New homes bonus

Consultation

www.communities.gov.uk

New homes bonus

Consultation

November 2010
Department for Communities and Local Government

Department for Communities and Local Government
Eland House
Bressenden Place
London
SW1E 5DU
Telephone: 030 3444 0000
Website: www.communities.gov.uk

If you require this publication in an alternative format please email alternativeformats@communities.gsi.gov.uk

DCLG Publications
Tel: 030 0123 1124
Fax: 030 0123 1125

Email: product@communities.gsi.gov.uk
Online via the website: www.communities.gov.uk

November 2010

ISBN: 978 1 4098 2612 5

Ministerial foreword

We all knew last month's Spending Review settlement was going to be tough, but not reducing the public deficit would be tougher. It would put the country's economic recovery at risk. The Government had to take hard decisions to address the level of debt that was in danger of crippling the UK and we took them. If we didn't tackle the deficit, interest rates would rise, making housing less affordable. The interest repayments on £1 trillion of public debt would also suck money away from frontline services and future investment. We could not go on like that.

We also inherited a catastrophic decline in home building from the previous Government. A combination of divisive top-down targets and a public subsidy-driven approach delivered just 118,000 completions in 2009, the lowest level of house building in England and Wales in peace-time since 1923-24. We need to take urgent action to ensure that we build more of the homes that people want in the places they want to live. We need a fundamentally different approach.

The current system does not provide the right incentive for councils or communities to welcome new homes. If a local authority enables the building of new homes, little benefit is seen by the local community. Existing residents only see further strain on public services. They see increased competition for scarce resources from the people who move into the new homes. They and their elected local councillors, therefore quite naturally object to much of the proposed development.

Rewarding rather than penalising councils and communities for new homes is not only fairer, but will be far more effective than the failed top-down regional targets which served only to antagonise. It will help local politicians to lead a mature debate about the benefits of development, not just the costs. Incentives will be a powerful driver. Communities could see reductions in council tax, or a redeveloped town centre or a new community centre in return for accepting new homes.

Nor does the current system incentivise local authorities to bring empty homes back into use. This consultation asks whether bringing long-term empty homes back into use should be counted as additional supply for the New Homes Bonus. Local authorities would then be able to consider these properties with equal weight alongside new build.

The New Homes Bonus will return the ownership of this debate to a local level and encourage local authorities and communities to develop their housing plans in ways that meet their needs and concerns. I am committed to ensuring that rewards start to flow in the next financial year to those authorities going for growth. We need your ideas to make sure the New Homes Bonus delivers the homes your communities need. I look forward to reading your responses to the questions set out in this consultation.

Thank you

The Rt Hon Grant Shapps MP

Minister for Housing and Local Government

Contents

Section 1: Scope of the consultation

Scope of the consultation

Topic of this consultation:	This consultation seeks views on the implementation of the 'New Homes Bonus' - which will provide a powerful, simple, transparent and permanent means of incentivising local authorities to increase their housing supply. This follows the commitment in the Coalition Agreement: *to provide incentives for local authorities to deliver sustainable development, including for new homes and businesses.*
Scope of this consultation:	This consultation sets out the details of the scheme and the rationale for the proposed mechanisms. It also sets out how the scheme sits within the wider context of the Government's locally-driven growth strategy. This is largely a technical consultation for local authorities. In the current financial circumstances, it is important that the final scheme is announced alongside the local government finance settlement early in the new year so that local authorities have clarity when they set their budgets and council tax in March. As a result this is a **six week consultation**. We would like to invite views from interested parties on some key design features.
Geographical scope:	This consultation is applicable to England only.
Impact Assessment:	A consultation stage impact assessment has been completed for this consultation and can be found at Appendix E. In line with guidance issued by the Government Equalities Office (GEO), we have had regard to equalities issues as the proposed New Homes Bonus has been designed. However, we consider it good practice to consult as widely as possible on these issues and as part of this consultation we are asking respondents to consider whether the proposed scheme design is likely to have any equalities impacts.

Basic information

To:	Local authorities Housing and Trade Bodies
Body/bodies responsible for the consultation:	The Department for Communities and Local Government Housing Supply Division Incentives Team
Duration:	The consultation will commence on 12 November and end on 24 December 2010 and is published online at http://www.communities.gov.uk/housing/housingsupply/newhomesbonus
Enquiries:	newhomesbonus@communities.gsi.gov.uk Junaid Azam New Homes Bonus Consultation 1/A6 Incentives Team Housing Supply Division Department for Communities and Local Government Eland House Bressenden Place London SW1E 5DU Tel: 030344 43598
How to respond:	See Section 5.4 Please send responses electronically to: newhomesbonus@communities.gsi.gov.uk (with attachments in MS Word only) Hard copy responses can be sent to: New Homes Bonus Consultation 1/A6 Incentives Team Housing Supply Division Department for Communities and Local Government Eland House Bressenden Place London SW1E 5DU

Additional ways to become involved:	As this is largely a technical consultation this will be a written exercise. Should you require a copy of the document in an alternative format then please contact newhomesbonus@communities.gsi.gov.uk to make a request.
After the consultation:	Following the consultation we will review the responses received and announce the final design of the scheme early in 2011.
Compliance with the Code of Practice on Consultation:	This consultation document and consultation process have been planned to adhere to the Code of Practice on Consultation issued by the Department for Business Innovation and Skills and is in line with the seven consultation criteria, which are: 1. Formal consultation should take place at a stage when there is scope to influence the policy outcome. 2. Consultations should normally last for at least 12 weeks with consideration given to longer timescales where feasible and sensible. 3. Consultation documents should be clear about the consultation process, what is being proposed, the scope to influence and the expected costs and benefits of the proposals. 4. Consultation exercises should be designed to be accessible to, and clearly targeted at, those people the exercise is intended to reach. 5. Keeping the burden of consultation to a minimum is essential if consultations are to be effective and if consultees' buy-in to the process is to be obtained. 6. Consultation responses should be analysed carefully and clear feedback should be provided to participants following the consultation. 7. Officials running consultations should seek guidance in how to run an effective consultation exercise and share what they have learned from the experience. Representative groups are asked to give a summary of the people and organisations they represent, and where relevant who else they have consulted in reaching their conclusions when they respond. Information provided in response to this consultation, including personal information, may be published or disclosed in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act

	1998 (DPA) and the Environmental Information Regulations 2004). If you want the information that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals, amongst other things, with obligations of confidence. In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on the department. The Department for Communities and Local Government will process your personal data in accordance with DPA and in the majority of circumstances this will mean that your personal data will not be disclosed to third parties. Individual responses will not be acknowledged unless specifically requested. Your opinions are valuable to us. Thank you for taking the time to read this document and respond. Are you satisfied that this consultation has followed these criteria? If not or you have any other observations about how we can improve the process please contact: DCLG Consultation Co-ordinator Department for Communities and Local Government Zone 6/H10 Eland House Bressenden Place London SW1E 5DU or by e-mail to: consultationcoordinator@communities.gsi.gov.uk

Background

Getting to this stage:	There has been a long-term pressure on housing supply, which top-down targets failed to resolve. Supply has now fallen to an historic low. 2009 saw the lowest level of housebuilding in peace-time since 1923-24. However, the long-term demand for housing is strong. The latest published household projections show that around 252,000 new households could form each year between now and 2031 (as a result of increased longevity, migration and a rise in the number of one-person households), 134,000 above current build levels. The previous Government tried to remedy this by using centrally determined, top-down housing targets which were imposed on local authorities and local communities. These failed to deliver the housing this country needs. A series of independent reviews – most recently by Sir Michael Lyons, Kate Barker and Professor Michael Ball – highlighted the powerful role that local incentives could play in driving housing delivery. International comparisons also show the role enhanced local fiscal incentives can have in supporting development (see for example, Evans and Hartwich (2006) for Policy Exchange). However, in the UK the state has become more centralised over time. For example, local government grants from the centre increased from 34 per cent in 1950 to 61 per cent in 2008[1]. Recognising that a new approach was required, the Coalition Agreement set out *to provide incentives for local authorities to deliver sustainable development, including for new homes and businesses*. The proposed scheme will provide this incentive by returning the benefits of growth back to communities.

[1] Layfield, *Local Government Finance: Report of the Committee of Enquiry*, 1976, 1949/50 and 1973/74 data: *Local Government Finance: Report of the Committee of Enquiry*, F. Layfield, 1976, 2007/08 data: Department for Communities and Local Government, *Local Government Finance Statistics (England No 19)*, 2009

Previous engagement:	The Department for Communities and Local Government has carried out a range of activities with private and public sector partners over the summer of 2010 to develop the scheme design options. Two joint Department for Communities and Local Government/Local Government Association workshops were held with a number of local authorities to work through the mechanics of the scheme. In addition the Department has held a number of bilateral meetings with key partners in the housing industry such as British Property Federation, Home Builders Federation, National Housing Federation, Shelter, Campaign to Protect Rural England and a number of academics to share the emerging scheme design issues and consider their views. An email address for enquiries, issues of concern and any suggestions was also introduced over the summer. All emails are logged and will be used to inform the scheme design. newhomesbonus@communities.gsi.gov.uk

2. Introduction

Aim

2.1. The aim of the New Homes Bonus is to create a powerful, simple, transparent and permanent incentive which rewards local authorities that deliver sustainable housing development.

Background

2.2. The Coalition Agreement set out the Government's commitment to provide incentives for local authorities to deliver sustainable development, including for new homes and businesses. At the heart of the Government's strategy for locally-driven growth is a framework of powerful incentives. This will involve changes to the local government finance system to reward those authorities that go for growth. This framework will encourage local authorities and communities to increase their ambitions for housing and economic growth by returning the benefits of this growth and allowing them to take the lead in managing the way in which villages, towns and cities develop.

2.3. The current local government finance system does not provide the right incentive or rewards for councils to build new homes or bring long-term empty properties back into use. If a local authority promotes the building of homes in the area it governs, little of the economic gain is captured by the local community. As a result existing residents can only see a further strain on public services and reduced amenities when new homes are built. They and their elected representatives on local councils therefore quite naturally object to much of the proposed development. We have seen a sustained fall in housing development, on average 26,000 fewer homes were built each year from 1997 to 2009 than under the previous Conservative government. In 2009, we achieved just 118,000 completions, that's the lowest level of house building in peacetime since 1924.

2.4. The previous Government tried – and failed – to remedy this by imposing development through top-down targets. The Housing and Planning Delivery Grant (HPDG) was introduced to improve housing delivery but this was ineffective and complicated, and local authorities could not rely on it as a sufficient and stable incentive. Changing this and rewarding rather than penalising councils for new homes is not only fairer, but will be far more effective than the failed top-down regional targets.

2.5. The impact assessment sets out a strong evidence base for action. A series of independent reviews – most recently by Sir Michael Lyons, Kate Barker and Professor Michael Ball – have highlighted the powerful role that incentives could play in driving housing delivery. International comparisons and experience with growth funding show the practical impact financial rewards can have.

2.6. Government will not tell local authorities what type of development or homes they should build or where, but we will reward authorities and communities where growth takes place. The scheme will return power back to local communities and allow them to decide where and how housing development occurs in their area whilst ensuring that the benefits of growth are returned to those communities.

2.7. The Local Growth white paper, published on 28 October 2010, sets out the Government's new approach to rebalancing the economy and driving sustainable growth by focusing on three key themes:

- **Shifting power to local communities and businesses** - by establishing dynamic local enterprise partnerships of local business and civic leaders.
- **Focused investment** – by tackling barriers to growth through the £1.4bn Regional Growth Fund to encourage private sector enterprise, create sustainable private sector jobs and to help places currently reliant upon the public sector.
- **Increasing confidence to invest** – by creating the right conditions for growth through a consistent and efficient framework for investment, an effective planning framework and new incentives to make sure local communities benefit from development.

2.8. The New Homes Bonus is a key part of a wider family of incentives set out in the Local Growth white paper. In particular, we have considered ways of enabling councils to retain locally raised business rates. This will be considered within the Local Government Resource Review which will be launched in January 2011 after a period of consultation on the proposals in the white paper on Local Growth. The Government is committed to protecting business rates payers. Businesses should not be subjected to locally imposed tax increases that they do not support.

2.9. Since the publication of the Local Growth white paper, the Government has announced that it will retain and reform the existing Community Infrastructure Levy to improve its incentive effect and give more control over its use to local communities.

2.10. Alongside the reforms outlined in the white paper, the New Homes Bonus plays a key role in this new approach. The scheme will help local authorities and their partners realise their growth ambitions and ensure that local communities can see the benefits, as well as the costs, of economic growth in their area.

3. Scheme design

3.1. A range of options have been explored for implementing the scheme and the following section sets out the Government's preferred model with the rationale for each design feature. Appendix B sets out the scheme payment model and Appendix C provides a worked example.

Summary

3.2. The scheme will incentivise local authorities to increase housing supply by rewarding them with a New Homes Bonus, equal to the national average for the council tax band on each additional property and paid for the following six years as an unringfenced grant. There will be an enhancement for affordable homes.

The New Homes Bonus is designed to create an effective fiscal incentive to encourage local authorities to facilitate housing growth. In particular we have designed the scheme in line with the following key principles:

- *Powerful* - the grant will be payable for the following six years, so the total will rise for at least the first six years. The diagram below shows how the profile will rise as the grant rolls forward. By year six, even at a steady rate of build, we expect it to be over £1bn. In fact, we expect building rates to increase and the grant to be significantly higher by year six. DCLG has set aside nearly £200m to fully fund the scheme in 2011-12. For the following three years of the spending review (2012-13 to 2014-15) we have set aside £250m per annum and funding beyond these levels will come from Formula Grant. Those authorities which respond to the incentive and drive growth will reap the benefits.

	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18
Year 1	£	£	£	£	£	£	
Year 2		£	£	£	£	£	£
Year 3			£	£	£	£	£
Year 4				£	£	£	£
Year 5					£	£	£
Year 6						£	£
Year 7							£

- *Simple* - additional homes will be rewarded with six years of grant based on the council tax, returning the economic benefits of growth to the local community.

- *Transparent* - easy for councillors, the community and developers to calculate and see the early benefits of growth. The Government is publishing an online calculator[2] alongside this consultation so that communities can see how much they can gain from the scheme.

- *Predictable* - the scheme is intended to be a permanent feature of local government funding and will therefore continue beyond the six year cycle. We will keep the design features simple and stable to ensure that expected rewards for growth are delivered.

- *Flexible* - local authorities can decide how to spend the funding in line with local community wishes. The Government expects local councillors to work closely with their communities – and in particular the neighbourhoods most affected by growth – to understand their priorities for investment and to communicate how the money will be spent and the benefits it will bring. This may relate specifically to the new development or more widely to the local community. For example, they may wish to offer council tax discounts to local residents, support frontline services like bin collections, or improve local facilities like playgrounds and parks. This will enable local councillors to lead a more mature debate with local people about the benefits of growth, not just the costs. The Bonus will be paid through section 31 of the Local Government Act 2003 as an unringfenced grant.

3.3. We have identified a list of issues which we would like to consult on. Broadly, these relate to:

- How we should reward local authorities for the additional properties made available in their community for the following six years.
- The level of the enhancement for affordable homes and how we should define an affordable home.
- Whether we should reward local authorities for bringing empty properties back into use.
- Whether, in two tier areas outside London, allocating 80 per cent of the New Homes Bonus to the lower tier and 20 per cent to the upper tier authority is an appropriate split. If not, what would the appropriate split be, and why?
- Whether the proposed methods of data collection to track increases to the housing stock are appropriate.
- We would also welcome your wider views on the proposed New Homes Bonus, particularly where there are issues that have not been addressed in the proposed model.

[2] http://www.communities.gov.uk/housing/housingsupply/newhomesbonus

Unit of reward

3.4. The previous Government's policies did not meet Britain's housing needs. The top-down targets that were set were not reached and often led to undesirable outcomes. For example, local authorities were encouraged to focus on high density developments of at least 30 dwellings per hectare. One consequence of this was fewer houses were built - the proportion of flats built increased considerably from 15 per cent in 1997-98 to 45 per cent in 2009-10 - but this did not necessarily reflect the types of homes the local community needed or wanted. This left demand for larger family homes unmet.

3.5. We want to return the economic benefits of growth to the local community. We have therefore designed the New Homes Bonus around the council tax revenues generated from housing development.

3.6. We propose to link the level of grant for each additional dwelling to the national average of the council tax band for the following six years to incentivise local authorities to build the types of homes people want and need, in the places that people want them.

3.7. We propose to do this by measuring the change in dwellings on council tax valuation lists as set out in Section 4. This approach recognises:

- increases in housing stock
- the relative value of the properties – larger family homes require more land and that homes built in areas of highest need are more expensive and tend to be in a higher council tax band and
- that local council tax levels have a variety of historic and local reasons and we do not want to penalise authorities which have been prudent

3.8. Currently this would mean that the amount of grant relating to an additional council tax band D property would be about £1,439 per annum or £8,634 over six years, where as the grant relating to an additional band E property would be about £1,759 per annum or £10,553 over six years. This would be reviewed if council taxes rise.

3.9. The full calculation is set out fully in Section 4 and exemplified in Appendix C.

Consultation question 1

Do you agree with our proposal to link the level of grant for each additional dwelling to the national average of the council tax band?

Affordable housing enhancement

3.10. It is crucial that there is a good balance of market and affordable housing. We want to reward local authorities that provide the right balance of housing to meet the needs of local people. Particularly in bringing forward land for development, granting planning permissions and negotiating section 106 agreements. This will support the commitment made in the Spending Review of almost £4.5bn over a four year period to support affordable housing.

3.11. To ensure that affordable homes are sufficiently prioritised within supply, we propose a simple and transparent enhancement of a flat rate £350 per annum for each additional affordable home. This is about 25 per cent of the current average Band D council tax and would be reviewed if council tax rises. Over six years an affordable home would receive an enhancement of £2,100. A flat rate also means we can use existing data sources to calculate the reward. (See Section 4).

Consultation question 2

The Government proposes an affordable homes enhancement of £350 for each of the six years - what do you think the enhancement should be?

Affordable housing definition

3.12. The Government considers that the housing market should offer a range of affordable housing options that meet people's varying needs. There are low cost homeownership products that offer housing at less than market cost, for example shared ownership, which allow households who would otherwise have been excluded from the market to purchase a home. These products allow purchasers to get a first step up on the property ladder with the later ability to 'staircase up' and own a larger share later.

3.13. Affordable housing will include the new 'affordable rent' homes which will be offered to new tenants at a level between social rents and local market rents and on a tenancy agreement that will be reviewed after an agreed period of time. Local authorities will be able to nominate prospective tenants to these properties in the same way as they do now. We will publish more details shortly. Affordable rent homes will be eligible for the same bonus as other affordable homes.

3.14. Traveller sites in public ownership also contribute to the supply of affordable homes. Provision of public Gypsy and Traveller caravan sites is now included in the Homes and Communities Agency's affordable housing programme. In agreeing Local Investment Planning with local authorities, the Homes and Communities Agency will seek to ensure that provision of appropriate sites forms part of the overall package of housing and regeneration in the area.

3.15. We propose to define affordable homes using Appendix B of Planning Policy Statement 3 (PPS3) and also include pitches on Gypsy and Traveller sites owned and managed by local authorities or registered social landlords. Appendix A of this consultation document sets out the types of housing which would be eligible for the enhanced rate.

Consultation question 3

Do you agree with the proposal to use PPS3 and also include pitches on Gypsy and Traveller sites owned and managed by local authorities or registered social landlords to define affordable homes?

Empty homes

3.16. The Coalition Agreement set out the Government's commitment to explore a range of measures to bring empty properties back into use.

3.17. There are a number of reasons why properties become and remain empty including low demand, the cost of repairs, reluctance to rent, or personal circumstances. Around 300,000 privately owned homes have been vacant for over six months and many are in areas of high demand. Empty homes are a blight on local communities and a waste which we cannot afford. We need to harness this potential to meet pressing housing need.

3.18. The Spending Review announced that the Government is investing £100m - through the Homes and Communities Agency - to support housing associations to refurbish over 3,000 empty properties and manage them at an affordable rent for up to 10 years.

3.19. Many local authorities already work with property owners to bring homes back into use. Some also take enforcement action where advice and support fails. Through the New Homes Bonus, the Government proposes to strengthen the incentive for local authorities to identify empty properties and work with property owners to find innovative solutions that allow these properties to be brought back into use.

3.20. Bringing empty homes back into use is also important in overcoming some local opposition to new housing. **We therefore propose to reward local authorities for bringing empty properties back into use through the New Homes Bonus.**

Consultation question 4

Do you agree with the proposal to reward local authorities for bringing empty properties back into use through the New Homes Bonus?

Are there any practical constraints?

New Homes Bonus allocation

TIER SPLIT

3.21. For the incentive to be most powerful, it must be strongest where the planning decision sits – the lower tier in two tier areas. However, in two tier areas outside London, we recognise the role of the upper tier in the provision of services and infrastructure and the contribution they make to strategic planning.

3.22. We propose to split the payment of the New Homes Bonus between tiers outside London: 80 per cent to the lower tier and 20 per cent to the upper tier, as a starting point for local negotiation. In London 100 per cent will go to the London borough.

Consultation question 5

Outside London: Do you agree with the proposal to split the payment of the New Homes Bonus between tiers: 80 per cent to the lower tier and 20 per cent to the upper tier, as a starting point for local negotiation?

If not, what would the appropriate split be, and why?

LOCAL FLEXIBILITY

3.23. The proposed tier-splits are a starting point for local debate. Every development is different and will need different services to support it. Local authorities are best placed to negotiate these to meet the needs of local neighbourhoods and communities. In many cases this will involve advanced planning with other local service providers to ensure that there is timely delivery of infrastructure for the new development. For example, local authorities can pool funding by allocating more to the upper tier to deliver infrastructure. In National Park areas, the local authority may negotiate funding with the national park authority.

3.24. Local Enterprise Partnerships can support the delivery of new housing through infrastructure planning and providing the best business environment for growth. Pooling some New Homes Bonus at the level of the Local Enterprise Partnership could have many benefits, such as ensuring that the money is reinvested into shared priorities which support long-term prosperity for the area, increased efficiency and reduced transaction costs by managing the money collectively, greater transparency and increased potential for alignment with other partner sources of funding (e.g. Regional Growth Fund and European Structural Funds).

4. Basis of calculation

Grant calculation

4.1. The basis on which grant to individual authorities is calculated must be fair and equitable and support the objective of the scheme – to increase housing supply. We want to collect data in a way which is simple and minimises additional burdens on local authorities and others, but is robust and sufficiently timely.

4.2. Our preferred option is the Council Tax Base form[3], which has the advantage of bringing together data on additions, demolitions and empty homes in one place and it is already used to calculate formula grant. Collection of affordable homes data is considered separately below.

4.3. We would calculate the grant for a billing authority's area and a financial year ('the relevant year') as follows:

- The base position for the preceding financial year would be established using the following lines in the Council Tax Base form submitted by the authority for the preceding year:

Dwellings on the valuation list (Line 1) – adjustment for recent demolitions and out of area dwellings (Line 3) – Long term empty homes (Lines 12, 14 & 15)

- The position for the relevant year would be established in the same way, but using the Council Tax Base form for that year.

- Both these calculations would be converted to Band D equivalents using the standard table below.

	Ratio to Band D
Band A	6/9
Band B	7/9
Band C	8/9
Band D	1
Band E	11/9
Band F	13/9
Band G	15/9
Band H	2

- We would then calculate the annual change from the preceding financial year ('the relevant figure') using the Band D equivalent calculations.

[3]http://www.communities.gov.uk/localgovernment/localregional/localgovernmentfinance/statistics/usefulinformation/formstimetable/otherforms

- The grant for the authority's area would be calculated by multiplying the relevant figure by the average Band D council tax in England for the previous year.

- The grant would be payable for the relevant year and the five financial years following that year (that is, for a total of six financial years).

- This process would be repeated each financial year with each new amount of grant being added to the amount of grant payable in the preceding financial year. The total would not be less than zero.

- From the seventh year of the scheme onwards the grant calculated six years earlier will no longer be included in the total grant payable (and so in the seventh year the amount calculated for the first year will not longer be paid, in the eighth year the amount calculated for the second year will no longer be paid and so on). See table at Appendix D.

Consultation question 6

Do you agree with the proposal to use the data collected on the Council Tax Base form as at October to track net additions and empty homes?

Timing of grant allocation and payments

4.4. The grant has been designed to be stable and predictable. To maximise this we propose to pay the New Homes Bonus alongside the local government finance timetable, as set out in Appendix D. This means that provisional allocations would be announced in early December and final allocations in early February. This would allow local authorities to include the grant in their budget setting process in February. In Year One we would issue allocations as soon as possible after the consultation.

4.5. Grant for houses built between successive Octobers would be paid from the following April. Using this approach means that there is a potential time lag for payment of the grant. The diagram in Appendix D exemplifies Year Two, where grant for houses built between October 2010 and October 2011 would be paid the following financial year - between April 2012 and March 2013.

4.6. We are seeking views on whether this time lag between completions and payment of the grant could and should be reduced. For instance data could be collected on additions only, at a mid-point in April and an additional payment made as soon as reasonably possible. The fuller October data set would correct for demolitions and empty homes. This would increase the timeliness of the data, but would increase the burden on local authorities and mean the annual grant would be harder to predict when budgets were set in the previous February, possibly reducing transparency.

Consultation question 7

Do you agree with the proposal for one annual allocation based on the previous year's Council Tax Base form, paid the following April?

Consultation question 8

Do you agree that allocations should be announced alongside the local government finance timetable?

Affordable homes

4.7. We have considered how to include data on affordable homes in the scheme design, in a way which is proportionate – minimising administration burdens on central and local government, while ensuring that the data is consistent and accurate.

4.8. Currently, the best source of data on affordable homes defined by Planning Policy Statement 3 and including Traveller Sites is considered to be the Department for Communities and Local Government official statistics on gross additional affordable housing supply[4]. This includes data from a range of sources including the Homes and Communities Agency Investment Management System and other Homes and Communities Agency monitoring systems, and returns made by local authorities to DCLG through the Housing Strategy Statistical Appendix, the P2 quarterly house building return and the P1B quarterly social housing sales returns. The data is collected for financial years and published in the following October. It includes newly built affordable homes and acquisitions to the affordable stock.

4.9. We propose to use the Department for Communities and Local Government official statistics on gross additional affordable housing supply to calculate the affordable homes enhancement. Local authorities would receive an additional £350 for the following six years for all additional affordable homes reported in this statistical release. Similar to paragraph 4.3, this process would be repeated each financial year with each new amount of grant being added to the amount of grant payable in the preceding financial year. From the seventh year of the

[4] http://www.communities.gov.uk/housing/housingresearch/housingstatistics/housingstatisticsby/affordablehousingsupply/

scheme onwards the grant calculated six years earlier will no longer be included in the total grant payable.

4.10. These statistics measure additional affordable supply on a gross basis. They do not deduct demolitions or other losses to stock. We would welcome views on how significant this is and whether demolitions by local authority, including demolitions by Registered Providers, could be collected.

4.11. The statistics also measure acquisitions. Acquisitions increase the availability of affordable homes and so would receive the £350 enhancement. They would not receive the council tax element as they are not new supply and would not be included in the data set from the valuation list.

4.12. These statistics run from April to April and the Council Tax Base data from October- October. This means there will in some cases be up to a further six month delay for the affordable homes enhancement. Data from April 2010 – April 2011 on affordable homes will not be available October 2011. We will be considering when the first affordable homes enhancement payments should be made.

4.13. We propose to involve local authorities in ensuring that the data set is robust and would welcome comments on how this could be achieved.

Consultation question 9

Do you agree with the proposal to reward local authorities for affordable homes using data reported through the official statistics on gross additional affordable supply?

Consultation question 10

How significant are demolitions?
Is there a proportionate method of collecting demolitions data at local authority level?

5. Additional issues

Equalities

5.1. In line with guidance issued jointly by the Government Equalities Office (GEO) and the Department for Communities and Local Government[5], we have had regard to equalities issues as the proposed New Homes Bonus has been designed. In particular, discussions have been held with interested parties to allow them to comment on any equalities issues they see arising from the scheme design and no equality issues (intended or unintended) have been identified to this point.

5.2. However, we consider it good practice to consult as widely as possible on these issues and as part of this consultation we are asking respondents to consider whether the proposed scheme design is likely to have any equalities impacts. We will take any representations into account in deciding how to proceed with the New Homes Bonus.

5.3. The Department's view is that the proposed New Homes Bonus is fair; in particular, all relevant local authorities are able to access the scheme funds. The New Homes Bonus grant will not be ringfenced and so authorities will have the power to spend the grant as they see fit and they will be subject to equality legislation in making those decisions. Local authorities are responsible delivery agents and so subject to any representations received our conclusion is that no equality issues arise with regard to the proposed New Homes Bonus.

Consultation question 11 **Do you think the proposed scheme will impact any groups with protected characteristics?**

5.4. A full list of these groups can be found in the Equality Act 2010[6].

[5] http://www.equalities.gov.uk/PDF/20414%20Equality%20Guide%20bookmarked.pdf
[6] http://www.legislation.gov.uk/ukpga/2010/15/part/2/chapter/1

Consultation stage impact assessment

5.5. A consultation stage impact assessment for the New Homes Bonus is being published alongside this consultation document. A link to this can be found at Appendix E. The analysis is based on a series of assumptions, empirical evidence, international comparisons and previous reviews.

Consultation question 12 **Do you agree with the methodology used in the impact assessment?**

Conclusions

Consultation question 13 **We would welcome your wider views on the proposed New Homes Bonus, particularly where there are issues that have not been addressed.**

Handling of responses to this consultation

5.6. This consultation will be available for viewing at: http://www.communities.gov.uk/corporate/publications/consultations/

5.7. Your comments should be sent by 24 December 2010 if possible by email to:
newhomesbonus@communities.gsi.gov.uk
(with attachments in MS Word only)

5.8. Comments received on the proposals set out in the consultation will be collated and a formal response document published within three months of the closing date of the consultation. This consultation follows the Government's Code of Practice on consultations, which is set out in section one.

5.9. Information provided in response to this consultation, including personal information, may be published or disclosed in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004).

5.10. If you want the information that you provide to be treated as confidential, please be aware that, under the Freedom of Information Act, there is a statutory Code of Practice with which public authorities must comply and which deals, amongst other things, with obligations of confidence. In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on the department.

5.11. The Department for Communities and Local Government will process your personal data in accordance with the Data Protection Act and in the majority of circumstances this will mean that your personal data will not be disclosed to third parties. Individual responses will not be acknowledged unless specifically requested.

6. Summary of consultation questions

1. Do you agree with our proposal to link the level of grant for each additional dwelling to the national average of the council tax band?

2. The Government proposes an affordable homes enhancement of £350 for each of the six years - what do you think the enhancement should be?

3. Do you agree with the proposal to use PPS3 and also include pitches on Gypsy and Traveller sites owned and managed by local authorities or registered social landlords to define affordable homes?

4. Do you agree with the proposal to reward local authorities for bringing empty properties back into use through the New Homes Bonus? Are there any practical constraints?

5. Outside London: Do you agree with the proposal to split the payment of the New Homes Bonus between tiers: 80 per cent to the lower tier and 20 per cent to the upper tier, as a starting point for local negotiation?

   If not, what would the appropriate split be, and why?

6. Do you agree with the proposal to use the data collected on the Council Tax Base form as at October to track net additions and empty homes?

7. Do you agree with the proposal for one annual allocation based on the previous year's Council Tax Base form, paid the following April?

8. Do you agree that allocations should be announced alongside the local government finance timetable?

9. Do you agree with the proposal to reward local authorities for affordable homes using data reported through the official statistics on gross additional affordable supply?

10. How significant are demolitions? Is there a proportionate method of collecting demolitions data at local authority level?

11. Do you think the proposed scheme will impact any groups with protected characteristics?

12. Do you agree with the methodology used in the impact assessment?

13. We would welcome your wider views on the proposed New Homes Bonus, particularly where there are issues that have not been addressed in the proposed model.

Appendix A – Calculation of council tax

Each authority is required to set a ‘basic amount of council tax’. This is a Band D amount set by an authority under section 33(1) (if the authority is a billing authority), or 44(1) (if the authority is a major precepting authority other than the GLA) of the Local Government Finance Act 1992, or sections 88(2) and 89(3) of the Greater London Authority Act 1999 in the case of the GLA. An authority calculates it ‘basic amount of council tax’ by dividing the total council tax requirement (the total amount that it wishes to raise in council tax) by its tax base.

The tax base is the number of Band D equivalent dwellings in a local authority area. To calculate the tax base for an area, the number of dwellings in each council tax band is reduced to take account of discounts and exemptions. The resulting figure for each band is then multiplied by its proportion relative to Band D (from 6/9 for Band A to 18/9 for Band H) and the total across all eight bands is calculated. The tax base figure that is used by a local authority when it sets its council tax uses an adjustment for the collection rate and the actual discount for second homes.

The average Band D is calculated by taking the total council tax requirement for England and dividing by the total tax base for England. The average for each band is calculated by using the proportions relative to Band D.

Appendix B – PPS3, affordable housing definition

This Appendix should be read in conjunction with Planning Policy Statement 3[7].

Affordable housing is:

Housing which includes social rented and intermediate housing, provided to specified eligible households whose needs are not met by the market.

Affordable housing should:

- Meet the needs of eligible households including availability at a cost low enough for them to afford, determined with regard to local incomes and local house prices.
- Include provision for the home to remain at an affordable price for future eligible households or, if these restrictions are lifted, for the subsidy to be recycled for alternative affordable housing provision.

Social rented housing is:

Rented housing owned and managed by local authorities and registered social landlords, for which guideline target rents are determined through the national rent regime. The proposals set out in the *Three Year Review of Rent Restructuring* (July 2004) were implemented as policy in April 2006. It may also include rented housing owned or managed by other persons and provided under equivalent rental arrangements to the above, as agreed with the local authority or with the Housing Corporation as a condition of grant.

Intermediate affordable housing is:

Housing at prices and rents above those of social rent, but below market price or rents, and which meet the criteria set out above. These can include shared equity products (e.g. HomeBuy), shared ownership, other low cost homes for sale and intermediate rent.'

For the purposes of the New Homes Bonus, this definition can include homes provided by private sector bodies and homes without grant funding provided that the above criteria are met.

[7] http://www.communities.gov.uk/documents/housing/pdf/152897.pdf

Appendix C – Worked examples

The following table illustrates the size of the gross incentive payments to a local authority based on assumed delivery. Calculations are based on the scheme parameters set out in the consultation document with gross incentive payments based on the full amount received over six years. (Note: delivery of the same units may differ by local authority should units be built at differing band – in this illustration new delivery is assumed to be in-line with the existing stock of our example local authority).

Local authority A

Type of delivery	Units	Gross incentive
Net additions	1,800	£12.5m
- of which are affordable homes	500	£1.1m
Empty homes bought back into use	20	£0.1m
Gypsy and Traveller sites	10	£0.1m
Total		**£13.8m**

Local authority B

Type of delivery	Units	Gross incentive
Net additions	400	£3.3m
- of which are affordable homes	40	£0.1m
Empty homes bought back into use	10	£0.1m
Gypsy and Traveller sites	40	£0.2m
Total		**£3.6m**

To illustrate the incentive payments to particular local authority readers are invited to explore the online payment calculator[8].

[8] http://www.communities.gov.uk/housing/housingsupply/newhomesbonus

Appendix C (Part 2) – Worked examples

<u>Year X</u>

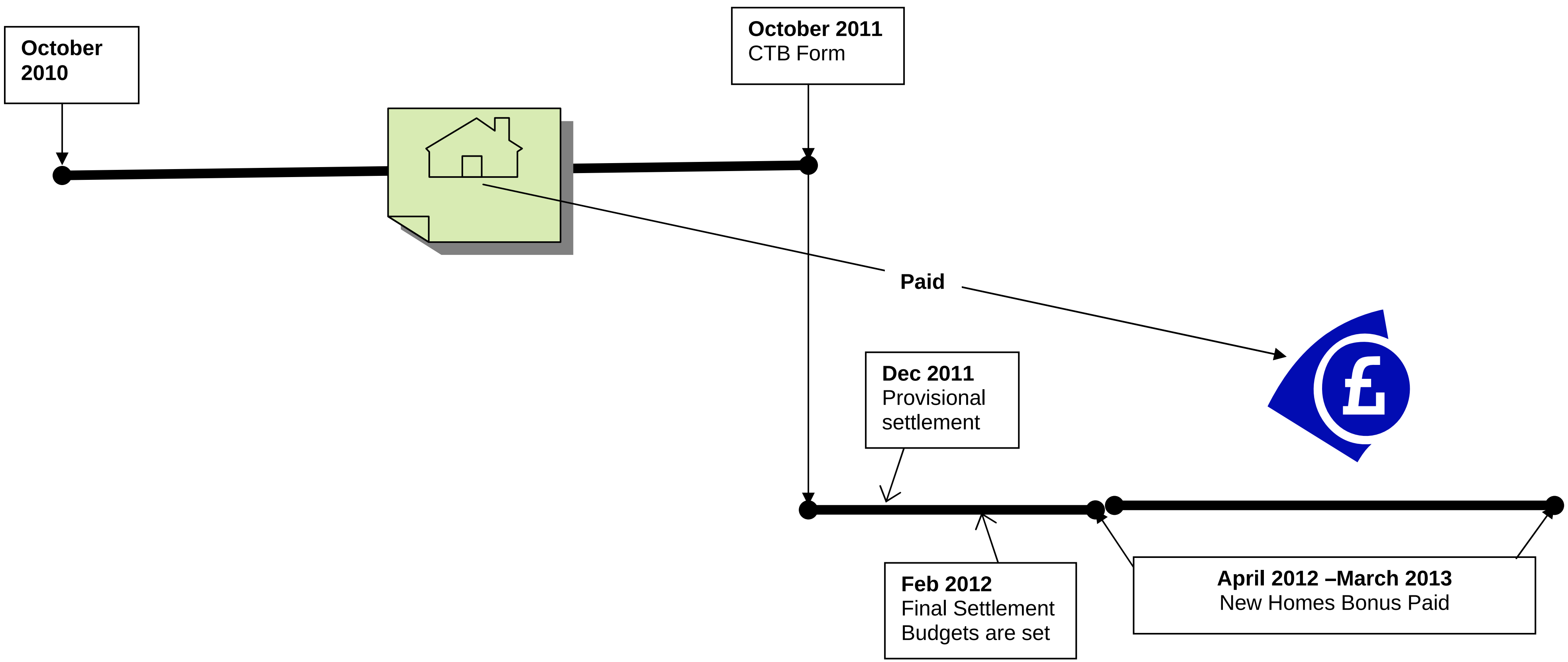
Council Tax Band	**A**	**B**	**C**	**D**	**E**	**F**	**G**	**H**
Line 1	600	750	500	300	250	100	50	10
minus								
Line 3	20	10	12	8	3	1	0	0
minus								
Lines 12, 14, 15	50	20	2	0	0	0	1	0
Adjusted line 1	530	720	486	292	247	99	49	10
Adjust to band D	6/9	7/9	8/9	1	1/9	13/9	15/9	2
Band D equivalent	353	560	432	292	302	132	71	20

<u>Year X+1</u>

Council Tax Band	**A**	**B**	**C**	**D**	**E**	**F**	**G**	**H**
Line 1	650	780	520	340	260	110	55	12
minus								
Line 3	18	9	12	5	3	2	0	0
minus								
Lines 12, 14, 15	40	18	2	0	0	0	0	0
Adjusted line 1	592	753	506	335	257	108	55	12
Adjust to band D	6/9	7/9	8/9	1	11/9	13/9	15/9	2
Band D equivalent	395	586	450	335	314	144	79	24
Net change	41	26	18	43	12	12	9	4

Multiply by £1,439	59,479	36,934	25,582	61,877	17,588	17,268	12,471	5,756
Gross incentive (Y1)	**£236,955**							
Gross incentive over 6 years	**£1,421,732**							

Appendix D – Payment model (example for year two)



Appendix D (Part 2) – Payment model

	2011-12	2012-13	2013-14	2014-15	2015-16	2017-18	2018-19
Year 1	£10,000	£10,000	£10,000	£10,000	£10,000	£10,000	
Year 2		£15,000	£15,000	£15,000	£15,000	£15,000	£15,000
Year 3			£15,000	£15,000	£15,000	£15,000	£15,000
Year 4				£20,000	£20,000	£20,000	£20,000
Year 5					£15,000	£15,000	£15,000
Year 6						£25, 000	£25,000
Year 7							£20,000
Total	**£10,000**	**£25,000**	**£40,000**	**£60,000**	**£75,000**	**£100,000**	**£110,000**

Appendix E Consultation stage impact assessment

Impact assessment: New Homes Bonus

This document provides a robust analysis of the potential impacts of one element of a package of policies that will have an impact on housing supply.

This document should be read in conjunction with impact assessments for related measures that form part of the Government's housing supply strategy. It should be recognised that some measures, considered in isolation, may not increase supply. However, they contribute to a new approach, which will deliver more of the homes that people want, where they want them. This new approach aims to rebalance power from central government to local authorities and local people, combined with new freedoms and financial incentives.

Title: New Homes Bonus	Impact Assessment (IA)
Lead department or agency: Department for Communities and Local Government	**IA No:**
Other departments or agencies:	**Date:** 05/11/2010
	Stage: Consultation
	Source of intervention: Domestic
	Type of measure: Other
	Contact for enquiries:

Summary: Intervention and options

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

There is a significant and persistent gap between the supply of and demand for new homes in the UK. This undersupply has led to significant problems of affordability, particularly for those seeking to buy their first home. It has also led to wider social and economic problems, for example higher labour costs for firms and reduced labour mobility.

The fact that housing supply is not as responsive to changes in demand in England as it is in many other markets might be due to various factors including: the availability of credit to developers; planning and building regulation and the availability of land and the provision of infrastructure. Therefore, Government intervention is necessary to alleviate policy barriers, provide support and incentives for housing growth.

What are the policy objectives and the intended effects?

The key objective of the New Homes Bonus is to create a powerful financial incentive for local authorities to facilitate housing growth. We aim to ensure that the scheme is simple and transparent so that it is easily understood and that it is a predictable and permanent feature of the local government finance system. The intended effect is to increase housing supply and provide the homes that communities need and want.

What policy options have been considered? Please justify preferred option (further details in Evidence Base)

The current system penalises local authorities for new homes and the previous grant scheme, Housing and Planning Delivery Grant, did not provide a sufficient incentive to change this. The Government considers a new approach is required. Local authorities and local communities need to see the benefits of growth and not just the costs. They should be given greater control over how their towns and villages grow. This scheme is part of a framework of incentives to increase housing and business growth and this policy enacts a manifesto commitment.

When will the policy be reviewed to establish its impact and the extent to which the policy objectives have been achieved?	It will/will not be reviewed 01/2010
Are there arrangements in place that will allow a systematic collection of monitoring information for future policy review?	Yes/No

SELECT SIGNATORY Sign-off For consultation stage Impact Assessments:

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: .... Date: 12 November 2010

Summary: Analysis and Evidence

Policy Option 1

Description:

Implement the New Homes Bonus.

Price Base Year 2010	PV Base Year 2010	Time Period Years 10	Net Benefit (Present Value (PV)) (£m)		
			Low: £2,006m	**High: £3,845m**	**Best Estimate: £2,821m**

COSTS (£m)	**Total Transition** (Constant Price)	Years	**Average Annual** (excl. Transition) (Constant Price)	**Total Cost** (Present Value)
Low	Optional		-	**-**
High	Optional		-	**-**
Best Estimate			-	**-**

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

This policy redistributes a portion of formula grant on the basis of housing delivery. As a result - in the long run - there are no additional cost implications to central Government. However, over the course of the Spending Review period, additional funding (over £900m) from central Government will be provided from the abolition of Housing and Planning Delivery Grant. This will fund the total cost of the scheme in year 1; with the remainder spread across years 2-4.

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

BENEFITS (£m)	**Total Transition** (Constant Price)	Years	**Average Annual** (excl. Transition) (Constant Price)	**Total Benefit** (Present Value)
Low	Optional		£257.2m	**£2,006m**
High	Optional		£493.1m	**£3,845m**
Best Estimate			£361.7m	**£3,821m**

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

Additional housing units provide a welfare benefit as estimated using land value uplift (see details in the evidence base). We estimate this policy will lead to an 8 to 13 per cent increase in net additions above the baseline from 2016-17 onwards.

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

Additional housing units boost the construction industry providing more jobs. (mid-point estimate of 11,100 p.a. net jobs supported – see evidence base for calculation)

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

The distribution of financial winners and losers is illustrated through retrospective modelling of housing output to which a broad set of behavioural responses are applied to get an estimated impact in terms of housing supply (as discussed further in the evidence base).

The best estimate represents scenario 2 of modelling and not simply the average of high and low. With some local authorities facing budget reductions there may be trade-offs for existing expenditure.

Impact on admin burden (AB) (£m):			**Impact on policy cost savings (£m):**	**In scope**
New AB:	**AB savings:**	**Net:**	**Policy cost savings:**	Yes/No

Enforcement, Implementation and Wider Impacts

What is the geographic coverage of the policy/option?			England		
From what date will the policy be implemented?			01/04/2011		
Which organisation(s) will enforce the policy?			DCLG		
What is the annual change in enforcement cost (£m)?			n/a		
Does enforcement comply with Hampton principles?			Yes		
Does implementation go beyond minimum EU requirements?			Yes		
What is the CO_2 equivalent change in greenhouse gas emissions? (Million tonnes CO_2 equivalent)			**Traded:** n/a		**Non-traded:** n/a
Does the proposal have an impact on competition?			No		
What proportion (per cent) of Total PV costs/benefits is directly attributable to primary legislation, if applicable?			**Costs:** n/a		**Benefits:** n/a
Annual cost (£m) per organisation (excl. Transition) (Constant Price)	**Micro**	**< 20**	**Small**	**Medium**	**Large**
Are any of these organisations exempt?	Yes/No	Yes/No	Yes/No	Yes/No	Yes/No

Specific Impact Tests: Checklist

Set out in the table below where information on any SITs undertaken as part of the analysis of the policy options can be found in the evidence base. For guidance on how to complete each test, double-click on the link for the guidance provided by the relevant department.

Please note this checklist is not intended to list each and every statutory consideration that departments should take into account when deciding which policy option to follow. It is the responsibility of departments to make sure that their duties are complied with.

Does your policy option/proposal have an impact on…?	Impact	Page ref within IA
Statutory equality duties[1] Statutory Equality Duties Impact Test guidance	No	18
Economic impacts		
Competition Competition Assessment Impact Test guidance	No	18
Small firms Small Firms Impact Test guidance	No	18
Environmental impacts		
Greenhouse gas assessment Greenhouse Gas Assessment Impact Test guidance	No	18
Wider environmental issues Wider Environmental Issues Impact Test guidance	Yes	18
Social impacts		
Health and well-being Health and Well-being Impact Test guidance	No	18
Human rights Human Rights Impact Test guidance	No	18
Justice system Justice Impact Test guidance	No	18
Rural proofing Rural Proofing Impact Test guidance	No	18
Sustainable development Sustainable Development Impact Test guidance	No	18

[1] Race, disability and gender Impact assessments are statutory requirements for relevant policies. Equality statutory requirements will be expanded 2011, once the Equality Bill comes into force. Statutory equality duties part of the Equality Bill apply to GB only. The Toolkit provides advice on statutory equality duties for public authorities with a remit in Northern Ireland.

Evidence Base (for summary sheets) – Notes

Use this space to set out the relevant references, evidence, analysis and detailed narrative from which you have generated your policy options or proposal. Please fill in **References** section.

References

Include the links to relevant legislation and publications, such as public impact assessment of earlier stages (e.g. Consultation, Final, Enactment).

No.	Legislation or publication
1	Open Source Planning, Conservative Party, 2010 www.conservatives.com/~/media/Files/.../planning-green-paper.ashx
2	Barker Review of Land Use Planning, Kate Barker, 2006 www.communities.gov.uk/documents/planningandbuilding/.../154265.pdf
3	
4	

+ Add another row

Evidence Base

Ensure that the information in this section provides clear evidence of the information provided in the summary pages of this form (recommended maximum of 30 pages). Complete the **Annual profile of monetised costs and benefits** (transition and recurring) below over the life of the preferred policy (use the spreadsheet attached if the period is longer than 10 years).

The spreadsheet also contains an emission changes table that you will need to fill in if your measure has an impact on greenhouse gas emissions.

Annual profile of monetised costs and benefits* - (£m) constant prices

	Y_0	Y_1	Y_2	Y_3	Y_4	Y_5	Y_6	Y_7	Y_8	Y_9
Transition costs										
Annual recurring cost										
Total annual costs										
Transition benefits										
Annual recurring benefits										
Total annual benefits										

* For non-monetised benefits please see summary pages and main evidence base section

Microsoft Office Excel Worksheet

Evidence base

Problem under consideration

There is a significant gap between the supply of and demand for new homes. For decades, the housing market has failed to keep up with the needs of our growing population. This has led to significant problems of affordability, particularly for those seeking to buy their first home. It has also led to wider social and economic problems for example higher labour costs for firms and reduced labour mobility. The reasons for the lack of responsiveness of housing supply are discussed in detail in the Barker Review (2006).

House building in England is at its lowest levels since 1946, with just 118,000 completions in 2009. If you take into account the obvious effect of the Second World War, this is the lowest rate of house building across England and Wales since 1923-24. However, the long-term demand for housing is strong. The latest published household projections show that around 252,000 new households could form each year between now and 2031 (as a result of increased longevity, migration and a rise in the number of single-person households), 134,000 above current build levels.

This stagnation in growth comes at a time when house-building is crucial to the state of the wider economy and demographic changes mean that demand for new homes is growing.

Housing supply accounts for between 2¾ per cent and 3¼ per cent of GDP and provides 1 to 1¼ million UK jobs (3½ per cent to 4 per cent of the total). 85 per cent of adults aspire to own their own home 10 years from now[2] and as incomes rise they have a strong propensity to consume housing services.

Rationale for intervention

The current local government finance system does not provide the right incentive or rewards for councils to build new homes. Housing growth can place additional demands on services and infrastructure without corresponding benefits which often provokes a strong resistance to growth from local communities. In addition the top down target led approach which attempted to force developments on communities would often antagonise communities and increase resistance.

The New Homes Bonus is the cornerstone of the new Government's approach to housing supply incentives and seeks to transform this situation. The scheme is part of a wider family of incentives that were set out in the Local Growth white paper, published on October 28. The white paper detailed the Government's new approach to rebalance the economy and drive sustainable growth. This section provides evidence on the analytical underpinnings for this approach in the context of housing supply and the goal of meeting people's housing aspirations.

[2] CML (2010) http://www.cml.org.uk/cml/media/press/2708

Policy objective

The principle aim of the scheme is to create a powerful, simple, transparent and permanent incentive for local authorities and communities to increase their aspirations for housing growth.

The scheme will help ensure that communities reap the benefits of growth and not just the costs. We will not tell local authorities what type of development or homes they should build or where, but we will reward authorities and communities where growth takes place. To achieve growth, local authorities will need to lead a mature debate within their communities and this new funding system will help facilitate that debate.

Descriptions of options considered (including do nothing)

The Government's view is that the previous system of setting top-down targets meant that communities moved against development. This approach failed to deliver enough houses even at the height of a debt-fuelled housing boom and created distortions that did not to deliver the right investment in the right places. And the recent downturn in the housing market makes reform all the more necessary.

Furthermore, the current finance system penalises local authorities for new homes and the previous attempt to address this, Housing and Planning Delivery Grant, did not provide a sufficient incentive.

The Government considers a new approach is essential. Local authorities and local communities need to see the benefits of growth and not just the costs and they should be given greater control over how their towns and villages grow. This can only be done by returning the benefits of growth to those communities. The consultation sets out the Government's preferred model and the responses will determine the final scheme design.

Summary and description of preferred option and implementation plan

The proposed scheme will incentivise local authorities to increase housing supply by rewarding them with a New Homes Bonus, paid as an unringfenced grant, equal to the average council tax on each additional property and for properties brought back into use, for the following six years. The scheme will by implemented in April 2011.

Evidence – the role of incentives

In developing the proposal, Government is drawing on an extensive evidence base around the role of incentives in changing behaviours. Incentives are essentially concerned with changing collective or individual agent behaviour: an incentive is any factor that motivates a particular course of action, or counts as a reason for preferring one choice over another. In public policy incentives are often used to induce us to consumer more or less of particular goods. For example, lower car tax on 'green' cars encourages greater consumption, whilst taxes on alcohol aim to reduce consumption.

Incentives alone, however, are often insufficient and need to be supported by other measures. Models of behavioural change often consider a cyclical process involving five stages. Figure 1.1 illustrates this process using the example of smoking: an area that has seen numerous incentive-based policies implemented and where the proportion of male smokers has fallen from 65 per cent in 1948 to 21 per cent today.

Figure 1.1: Example of smoking in the process of behavioural change

	Awareness of the problem and need for change	Better information about the health impact of smoking on the individual and those around (via second hand smoke).
Use of Incentives	Motivation to make the change	Financial incentives via rising taxes, as well as moral incentives that smoking is not ‘right’
	Skill development to prepare for change	Provision of free NHS ‘stop smoking services’ to offer advice and support for those wanting to quit.
	Initial adoption of new activity or behaviour	Self monitoring of newly adopted behaviours, opportunities for reflection and comparison
Use of Incentives	Maintenance of the new activity and integration into lifestyle	Provision of feedback on how the change is going, and injection of new ideas or strategy: behavioural change reinforced by new incentives (smoking ban in public places)

This example highlights the importance of an awareness of the problem and need for change, without which the motivation for change – induced by the implementation of incentives – is likely to be less effective.

Effective incentive design

Incentives come in many different forms and this section discusses numerous factors to consider when designing incentives. It must be noted that this is not a blue-print to the formulating a perfect incentive, but rather a framework of factors to consider, as factors will vary in importance depending on specific objectives.

TYPE
The main incentives tools used are financial (via taxes and subsidies) whereby agents are rewarded for acting in a certain way. Other categories of incentive include moral incentives (enforced as they are the ‘right thing to do’ and that agents will gain non-material benefits i.e. admiration or self-esteem for particular actions) and coercive incentives (in which failure to act as required will lead to ‘physical force’ such as imprisonment or confiscation of property). In general, financial incentives are considered the most effective.

FLEXIBILITY
Linked to the type of incentive is the issue of flexibility. Mostly related to financial incentives this considers where and in what time frame the monies received can be spent. For example, financial benefits received can be restricted to expenditure on certain items within a time limited period or at the discretion of the recipient. Greater flexibility is likely to maximise behavioural change but could distort the intended policy outcome (i.e. if the monies are spent less efficiently without restrictions).

SIZE
Larger incentives are likely to induce the greatest behavioural response at an individual level (though the relationship is likely to be non-linear). It must also be noted that bigger incentives may not always produce the best outcome at a society level. This is because for a given budget, there is a trade off between magnitude of impact and numbers targeted: large incentives aimed

at few can lead to perverse incentives (see later) thereby undermining the intended outcome whilst incentives that are too small will result in no impact on behaviour.

Maximising both impact and number can be particularly important as large numbers of people changing behaviour can help to reinforce change by changing the social norm and thereby installing a moral incentive also.

TARGETING

Government incentives are designed to create a better outcome for society yet they can be targeted via different agents. For example, a financial incentive to encourage more households to insulate their homes could be given directly to the consumer or to the producer. Optimal targeting will vary by policy area: producers may have more certainty and benefit from economies of scale if they receive the incentive (or not pass on the full benefit gained).

TIMING

In general we prefer benefits now rather than later, but in some cases this will be more important than others. Much of this depends on (assuming a financial incentive) what the monies received will be spent on. For example, if the monies are to be spent on expensive time-consuming projects then it is important to receive the money early.

CERTAINTY

Certainty of an incentive relates to the length of time it will last and its size. In terms of time period, changing behaviour is likely to occur incrementally: agents need time to adapt, new systems may need to be set up and changes reinforced by real positive outcome/updated social norms.

Beneficiaries also need certainty over the size of incentive. For example, if the size of incentive is dependent on external factors (or the actions of others) recipients will be less able to plan ahead on the basis of what they expect to receive. Overall, uncertainty about the length and size of incentives will undermine the level of behavioural change and thus the impact of the incentive.

SIMPLICITY

Linked to the issue of certainty is the simplicity of the incentive, that is, do potential recipients understand what they have to do to realise the benefit of the incentive and what the incentive is trying to achieve overall. Individuals in general do not like change and thus unnecessary complexity may lead to greater numbers sticking with the ‘status quo’. This serves to highlight the trade-off between simplicity and effectiveness.

PERVERSE INCENTIVES

A perverse incentive is where an incentive leads to an unintended or undesirable effect that is against the intention of the policy maker: they produce unintended consequences. For example, there is some evidence in the US that the smoking ban in public spaces has led to more children exposed to smoking within the home. These issues are often difficult to identify but careful consideration must be given or the outcome could be worse than the counterfactual.

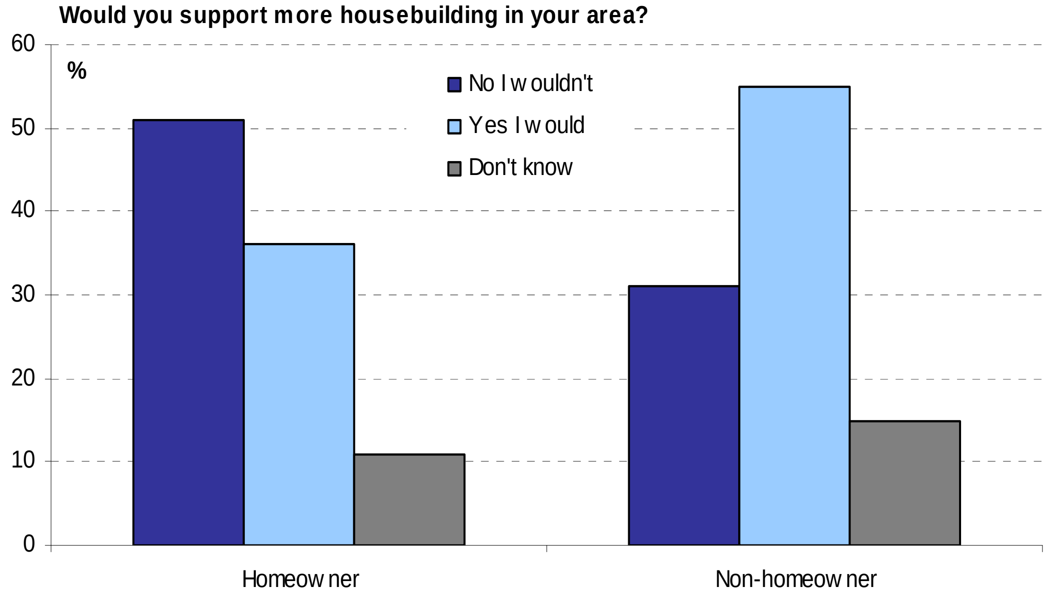
MEASUREMENT

For any incentive to be successful it is essential for agents to understand the desired outcome. This will be determined by both clarity of objectives and method of measurement. Without clear measurement of progress it is very difficult to evaluate incentives and allow opportunities to improve outcomes.

Evidence - Incentives in theory and practice

THEORY

In the UK, it is often perceived that the key factor influencing housing supply is local politics: the interaction between local residents and the local authority. Local authorities have little incentive to welcome house building, as do local residents. It has been found that 'organised local amenity groups and those opposing specific development proposals are more likely to participate in community engagement[3].



There is also variation by current tenure: over half of homeowners would oppose more houses being built in their area, compared with less than a third of non-homeowners[4]. The reasons for local authority and resident opposition overlap; it often revolves around supporting infrastructure. Local authorities concern is finance; for local residents is the potential strain on infrastructure and local services. Evidence suggests that private residential development most often opposed due to traffic congestion, pollution and protection of green space/environment[5]. A survey of the South East finds that there seems to be no blanket opposition to land being used for development. It emphasises that people support new housing and growth when it is coupled with open space, services and infrastructure[6].

Hence, the reasons for opposition are due to the negative externalities arising from development. Incentives are used to mitigate externalities, which can reduce local opposition to development and thus can lead to greater supply. Economic theory states that agents can be compensated for externalities. For example, there is one group who frequently favour development because of the compensation received – those who own a large garden or farm with planning permission: in the South East a hectare of agricultural land is worth £7,410 while the same hectare with planning permission for housing is worth £3.32m[7]. These landowners may not welcome the development as such, but the compensation is likely to be sufficient to counter the detrimental effects of extra housing. Therefore, if communities as a whole could capture the value of the planning permission granted, local people would be fairly compensated. This provides an incentive to support rather than oppose new development.

---

[3] Ferrari et al., 2010. *Behavioural Change Approach and the Housing Sector: a note on incentivising community engagement. Sheffield University*
[4] NHPAU YouGov Survey, May 2009.
[5] Saint Consulting. 2009 UK Saint Index.
[6] The Joseph Rowntree Foundation. *Public views of development options in the South East*. June 2004.
[7] Leunig, T. 2007. *In my back yard*. VOA, 'Agricultural land and property', Property Market Report, July 2006.

Another key constraint on development is funding supporting infrastructure; a concern of local authorities and residents. Infrastructure costs will vary by scheme. One estimate for a 'typical' scheme of 1,000 units puts these infrastructure costs, such as education and healthcare at £20m[8]. It could be argued that given the scale of these costs, they should be financed by the developer rather than central government (such as via community infrastructure levy). Theory states that infrastructure, such as roads, are public goods. It could be said that developers may be reluctant to provide infrastructure due to free-riding: they can benefit from the provision of services by other developers/government and thus bear less than a fair share of the production costs.

It is important to acknowledge however, that such methods may get around the infrastructure provision issue but are not always best in all cases: certain groups would not benefit from improvements to infrastructure and local amenities in the same way as others. For example, to address externalities such local residents losing value in their property, it may be more efficient for compensation to be paid directly to the homeowner rather than via the local authority.

Both the Barker Review of Housing Supply and the Lyons Inquiry into Local Government recommended the use of incentives to *"provide space – at the margins, but with enough weight to change local government behaviours – to incentivise local government to grow their tax bases and crucially enable local communities to receive some reward for allowing their area to develop and grow"*. Furthermore, Prof. Ball stated *"there should be further investigation of a greater range of fiscal options than exists at present to incentivise local authorities against adopting excessive planning restrictions and reward those providing additional housing"*[9]. In response two main policies – each of which target the local politics side of the housing supply equation – have been implemented.

Empirical findings from Hilber et al (2010) imply that in fact *"LPAs have strong fiscal disincentives to permit new residential developments. This is due to a misalignment of costs (too much burden on LPAs) and benefits (too low long-term payback) associated with residential developments"*. The report thus recommends the *"fiscal system to provide serious fiscal incentives to permit residential developments"*[10].

We can also look to past forms of intervention for evidence of the role that financial incentives have played in encouraging housing supply. For example, launched in 2005 the Growth Fund supported the provision of infrastructure for housing growth in Growth Areas and Growth Points: local authorities were invited to bring forward their own proposals for large scale sustainable growth, in return for infrastructure funding support.

Across the programme local authorities committed to build an additional 350,000 units. This is at an average cost of 500 units per £m or a cost per unit of £2,000. However, it must be noted that this assumes all units are additional i.e. they would not have been built without funding and in practice due to wider market conditions, many of the units may not in fact be delivered (or will be delivered more slowly). But the example serves to illustrate the point that by providing for an area to benefit from the proceeds of growth then a positive incentive is generated which may act to change attitudes and behaviours to that growth. It is also worth noting the variation in commitments by local authority. For example, though the average promise of additional units was 42 per cent extra but this by between 1 per cent and 97 per cent. This highlights how incentives can lead to different impacts (i.e. behaviours) in different places.

[8] Estimates by Roger Tym & Partners consultancy.
[9] DCLG (2010) http://www.communities.gov.uk/documents/housing/pdf/1526670.pdf
[10] Hilber et al (2010) 'The effect of supply constraints on housing costs' NHPAU (forthcoming)

Analytical approach to measuring the impact on supply

Differences in the challenges faced by communities in delivering housing growth and in the financial distribution of money out of the formula grant settlement mean that local authorities are likely to respond in a variety of ways to the New Homes Bonus. Furthermore, the behavioural response of local authorities to their net financial position may change over time as attitudes and financial impacts alter. Together these factors make estimating the supply impact a challenge.

The approach adopted here is to use behavioural change based scenario modelling. Here, we consider a number of potential behaviours that local authorities could adopt, estimate the supply responses consistent with each of these behaviours, and analyse where different proportions of local authorities take each behavioural response. The following section outlines this approach in more detail.

FUNDING REQUIREMENT

The New Homes Bonus is set to be funded primarily by taking money out of the formula grant settlement. That is, money will be taken out of the formula grant allocation and redistributed based on the parameters of the bonus: the policy therefore – in the long run - is revenue neutral. This redistributive mechanism of the New Homes Bonus means that the scheme will create financial winners and losers: for any authority to gain financially (relative to their allocation before the bonus), one or more authorities must lose financially. Across the spending review period, however, these impacts will be mitigated by additional central Government money from the abolition of the Housing and Planning Delivery Grant: this will fund the full cost in year 1 and a falling proportion across years 2-4.

With uncertainties around the future amount and distribution of formula grant, along with the amount that would need to be take out of the formula grant settlement, the impact has been modelled retrospectively. In other words, we have calculated the annual funding requirement, taken this amount out of the formula grant settlement and redistributed it as if the scheme had been introduced in 2005-06 (i.e. six years ago).

This methodology provides a distribution of financial winners and losers. To explain: formula grant is distributed on a formula based on numerous variables such as council tax base, population etc. It also includes ‘floors’ which prevent authorities from being given too little to provide basic services. Both of these factors (the formula and floors) are based on the decisions of the Government of the day.

As a result, this analysis provides a useful illustration of the distribution of financial winners and losers based on the circumstances of the local government finance system in 2005-06. However, both the formula and floors are unlikely to be the same in the future and thus the distributional pattern of net ‘winners’ and ‘losers’ will most likely differ. Furthermore, these estimates are based on the previous delivery of net additions and thus do not capture the potential behavioural response to the incentive – something which is factored in later into the analysis (see below).

Despite these caveats these estimates do provide a best estimate of financial net winners and losers, which are required to estimate the overall impact on supply looking forward (see methodology below).

ESTIMATING THE IMPACT ON SUPPLY
We can't know how local authorities will behave in response to the New Homes Bonus, but we can consider a range of behavioural responses they could adopt and assess the implications for housing delivery. This means, for the purposes of the impact assessment, we can set out a range of outcomes that reflect the different strategies and the distribution of these strategies across local authorities.

When considering the financial impact of the New Homes Bonus it is important to focus on the net impact, that is: both monies taken away from formula grant and received through incentive payments upon housing delivery. As described above, our retrospective analysis provides us with an estimate of each local authority's net financial position; this analysis considers the behavioural impact in terms of housing supply resulting from this net financial position.

In the analysis there are three broad strategies that a local authority can adopt:

1. **maintain levels of expenditure on existing population**: here, winners are able to reduce their housing delivery, whilst losers strive to increase output
2. **building away the losses**: in this strategy local authorities that win will maintain their current build rates and those that lose will increase delivery
3. **'race-to-the-spade'**: local authorities try to increase their overall budgets by building more units; local authorities become more open to growth with only those strongly against growth not increasing output.

In order to quantify the supply impact we calculate how much each local authority would need to change their housing delivery by to be consistent with each of the three strategies. The scale of the effect varies by local authority and is dependent on the current build rate and the size of the fund removed from the formula grant settlement (percentage reduction).

For every local authority we estimate the income elasticity[11] of net additions with respect to income (percentage reduction due to money being taken from the formula grant settlement) associated with maintaining initial spend per household. This measure of responsiveness is then used to estimate supply responses for each behaviour. See Annex A for more detail.

These estimates are then constrained – by demand and land supply – as measured and ranked by the following:

- **affordability ratio**: the ratio of lower quartile earnings to lower quartile house prices
- **brownfield land suitable for housing**: the number of years land supply identified at current density and build rates

In both constraints, each local authority is measured and ranked relative to others. For example, local authorities with an affordability ratio above the national average are assumed to have no constraint; those above the national lower-quartile are assumed to be constrained to 20 per cent above the baseline and those below lower-quartile at just 10 per cent above the baseline. Land supply constraints are constructed similarly, with those having a five-year land supply having no constraint; three to five years restricted to 20 per cent; and less than three years limited to 10 per cent growth above the baseline.

Finally, estimates in the 'steady state' – from year six onwards – are constrained to 30 per cent above the baseline i.e. it is assumed a local authority can increase housing supply by a maximum of 30 per cent above the baseline (see below). Prior to this point, growth is assumed to build up exponentially as the scheme is implemented and behaviours change over time. Table one illustrates how the financial impact and two constraints work to estimate the overall impact on supply.

[11] Percentage change in housing supply resulting from a 1 per cent reduction in income.

Table 1: Illustrative impact on supply by local authority growth with financial impact and constraints

Local authority	*Financial impact*	*Housing demand constraint*	*Land capacity constraint*	***Impact on supply***
A	22%	20%	30%	**20%**
B	28%	30%	30%	**28%**
C	18%	10%	10%	**10%**

The analysis then needs to consider how these behavioural responses across different local authorities. To illustrate, we create three scenarios based on the proportion of authorities that will adopt each behavioural response and randomly allocate these across local authorities.

Table 2: Proportion of local authorities adopting each behaviour in lower, central and upper scenarios[12]

	Behaviour 1	**Behaviour 2**	**Behaviour 3**
S1	50%	50%	0%
S2	33%	33%	33%
S3	0%	50%	50%

HOUSING SUPPLY BASELINE

In making the assessments of potential impact, a baseline for future net additions has been assumed. This baseline is described below and has been used consistently in the analysis of a series of related policies that concern housing supply. This allows those potential 'quantitative' housing supply impacts to be considered collectively and to provide a net overall assessment. The baseline takes view of future housing supply (as measured by the net additions measure of changes in the housing stock) based on past performance in the market across housing market cycles. The table below summarises the assumptions made in the baseline:

Completions: net additions ratio	1.13
Peak to trough fall (per cent)	-42%
Recovery from (year)	2011-12
Rate of recovery (per cent)	5% - 8%

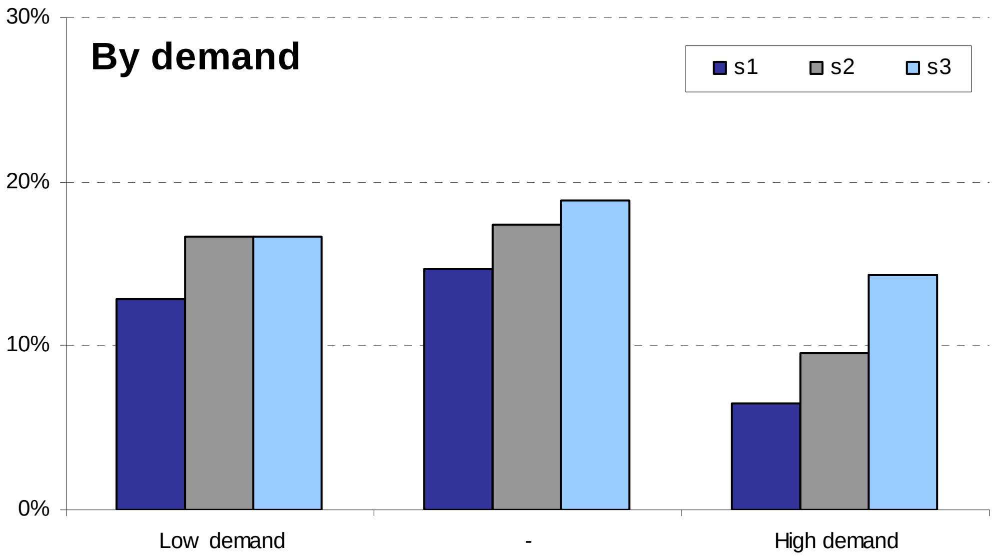
Headline results

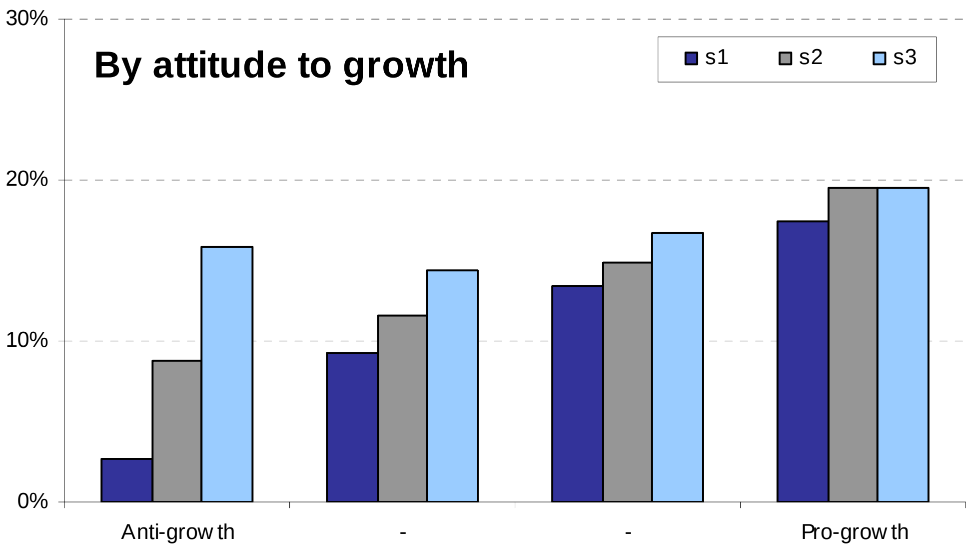
Following the behaviour based scenario approach above, and applying some additional assumptions around the current/near term fiscal environment we estimate the aggregate impact on supply. The Spending Review set out overall reductions in formula grant of 26 per cent[13]. As a modelling assumption we assume that 10 percentage points of this reduction will be potentially mitigated through a housing supply response, with the remainder absorbed by other means (e.g. reduced expenditure). These provide a range of supply estimates from 8 per cent (S1), 11 per cent (S2) to 13 per cent (S3). To explain: under scenario 2 housing supply will be

[12] Note: The response of authorities that lose out is the same under each strategy – to increase supply.
[13] HM Treasury (2010) http://www.hm-treasury.gov.uk/spend_sr2010_documents.htm

11 per cent higher than the baseline from 2016/17 onwards. Over the initial 10-year period this is equivalent to 140,000 additional units for the mid-point scenario.

Estimated impact on supply by various factors, 2016-17 on





As shown, in aggregate terms there is a range of housing supply impacts between the three scenarios. This range may be higher or lower depending on a range of factors:

- **demand**: The supply response is more variable in higher demand areas
- **attitude to growth**: Areas with more a more anti-growth attitude see greater variability across scenarios

These trends are driven by the estimated net financial impacts from our retrospective analysis as outlined above, and thus are sensitive to decisions taken about the formula and floors.

DEMAND AND LAND SUPPLY CONSTRAINTS
As outlined in the methodology, demand and land supply constraints[14] have been applied to produce the final results. These serve to constrain some authorities achieving their desired build rate. Removal of these constraints would boost the central supply estimates to 10 per cent (S1), 12 per cent (S2) and 15 per cent (S3) above the baseline from 2016/17 onwards. Of the two, demand is the more binding constraint.

Having outlined the analytical approach and headline results, we now move on to discuss the application of this behaviour-based scenarios modelling when considering the overall costs and benefits of the policy.

Costs

As discussed above, the New Homes Bonus is a redistributive policy. It essentially shifts the way that a proportion of formula grant is distributed towards the delivery of net additions. As a result there are no direct costs from the policy.

Indirectly, given the redistribution by definition create financial winners and loser's authorities will adjust their expenditure accordingly. This point, however, must be put into context with the New Homes Bonus only affecting the distribution of a small proportion of overall formula grant.

Benefits

As derived by the methodology above we estimate the New Homes Bonus to lead to an increase in supply of 8-13 per cent above the baseline from 2016-17 onwards (with growth built up exponentially in previous years). In order to quantify the value of these additional units we consider the resulting land value uplift and jobs supported.

For land value uplift: in short, this approach uses land value changes following the approval of new housing developments as a measure of the 'private' value of additional housing and then nets off any external impact (which may be positive or negative). It can be summarised as follows:

- net private value of new housing = residential land value – existing land use value
- net social value of new housing = net private value of new housing + net external impact of housing development

Based on January 2010 land values and densities over the past four years (at a regional level), this land value uplift can be applied to the additional housing units estimated above. This creates from £2,006m (S1) to £3,845m (S3) – in the central estimate (S2) the value is £2,821m.

In addition, additional housing units will support jobs across the housing supply chain: we estimate the number as follows. The average new build property is sold for £216,015 (DCLG, England, Q2, 2010). For the purposes of illustration we assume that around a third of this value represents the cost of construction (£72,000 per unit). Multiplying this up the number of units above and applying a coefficient of 21 gross direct jobs per £1m of construction output[15] provides a mid-point estimate of 21,000 gross direct jobs per annum.

[14] Note: it must be noted that as land designated as suitable for housing by a local authority it may be biased by the efficiency of that local authority.
[15] Based on: Construction skills (http://www.cskills.org/)

To this estimate we then increase to reflect the like supply-chain multiplier (of 1.59, source: Scottish Government) and finally, to account for additionality and displacement we make assume that one-third of these jobs are additional. This gives us a final estimate of 11,100 net direct and indirect additional jobs per annum resulting from this policy.

New burdens

There will be no new burdens imposed on local authorities. It is proposed that payment of the New Homes Bonus will be determined by the CTB form. This data is already collected, thus this does not require additional work from local authorities (see consultation document for further details).

One-in-one-out

It is not thought that this policy will place additional burden on business.

Specific impact tests

Statutory equalities

In line with guidance issued by the Government Equalities Office (GEO), we have had regard to equalities issues as the proposed New Homes Bonus has been designed. We consider it good practice to consult as widely as possible on these issues and as part of the consultation we have asked respondents to consider whether the proposed scheme is likely to have any equalities impacts.

Economic impacts

An increase in housing supply will lead to positive impact directly on the construction sector and more widely on business. This will be beneficial to both competition and small firms. This has been illustrated above in both the estimation of value created from additional units and the net jobs created.

Environmental impacts

The environmental impacts may result from increased development that takes place as a result of this policy. There may be impacts in respect of:

- consumption of land
- carbon emissions through construction and through general increased level of economic development

The scale of these impacts will be directly related to the extent to which the policy promotes housing and economic growth. But in practice, such impacts will still be the subject of nation guidance which seeks to minimise their scale, such as environmental impact assessments (EIA) and strategic environmental assessments (SEA).

Social impacts

Local authorities will be overseeing the quantity, type and location of development where they deem necessary, thus responding to and meeting local needs. This could lead to positive social impacts.
It is not anticipated that there will be any adverse impacts in terms of health/human well-being, human rights or the justice system.

Rural proofing

There could be concern that with a potential increase in development, there could be adverse impacts on development in rural areas and of Greenfield land. However, the risks are mitigated given that local authorities determine the quantity, type and location of housing development. Furthermore, Green Belt (PPG2) protection will remain and locally-led plans will provide a framework for where development should go following the abolition of regional spatial strategies (giving local communities greater control over where units are delivered). Therefore, it is not anticipated that there will be any adverse impacts on rural areas.

Sustainable development

It is not anticipated that this policy will have any negative impact on sustainable development. With communities able to play a greater role in decisions over local development it is possible there will in fact be a positive impact on sustainable development.

Annexes

Annex 1 should be used to set out the Post Implementation Review Plan as detailed below. Further annexes may be added where the Specific Impact Tests yield information relevant to an overall understanding of policy options.

Annex 1: Post Implementation Review (PIR) Plan

A PIR should be undertaken, usually three to five years after implementation of the policy, but exceptionally a longer period may be more appropriate. A PIR should examine the extent to which the implemented regulations have achieved their objectives, assess their costs and benefits and identify whether they are having any unintended consequences. Please set out the PIR Plan as detailed below. If there is no plan to do a PIR please provide reasons below.

Basis of the review: [The basis of the review could be statutory (forming part of the legislation), it could be to review existing policy or there could be a political commitment to review]; The Government is committed to the success of the New Homes Bonus and will monitor its impacts closely. We will formally consider the impact of the scheme in 2013/14 in preparation for the 2015-16 spending review.
Review objective: To assess the impact that the New Homes Bonus has in changing behaviours at the local level in favour of appropriate housing development.
Review approach and rationale: To be determined.
Baseline: The baseline of new housing supply (net additions) and the composition of that supply (by type, location and size).
Success criteria: To be determined.
Monitoring information arrangements Existing data collection arrangements will form part of the information monitored as part of any review, along with other evidence.
Reasons for not planning a PIR: N/A

Technical annex

Methodology – financial effects

1. We can't know how local authorities will behave in response to the New Homes Bonus, but we can consider a range of strategies they could adopt and assess the implications for housing delivery. This means, for the purposes of the impact assessment, we can set out a range of outcomes that reflect the different strategies that local authorities may adopt.

CONTEXT

2. Each local authority faces a budget constraint (LGF allocation), which implies a trade-off: spending on existing households versus spending on new households. As more homes are built, a given allocation must be spread more thinly over a larger number of households.

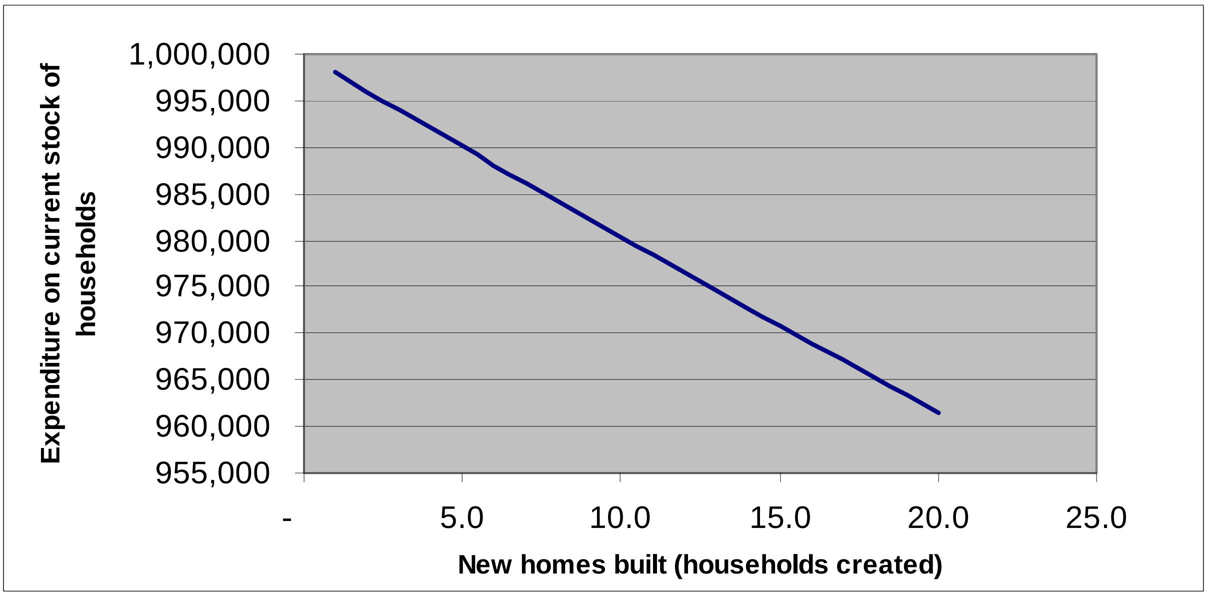
3. This highlights a problem with the current system: allocations are backward-looking and do not quickly adjust for household growth, which acts as a disincentive to growth.

4. A local authority's strategy, in response to the New Homes Bonus, may depend on a range of factors, including how much it values spending on existing households versus spending on new households.

5. The chart below is illustrative. For a £1,000,000 allocation, a local authority can choose different rates of new build. If it chooses to build five new units, then expenditure on existing households is reduced from £1,000,000 to £900,099.

6. The slope of the budget line is a function of the income allocation (M), the existing stock of households (n) and new homes built (X1): -M/(n+X1) (which in absolute terms equals spend per household). If there are 500 households, then a build rate of five net additions means that spend per household equals £1,980.

7. Spend per household is higher at lower build rates because a given income allocation is spread across a fewer households. If net additions are zero, spend per household equals £2,000; if net additions are 10, spend per household equals £1,961.



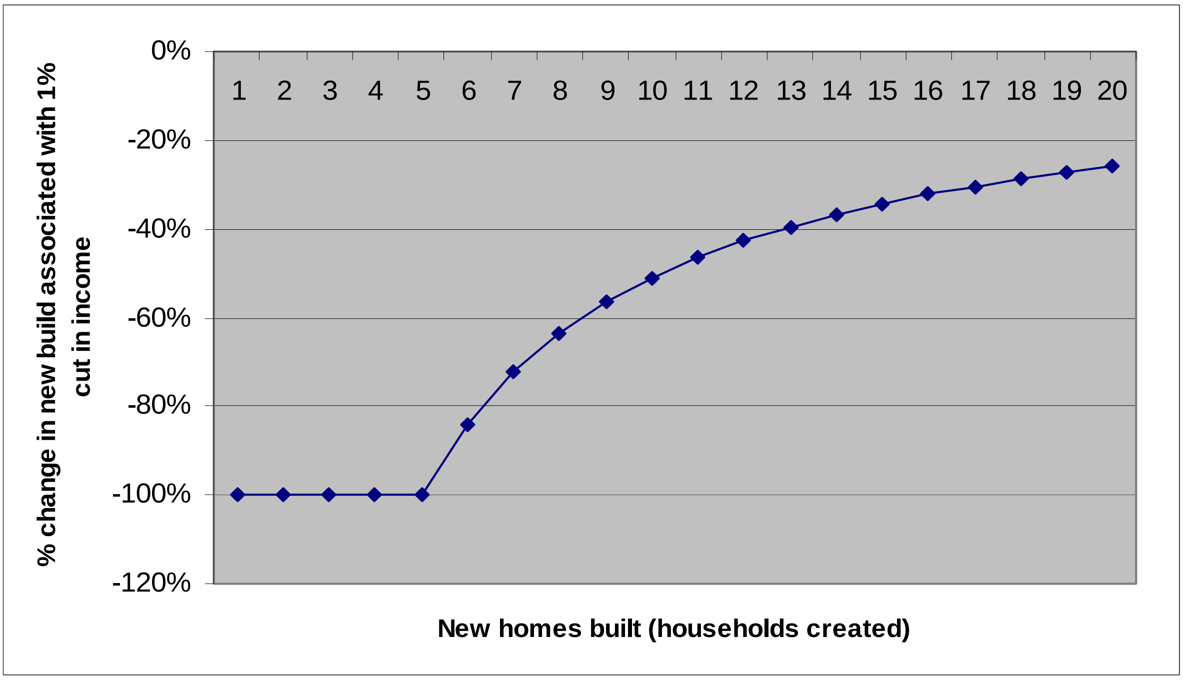
8. **Introduction of New Homes Bonus**. There are two elements we need to take into account. The first is a negative income effect associated with the money taken from formula grant. The second is an effect (positive or negative) associated with the per unit New Homes Bonus subsidy.

9. **Strategy 1**. Maintain initial spend per household.

   - all authorities attempt to maintain spend per household by reducing their build rate

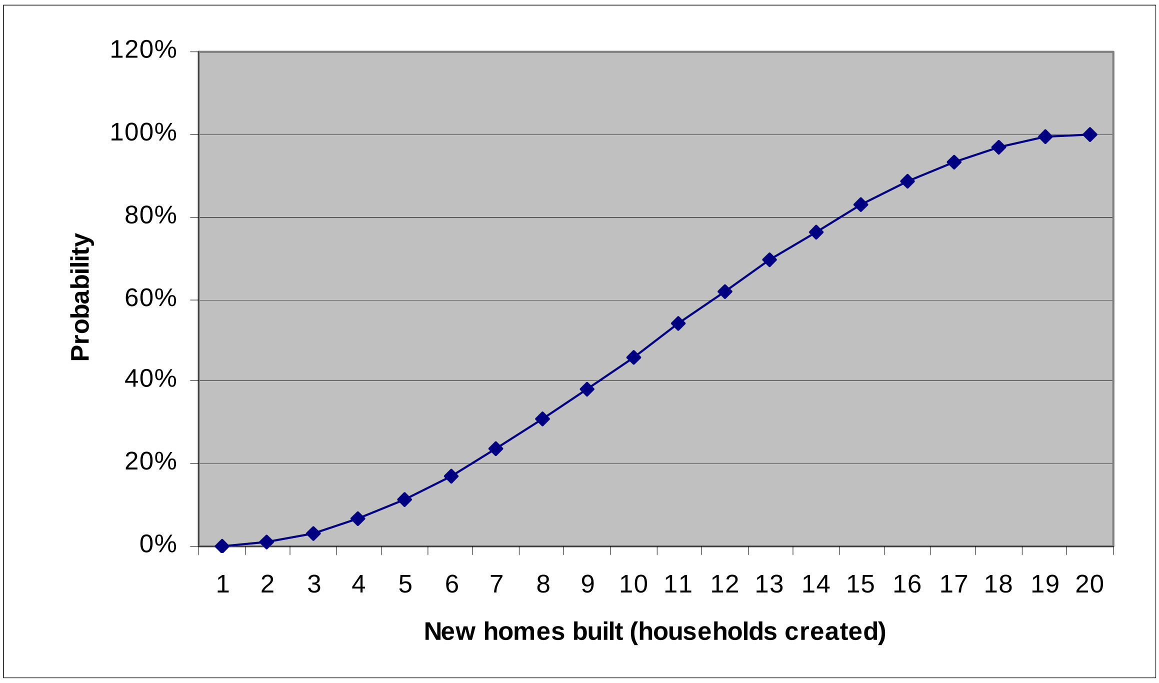
   The scale of the effect depends on the current build rate and the amount of money taken from formula grant (percentage reduction). In terms of the former: on the one hand, (a) a lower initial build rate means a higher initial level of spend per household (other things being equal) so that net additions must fall by more (in percentage terms) to maintain it. In other words, the elasticity of net additions with respect to income is inversely related to the initial build rate. On the other hand, (b) we think that the feasibility and likelihood of this strategy may be either positively or negatively related to the build rate.

   For every local authority we estimate the income elasticity of net additions with respect to income associated with maintaining initial spend per household. The chart below is illustrative. The maximum income elasticity is constrained to 100 per cent because we assume that net additions do not fall below zero[16].

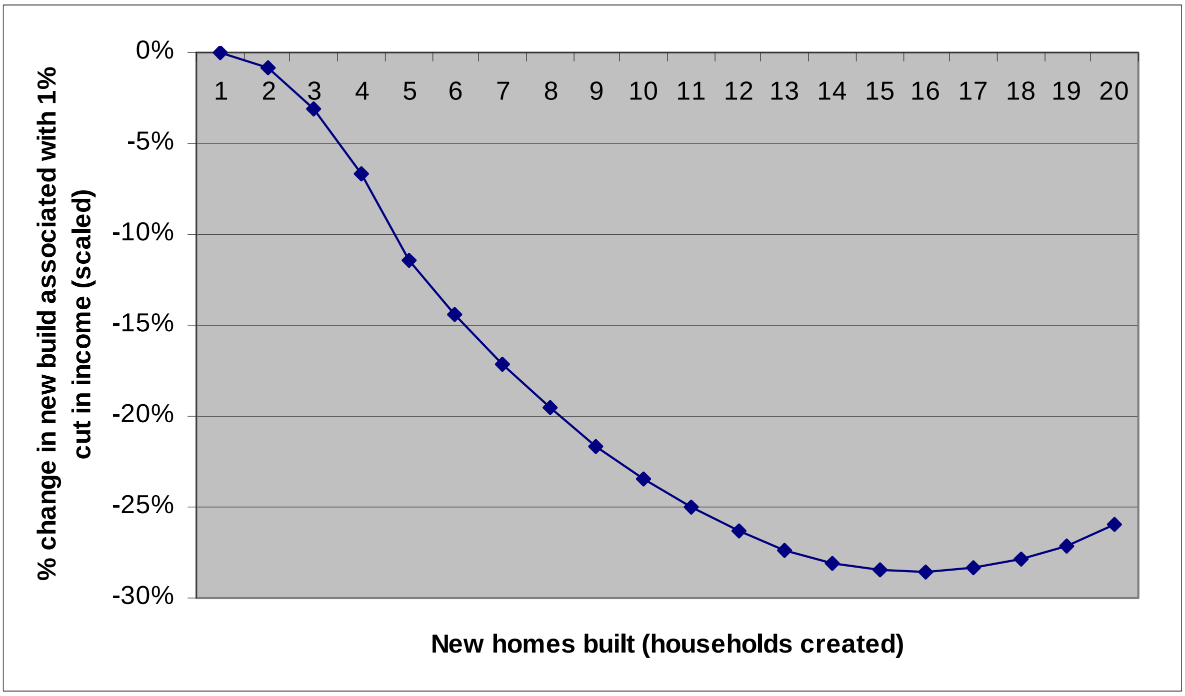


   The elasticity estimates are then scaled by a probability (between 0 and 1) to reflect point (b). The chart below is illustrative and shows that the probability of implementing the strategy (maintaining initial spend per household) rises (declines) at higher (lower) build rates. Alternatively we consider the opposite, where the probability of implementing the strategy declines (rises) at higher (lower) build rates.

[16] Net additions can feasibly be negative, but we rule out the possibility that a local authority could or would actively pursue negative net additions in order to maintain a desired level of spend per household.



Finally, the scaled elasticity estimates are applied to the amount taken from formula grant in order to estimate the impact on net additions. For illustration, at an initial build rate of 1 unit, the effect of a 1 per cent reduction in formula grant is -1 per cent*100 per cent*0 = 0; at an initial build rate of 20, the effect is -1 per cent*26 per cent*1 = -26 per cent (fall in net additions). The chart below is illustrative (and consistent with the previous two charts).



'NHB subsidy'. This may be a positive or negative effect. We assume:

- 'Winners' build fewer homes. 'Winners' are local authorities whose spend per household would increase i.e. the subsidy that would be paid out at the initial build rate would more than offset the amount taken from formula grant.
- 'Losers' build more homes. 'Losers' are local authorities whose spend per household would decrease i.e. the subsidy that would be paid out at the initial build rate would less than offset the amount coming from formula grant.

The scale of the effect depends on the size of the 'per unit' subsidy (relative to the amount coming from formula grant) and the current build rate. In terms of the latter: on the one hand, (a) a lower initial build rate means a higher spend per household (other things being equal) so that net additions must rise (or fall) more (in percentage terms) to maintain the initial spend per household. On the other hand, (b) the feasibility and likelihood of this strategy is likely to vary with the initial build rate. As with the amount coming from formula grant, we can either assume feasibility and likelihood is positively related or negatively related to the initial build rate.

10. **Strategy 2.** Same as strategy 1 except 'winners' maintain rather than reduce their build rate. Only losers react to the NHB, by increasing their output in order to try to maintain initial levels of spend per household.

11. **Strategy 3.** Same as strategy 2 except some winners, namely those who are 'pro growth' do not maintain or reduce their build rate; rather they attempt to 'go for growth'. This category of local authorities is termed 'pro winners'.

12. We assume 'pro winners' try to increase their total income (M) by X per cent (relative to their initial allocation). This may lead to an increase or decrease in spend per household.

13. It should be noted that all the strategies describe what local authorities try to do, but what they achieve is constrained in two main ways:

- As described earlier, local authorities' income elasticities are constrained to reflect feasibility and likelihood. We assume a range of probabilities between zero and 1.
- Secondly, every local authority is constrained in its behaviour to an overall change in net additions by +30 per cent or -30 per cent.

Department for Communities and Local Government

ISBN: 978 1 4098 2612 5