200.[71] According to EHS data, the majority of these tenancies will be for 12 months or less (81%). The familiarisation burden to letting agents will involve:

- Reading guidance the department will publish fully outlining the requirements of the Bill.
- Spending time developing their business models as a result and reacting to the implications of the Bill. This will for the most part also involve considering their best response to changing the fees charged to landlords.
- Whilst the re-negotiation of tenancies already happens in the counterfactual, there will be some small additional re-negotiation to reflect the fact that there is a deposit cap, which rents may respond to, and the ban on letting fees, which rents levels may also respond to. Consequently rent levels may need to be re-considered more so than compared to the counterfactual.

We are limited with available data to monetise this familiarisation cost accurately. However, taking in that information, we expect that there will circa 1 hour per employee to read and comprehend the guidance, which we anticipate will be around 20-30 pages, and circa 15 hours or above to develop business models in response to the requirements of the Bill.

In total, that results in an estimate that each letting agent branch will need to spend a cumulative amount of approximately 20 hours adjusting to the ban. As stated there is uncertainty around the expected familiarisation time, consequently we vary this figure by 50% in the sensitivity analysis.

Landlords would also need to spend time adjusting to the ban, and understanding that the deposits they request can no longer be greater than 6 weeks' rent. We assume that landlords that use letting agents do not need to familiarise themselves with this Bill as they primarily appoint a letting agent to organise the management of their properties. In some cases, landlords using letting agents which incur familiarisation costs but we expect this to be mostly accounting for in our estimates of familiarisation costs to letting agents.

Regarding landlords that do not use letting agents, they will spend much less time familiarising themselves with the requirements of the Bill than letting agents. On average, landlords hold approximately two properties, though the majority of landlords hold only one dwelling, and a small number own a large number of dwellings. The familiarisation burden to landlords will involve:

- Reading guidance the department will publish fully outlining what the Bill does and does not permit.
- Considering their best response as a result, in terms of whether to charge higher rents as a result of the deposit cap and the letting fees ban, if they indeed charge a fee.
- Additional re-negotiation of around 2 tenancies which on average are likely to be renewed in a period of 12 months or less.

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[70] http://www.arla.co.uk/media/1045728/letting-the-market-down-assessing-the-economic-impacts-of-the-proposed-ban-on-letting-agents-fees.pdf
[71] http://www.arla.co.uk/lobbying/private-rented-sector-reports/december-2017/

Landlords are less dependent on tenant fees than letting agents but will still need to spend time understanding the implications for their business, and renegotiating contracts with tenants. Landlords will have significantly fewer tenancies to consider than agents (1-2 on average as opposed to 200). However, landlords are generally not as experienced as letting agents (most landlords are part time and use the property to supplement income) – consequently landlords may need to spend longer than letting agents in considering the implications of the Bill on a per tenancy basis.

Considering the above, we estimate that the familiarisation burden to landlords will amount to 2 hours (1 hour to read the guidance and 1 hour to consider any amendments to their tenancy agreements). This represents our best estimate and most sensible assumption but there is significant uncertainty around this estimate given the available data and evidence. Some landlords will spend less than 2 hours, and a small tail of professional landlords with very high levels of rental property ownership, such as small but full time investors and large scale investors such as those managing Build to Rent investments, are likely to spend considerably more than this. Due to the uncertainty around familiarisation time, we vary this figure by 50% in the sensitivity analysis.

To monetise the familiarisation cost, we multiply the number hours of hours needed for familiarisation by the median hourly salary for an estate agent as a proxy for landlords and letting agents taken from the 2017 Provisional Annual Survey of Hours and Earnings. When uplifted by a factor of 1.3 to allow for non-wage costs, we assume that the hourly cost of a landlord's and letting agent's time is £15.20.

*Familiarisation costs landlords = (Number of landlords * Hourly salary including uplift * No. of familiarisation hours *(1 – proportion of landlords using letting agents))* [72]

*Familiarisation costs to letting agents = (Number of letting agents * Hourly salary including uplift * No. of familiarisation hours)* [73]

Whilst there is uncertainty around the estimates of familiarisation costs, for context, the main effects of the bill that have been monetised form the vast majority of the EANDCB estimate. For example, the central estimate of familiarisation costs composes 1.3% of the total EANDCB estimate.

Enforcement costs

One trading standard body in England will be appointed as the lead enforcement body. Their remit will be to support local enforcement authorities in enforcing the ban and other relevant letting agent regulation. This is estimated to cost between £200k and £300k per annum based on the costs of similar bodies set up by other Government departments, such as the funding model for the National Trading Standards Estate Agency Team.

Local trading standards are already obliged to enforce rules governing transparency of fees, which in some cases is likely to be more burdensome than imposing a ban since it is easier for tenants to understand and enforce the fee ban. There is some overlap in enforcement with other regulatory measures. Letting agents will continue to be required by existing legislation to be transparent about their fees (e.g. their fees to landlords), their redress and Client Money Protection (CMP) provider, and these will continue to be enforced by local authorities. Similarly, local authorities are responsible for enforcing legislative requirements on landlords in the private rented sector. Enforcement of the Tenant Fees Bill provisions can be undertaken at the same time rather than necessitating additional compliance checks.

[72] 2.75m * £15.2 * 2 * (1-52%) = £39.8m

[73] 16,000 * £15.2 * 20 = £4.8m

There will however be additional costs, such as for cases where landlords or letting agents have not complied with the requirements of the Bill. This may involve cases where a letting agent or landlord continues to charge fees that are banned or where landlords or letting agents have taken deposits greater than permitted. The extent of these costs is not certain. They largely depend on the extent to which there is non-compliance with the requirements of the Bill. It is proposed that local authorities will be able to retain the money raised through civil penalties for future local housing enforcement. Therefore if levels of non-compliance are higher, the money generated for enforcement would be greater. We thus expect the costs to be fiscally neutral to local authorities.

We expect the additional burden on authorities to enforce on letting agents to be small, given there is significant crossover with existing requirements, and we expect the impact on landlords to be small, as evidence to the tenant fees consultation suggests landlords charge a much lower level of fee where they even charge one – the average fee was reported as £26, compared to £200-£300 for letting agents. Our central estimate is that 52% of landlords use letting agents, and of the 48% that don't, 50% charge fees (an estimate of 680,000 landlords in 2019). We therefore expect some, but low levels of non-compliance of requirements of the Bill.

In the central scenario, we assume on-going annual costs to Government of £200,000 per annum as a result of enforcement costs for a small number of issued civil penalties being appealed and thus cases progressing to court, as well as £250,000 for the lead enforcement agency. We assume additional enforcement costs of £300,000 to local authorities in Year 1, plus £200,000 in setup costs for the court system. These setup costs for local authorities may include training to local authority employees, and producing guidance for tenants, letting agents and landlords. From Year 2 onwards, we expect the cost to local authorities to be fiscally neutral as they can retain revenues from civil penalties issued. We vary all these estimates by 50% in the upper and lower scenarios.

The potential costs to local authorities need to be considered in the context of existing enforcement responsibilities held by local authorities. In addition, the enforcement costs of future overlapping requirements such as those on letting agents to belong to a Client Money Protection scheme when handling client money, need to be considered in parallel with this Bill to inform the total cost that will result to local authorities from a range of new measures.

6. Rationale and evidence that justify the level of analysis used in the IA (proportionality approach)

The impact of the policy is monetised using data from reputable sources such as the English Housing Survey, the Annual Survey of Housing and Earnings. Information from responses to the Government's consultation has also been considered, as well as information from existing studies, such as the Capital Economics study commissioned by ARLA Propertymark for estimates of pass through. These have informed assumptions that have needed to be made as part of the analysis.

Where assumptions have been made, these have been stated, and low, central, and high scenarios have been considered.

7. Direct costs and benefits to business calculations (following BIT methodology)

The cost benefit explanation can be found in section 5, including a list of which costs and benefits have been monetised as part of the analysis. The Equivalent Annual Net Direct Cost to Business (EANDCB) includes both landlords and letting agents who have been classified as businesses. As has been discussed, the EANDCB does not include any estimates of pass through, it is purely based on the loss of revenue from tenant fees to landlords and letting agents, and the cost to landlords from the deposit cap. All other NPV calculations include estimates of pass through.

The benefits and costs to tenants are not presented in the EANDCB as they are not a business, but do appear in the total estimates of Net Present Value (NPV).

Costs and benefits are estimated over a 10 year period, following Green Book guidelines and using the government's Impact Assessment calculator.

8. Wider impacts

Small and micro-business assessment

We are not proposing to exempt small and micro businesses as it would undermine the objective of the policy. The 2010 Private Landlord's Survey indicates that 74% of all private sector landlords own one property and 95% own between one and four properties.[74] A small or micro sized business is normally defined based on the level of turnover of their number of employees. Whilst we do not have data to reliably make these estimates of the turnover and employment of landlords, it is highly likely that landlords would be classified as a small or a micro business – we expect most of these landlords are unlikely to employee anybody but either appoint a letting agent, or manage their properties themselves. Similarly, for letting agents, the Capital Economics analysis indicates 60% of the market is comprised of small businesses, though this is based on a definition of a small agent being one with three or fewer branches and not based on the standard definitions of turnover and employment.[75]

Owing to the fact that the majority of letting agents and landlords are small businesses, the impact assessment presented therefore is in most part an assessment on these small businesses. Assuming that 60% of letting agents are small businesses, as are 95% of landlords, then we estimate approximately £186m of the estimated £259m 10 year discounted average annual benefit to tenants would be lost, before considering the wider impacts that exempting small businesses would have. Exempting these businesses would result in a large loss of benefit to tenants. It would also reduce the intended increase in competition in the private rented sector.

Exempting these small businesses from the Bill may also lead to some perverse outcomes for the market, particularly to the determinant of these businesses. There may be a disincentive to businesses in becoming successful and innovating their business models. Or, if small landlords and letting agents were exempt from charging tenant fees, tenants may be more likely to seek a potential property from larger letting agents thus negatively impacting small business. In turn, the effects of competition may drive smaller businesses to reduce or remove any fees, which would result in the same pass throughs (e.g. letting agents charging landlords higher fees) as described throughout the analysis.

In addition, exempting these businesses would result in the policy only affecting a small proportion of the private rented sector, which would hinder the policy's objective of introducing transparency and improving affordability for tenants and have potentially

[74] Private landlords survey, 2010 https://www.gov.uk/government/statistics/private-landlords-survey-2010
[75] In a sample of eight locations, the share of small firms ranged from 50 to 76%.

distortive measures. It would be very difficult for tenants to understand whether an agent qualified as a small or micro business and able to charge fees. The intended transparency and increased affordability from the cap on deposits would also be hindered.

Tenant led enforcement of the ban is important in order to support effective delivery of the policy and this would be undermined. It may also cause confusion to businesses on whether they are eligible to charge fees or otherwise, creating an additional burden and familiarisation cost. There would be additional costs to local authorities who will enforce the requirements of the Bill, as enforcement would become more complex. They would need to collect and verify information on the size of the business they are enforcing against to understand whether the business is exempt from the tenant fees ban or otherwise. It would also lead to unfair outcomes where some tenants are charged fees and others aren't.

We intend to provide guidance for landlords and agents to support them in understanding the ban and how it applies. This approach of including small and micro-businesses is consistent with other legislation agents in the Private Rented Sector, for example, Part II of the Housing and Planning Act 2016.

9. Wider Review of the Policy

The implications of the policy are already anticipated by much of the industry and landlords. There has been strong engagement through public consultation, pre-legislative scrutiny and participation in stakeholder events. MHCLG officials have been engaging with letting agents and their representative bodies since the policy was announced at Autumn Statement 2016 and the implications of the policy have been well debated. Feedback from this extensive stakeholder engagement is that agents have already started to make arrangements for the fee ban.

We do not intend to review the Tenant Fees Bill in isolation. There have recently been a number of legislative changes in the lettings industry, with more planned. It would not be helpful or informative to review the impact of the Tenant Fees Bill without wider consideration of the other changes affecting the private rented sector. These changes include the 3% increase in Stamp Duty on second homes (implemented in April 2016), the removal of mortgage interest relief for landlords (phased implementation from April 2017-April 2020) as well as the forthcoming proposals to regulate letting agents, to require agents to join a client money protection scheme and to require landlords to join a redress scheme.

The cumulative impact of these changes is to rebalance the relationship between tenants and landlords and to make renting fairer. The commitment to regulate letting agents has been well received by the industry on the understanding that the risk of reputable agents being undercut by non-compliant agents is reduced. Landlords and their representative bodies have raised concerns about the impact of taxation reform on private landlords.

Given the number of recent, and planned, policy changes in the private rented sector, we will monitor trends across the industry as a whole, utilising a range of data sources. These include VOA rental prices data, the ONS rental price index, and data from the English Housing Survey. The Private Landlord Survey 2018 is currently underway, with findings due to be reported at the end of Summer 2018. This will provide a useful baseline. However, it will not be possible to detect with any level of robustness any change in rental level or landlord behaviour that are attributable solely to the Tenant Fees Bill. For example, any changes in rental price growth could be due to a wide range of factors in the economy.

We plan to monitor the implications of the Tenant Fees Bill for any adverse impacts through continued engagement with key stakeholder groups representing landlords, agents and tenants as well as wider intelligence from agencies such as the Lead Enforcement Authority and trading standards who will enforce the requirements of the Bill. We expect minimal impact on landlords, given they charge much lower fees as evidenced in responses to the consultation than letting agents. Even with higher levels of pass through, the cost implications on individual landlords are likely to be small. For letting agents, as the ban on letting fees targets profits that would not be earned in an effective and competitive market, we do not anticipate significant adverse effects on letting agents.

10. Annex

Total discounted costs and benefits over the 10 year appraisal period (£ m), excluding familiarisation costs

Central scenario

	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10
Landlord costs	82.9	84.1	85.3	87.7	88.9	90.2	91.6	92.9	94.2	95.6
Letting agent costs	157.1	159.3	161.8	164.	166.3	168.8	171.4	173.7	176.2	178.9
Tenant benefits	241.3	244.8	248.5	253.1	256.7	260.5	264.5	268.1	271.9	276.1
Enforcement costs	1.	.4	.4	.4	.4	.4	.4	.4	.3	.3

Upper scenario

	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10
Landlord costs	117.4	120.2	123.2	127.6	130.6	133.8	137.2	140.4	143.7	147.3
Letting agent costs	273.9	280.5	287.4	294.3	301.2	308.6	316.3	323.7	331.4	339.7
Tenant benefits	392.7	402.1	412.1	423.3	433.3	444.	455.	465.7	476.7	488.6
Enforcement costs	1.4	.7	.6	.6	.6	.6	.5	.5	.5	.5

Lower scenario

	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10
Landlord costs	46.2	45.8	45.4	45.7	45.2	44.8	44.4	44.	43.5	43.1
Letting agent costs	76.8	76.	75.3	74.6	73.8	73.1	72.5	71.7	71.	70.4
Tenant benefits	124.3	123.1	122.	121.5	120.3	119.2	118.1	116.9	115.7	114.7
Enforcement costs	.5	.2	.2	.2	.2	.2	.2	.2	.2	.2

Key assumptions used in analysis

	Central	Upper	Lower
PRS Growth Rate	5%	6%	2.50%
Proportion of landlords that use agents	51.5%	63%	40%

Number of agents	16000	16000	16000
Number of landlords	2,715,828	2,794,164	2,526,422
Letting agent tenancy fee	223	279	167
Letting agent renewal fee	72	75	68
Landlord tenancy fee	26	50	1
Pass through - letting agents to landlords from tenant fees	50%	40%	60%
Pass through - landlords to tenants from tenant fees	50%	40%	60%
Estimated % of deposits that will result in landlord losing money	1.4%	1.7%	1.0%