Centre for Policy Studies

Pointmaker

DOWN WITH DEPOSITS: THE CASE FOR RENTAL INSURANCE

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EXECUTIVE SUMMARY

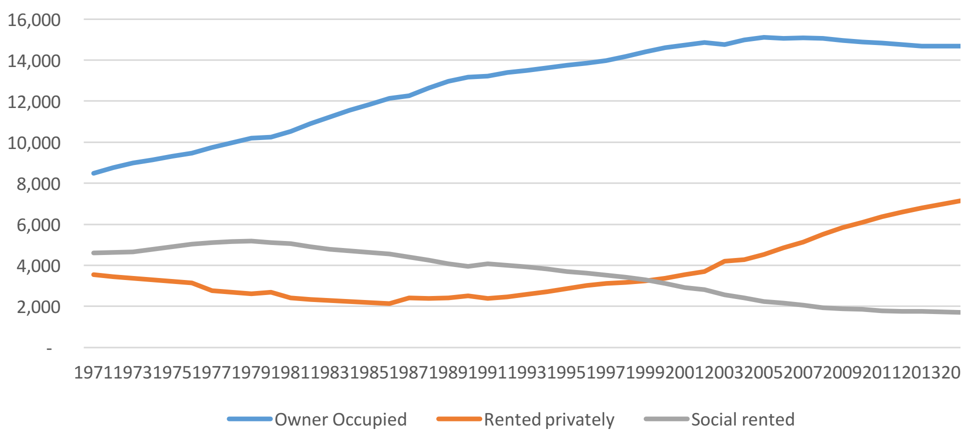
- In 2017, 4.79 million households, or 20.0 per cent of English households, were in the private rental sector. This number has been growing rapidly.
- While the only lasting solution to the housing crisis is to increase home ownership, the Government should also do what it can to help renters.
- The current mandatory deposit protection scheme is unfair, inefficient, wasteful and creates a risk of fraud. It also stops people from moving and is a barrier to younger people without affluent parents being able to rent.
- The draft Tenant Fees Bill published in November aims to scrap letting agents' fees and puts a maximum cap of six weeks on tenancy deposits. But this ignores the issue of the deposits themselves, which represent a far greater cost to tenants.
- This paper proposes that insurance-based options, involving lower up-front costs for tenants, should be promoted as a genuine alternative to the existing deposit system.
- Independent YouGov polling for this paper shows that a slight majority of tenants would prefer such a policy to deposits.
- The Government should incentivise competition and consumer choice via a package of measures to ensure that deposit schemes and insurance are equally viable.
- In the process, ministers would help make the lives of Generation Rent that little bit easier.

1. THE RETURN OF THE LANDLORD

The housing crisis is one of the greatest domestic policy challenges facing the Government. It has been driven by a failure to build enough homes, by the falling affordability of those homes that are available, and by changes in the balance of homes by tenure type.

Data from the Office for National Statistics shows how rapidly the nature of household tenure has changed in the last 25 years. Between 1992 and 2017, the number of households in England grew by 4.11 million.[1] But the number of owner-occupied households increased by only 1.67 million, just over forty per cent of the growth – and has been flat or falling for most of the past decade.[2]

Chart 1: Tenure patterns over time[3]



By contrast, the number of households in public housing fell by 2.34 million. But the rental sector (including privately registered providers such as housing associations) has risen dramatically, soaring from 2.52 million households in 1990 to 7.23 million in 2017, just under a third of the total.[4] Part of this rise is due to housing associations, which have grown steadily from 420,000 households in 1981 to 608,000 in 1991 then 2.44 million by 2017, or 10.2 per cent of all homes.[5]

But there has also been a stunning reversal in the numbers of private landlords.

During the 1980s, around 10 % of all households were privately rented.[6] This declined to around 9 per cent by 1991, as the property market expanded and government actively promoted the property-owning democracy. But from 1992 the sector rebounded, rising at an annual average rate of 0.42 per cent to reach 20.0 per cent of households by 2017.[7]

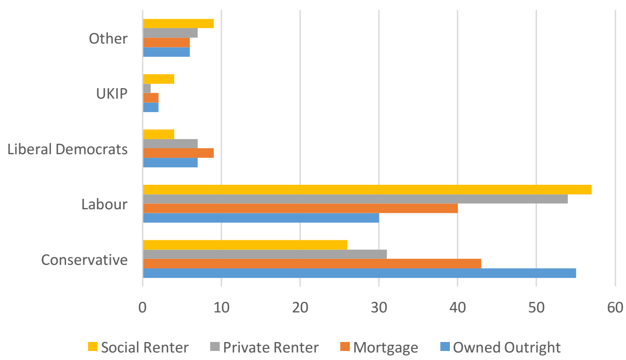
1. MHCLG. Live tables on dwelling stock (including vacants). Table 104: by tenure, England (historical series). https://www.gov.uk/government/statistical-data-sets/live-tables-on-dwelling-stock-including-vacants
2. Ibid.
3. Ibid.
4. Ibid.
5. Ibid.
6. Ibid.
7. Ibid.

This rise did not immediately impact on the owner occupied sector, which reached a peak of 15.1 million households in 2005.[8] But since then, the growth of the private rental sector has come mainly from households unable to gain tenure in a declining social housing sector, or squeezed out of an increasingly unaffordable owner-occupied sector. In other words, even as household numbers have grown (at an average rate of 0.8 per cent since 2005), fewer individuals have been stepping onto the housing ladder.[9]

These overall figures, however, mask a sharp generational divide. Younger people have always been overrepresented in the private rented sector, but the proportion of younger renters has increased markedly over the past 10 years. According to a recent Ministry of Housing, Communities and Local Government (MHCLG) housing survey, the proportion of those aged 25 to 34 living in the private rented sector rose from 24 per cent in 2005-6 to 46 per cent in 2016-17.[10] At the same time, the proportion living in owner occupation fell from 56 per cent to 37 per cent, while the proportion of the group living in the social housing sector fell from 20 per cent to 17 per cent.[11]

This has, inevitably, become a major political issue. In the 2017 general election, whether someone rented vs owning a home was an even better predictor of whether they voted for Labour or the Conservatives than their age. An Ipsos MORI poll of 7,505 people showed that the Conservative Party had a lead of 25 percentage points over Labour among owner-occupiers without a mortgage, and 3 points among those with a mortgage, but a deficit of 23 percentage points among private renters.[12] Such data showed a massive swing away from the Government among "Generation Rent", especially those on low incomes. It is clear many renters are unhappy with the current situation.[13]

Chart 2: Voting by tenure, 2017 general election[14]



8. MHCLG. Live tables on dwelling stock (including vacants). Table 104: by tenure, England (historical series). https://www.gov.uk/government/statistical-data-sets/live-tables-on-dwelling-stock-including-vacants
9. Ibid.
10. MHCLG. English Housing Survey 2016 to 2017: headline report. Section 1 household tables: Annex Table 1.4 https://www.gov.uk/government/statistics/english-housing-survey-2016-to-2017-headline-report,
11. Ibid.
12. Ipsos MORI. How Britain voted in the 2017 election. https://www.ipsos.com/ipsos-mori/en-uk/how-britain-voted-2017-election
13. Shelter Blog. Housing and the 2017 election: what the numbers say. http://blog.shelter.org.uk/2017/06/housing-and-the-2017-election-what-the-numbers-say/
14. Ipsos MORI. How Britain voted in the 2017 election. https://www.ipsos.com/ipsos-mori/en-uk/how-britain-voted-2017-election

Much of the ensuing debate has focused on the need to rekindle home ownership – which is certainly a priority area for the Centre for Policy Studies. But the conditions of tenure in the private rental sector, and the associated costs, have become increasingly important to a rising number of young people.

Labour have responded to this issue by proposing, essentially, rent controls – an appealing-sounding but economically illiterate measure that would, based on every other time it has been tried, do far more harm than good. (For example, it would likely restrict the supply of private rental accommodation, thereby exacerbating the problem it is meant to solve.)

The Conservatives' policies on private rental are less dramatic, including greater sanctions for bad landlords and build to rent guarantees. In November 2016, the Chancellor announced that the Government will ban the practice of charging tenants letting agents' fees.[15] The resulting legislation was published in November 2017 as the Draft Tenant Fees Bill.[16] This not only plans to ban agents' fees, estimated at an average of £350 across the country, but also to cap deposits at a maximum of 6 week's rent.[17]

This paper will argue for a wider reform. Instead of costly deposits – which Labour made compulsory in 1998 - tenants should have the option of paying for insurance when they rent a property. This move would save Britain's renters an average of £1041 in upfront costs,[18] while offering property investors significantly improved asset protection – at no cost to the Treasury. It would also make life easier for Generation Rent.

2. THE TROUBLE WITH DEPOSITS

The main cost faced by a potential tenant in the private rental sector is not any fee charged by an agent, but the size of the deposit required as security. In the United Kingdom, this is usually set as a multiple of the weekly or monthly rental payment and retained for the duration of the tenancy.

In June 1998, a report by the National Association of Citizens Advice Bureaux (NACAB) claimed that many private tenants who paid a rental deposit had difficulty getting it back from their landlord, and that the case for reform was "overwhelming."[19]

A two-year pilot scheme was launched in 2000 by John Prescott. This was followed by the 2004 Housing Act. Under the legislation, any landlord or letting agent that takes a deposit for an assured shorthold tenancy (usually up to 1.5 times the monthly rent) must protect the deposit in an authorised tenancy deposit scheme.

15. HM Treasury. Autumn Statement 2016. https://www.gov.uk/government/publications/autumn-statement-2016-documents/autumn-statement-2016
16. MHCLG. Draft Tenants Fees Bill. https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/656275/Cm_9529_Tenant_Fees_Bill_print.pdf
17. Ibid. p17
18. Tenancy Deposit Scheme Statistical Briefing: UK Tenancy Deposit Statistics (October 2016). https://www.tenancydepositscheme.com/resources/files/UK%20Tenancy%20Deposit%20Statistics.pdf
19. House of Commons Library. Tenancy Deposit Schemes. http://researchbriefings.parliament.uk/ResearchBriefing/Summary/SN02121#fullreport p3

Originally, three separate schemes were set up to encourage competition, but all three now operate in an essentially identical fashion, offering both “custodial” and “insured” schemes (see below). These schemes now cover approximately £4.1 billion in deposits.[20]

How the scheme works

There are now three authorised schemes in operation, the Tenancy Deposit Scheme (TDS), the Deposit Protection Scheme (DPS) and MyDeposits – all operating under licence from the Ministry of Housing, Communities and Local Government (MHCLG). The relative size of these three schemes are shown in Tables 1 and 2.

The money deposited by the tenant with a landlord or letting agent must either be held in one of two ways: a Custodial Model or an Insurance Based Model.

Table 1: Total number of deposits protected by scheme[21]

	As at March 2015
TDS	1,135,769
MyDeposits	738,853
DPS	1,170,564
DPS Insured	20,944
Total	3,066,130

Table 2: Average value of deposits protected by scheme[22]

	As at March 2015
TDS	£1181
My Deposits	£1,097
DPS	£867
DPS Insured	£1024
Total	£1040

Custodial: Custodial deposits, which currently account for roughly a third of total deposits, or £1.3 billion, involve agents and/or landlords transferring a tenant’s funds over until the end of the tenancy. The landlord pays no fee: instead, the schemes are funded by the interest earned on the deposits.

Insurance-based: Under the insurance-based scheme (currently accounting for the other two thirds) the deposit money is retained by the landlord, who pays an insurance fee to the scheme. The money is meant to be held by the landlord or letting agent in a segregated customer account, but there is no system to ensure that this happens.

20. Tenancy Deposit Scheme Statistical Briefing: UK Tenancy Deposit Statistics (October 2016). https://www.tenancydepositscheme.com/resources/files/UK%20Tenancy%20Deposit%20Statistics.pdf

21. TDS. Tenancy Deposit Protection in England & Wales: a digest of statistics to March 2015. https://www.tenancydepositscheme.com/resources/files/TDS__Statistical__Digest__at__March__2015.pdf p8

22. Ibid.

If there is a dispute at the end of the tenancy, concerning alleged damage or other issues, the agent/landlord and tenant are urged to make use of Alternative Dispute Resolution (ADR), a free and impartial "sounding board" comprised of property professionals such as solicitors and inventory clerks. The ADR evaluates evidence from both parties and reaches a judgment.

The purpose of the insurance payment is not, as many assume, to protect against the tenant's money being appropriated by the agent or landlord – it is solely to reimburse the tenant if the ADR finds in their favour, but the agent/landlord withholds the disputed funds.

At present the largest deposit scheme – Tenancy Deposit Scheme – charges a fixed rate of £16 for deposits up to £500 and £23 for deposits greater than £500. The others' charges are broadly similar. (See Table 3).

There are discounted rates for members of partner organisations, such as the Association of Residential Letting Agents (ARLA) – but it is also worth pointing out that some organisations such as the ARLA and National Landlords Association (NLA) own shares in the deposit schemes and only offer those schemes to their members. This raises concerns of a conflict of interest within their professional role.

The case against the deposits system

The current deposits system, is unfair, inefficient, wasteful, and subject to the risk of fraud.

1. Rental deposits are unfair: The system is unfair for several reasons. First, consumers miss out on interest earned on their money. During that period, the two thirds of landlords or agents using the insurance scheme can earn interest on the money, despite it not actually being theirs.

Admittedly, the law states that interest can only be kept by the agent if it is written into the tenancy agreement. But in practice, under the insurance schemes any interest generated is simply kept by the agent or landlord. And any tenant who questioned the terms related to interest would more than likely not be allowed to proceed with the tenancy.

The sums involved may not seem that large. But from the landlord's point of view, they can soon add up, given the volume of properties owned or managed by some of the larger operators – and, more importantly, the potential leverage obtainable against the deposits.

Table 3 Deposit insurance rates charged

	Deposits under £500		Deposits Over £500	
		*Discounted		*Discounted
TDS[23]	£16.00	£13.20	£23.00	£17.95
DPS[24]	£15.00	N/A	£22.20	N/A
MyDeposits[25]	£20.00	£14.00	£26.00	£18.20

23. TDS. Join the Tenancy Deposit Scheme for Landlords. https://www.tenancydepositscheme.com/landlord-membership-fees.html
24. DPS. https://account.depositprotection.com/documents/the-dps-rules-out-membership.pdf p1
25. MyDeposits. How mydeposits works for landlords. https://www.mydeposits.co.uk/landlords/how-it-works/

According to TDS, the largest deposit scheme, the average deposit covered under the insurance-based schemes is £1,361, substantially higher than the average custodial deposit of £997.[26]

A letting agent managing 5,000 tenancies on an insurance basis would, assuming they reflected that average, be holding £6.8m in deposits and earning interest on such sums. There are also economies of scale, which would encourage companies. For example, TDS offers negotiable premiums for companies (but not individuals) holding more than £100,000 of tenancy deposits and with total assets over £25 million.

Second, consumers actually lose money. At an estimated inflation rate per annum of 2.5 per cent, and an interest rate of 3 per cent, a tenant will end up foregoing a substantial amount of their deposit over a five-year period. That means that if you put down a deposit of £1,041 (approximately the national average), there would be a total loss of £320 over those five years, including not just the headline financial loss in foregone interest but the utility loss via inflation as a consequence of the confiscation of your wealth.[27] If interest rates were to rise higher, the losses would be even higher.

Third, rental deposits lock up people's cash, and prevent them from moving.

Average tenancy deposits are, obviously, a function of property values and rental rates: according to TDS, they range from £498 in the Ribble Valley in Lancashire to £3,266 in the City of London.[28] But when a tenant tries to move from one rental property to another, they are usually required to find their next deposit before having their current deposit returned.

The sums involved can, for those involved, be extremely significant. Research by the University of Bristol has discovered that 31 per cent of people in privately rented accommodation and Housing Association properties have less than £100 in the bank. This compares to 11 per cent of people who own their home outright.[29] And according to the English Housing Survey, renters are already devoting a substantial amount of their income to paying the bills: those in London spent 45 per cent of their income on rent, and those outside it an average of 32 per cent.[30]

In other words, for many within the private rental sector, it is already a struggle to pay the rent for their existing property, let alone to build up a deposit (generally equivalent to six weeks' rent) for another. If they do move, they may therefore need to rely on payday lenders, who will charge exorbitant rates of interest. They will also be subject to credit and reliability audits, whereas the landlord will not.

26. TDS Annual Review: 2016-2017. https://www.tenancydepositscheme.com/resources/files/Annual__Review__DIGITAL.PDF p5
27. Average figure from Tenancy Deposit Scheme Statistical Briefing: UK Tenancy Deposit Statistics (October 2016). https://www.tenancydepositscheme.com/resources/files/UK%20Tenancy%20Deposit%20Statistics.pdf. In terms of the total amount, when counting forward or back in time it is usual to only use the rate of interest. However, this is done when people are voluntarily choosing to save. In this case, the cost is the lost interest, but also the fact that the tenant has been forced to defer consumption from point A to point B rather than choosing it. Forced saving is very different to voluntary saving and the utility lost is therefore greater. There is a major difference between choosing to save and someone confiscating your money and then giving it back to you in several years' time – clearly the second is worse than the first, and so we use lost interest and inflation, since just using interest erroneously implies they are equivalent.
28. TDS Annual Review: 2016-2017. https://www.tenancydepositscheme.com/resources/files/Annual__Review__DIGITAL.PDF p7
29. Momentum UK. Household Financial Wellness Index: 2017 p18
30. DCLG. English Housing Survey: Housing costs and affordability, 2015-16. https://assets.publishing.service.gov.uk/government/

2. Rental deposits are inefficient: Renting a property carries with it a very high transaction cost – typically between 1 to 1.5 times the monthly rent. This is far higher than with any other class of asset – and bears no relation to the individual's track record as a tenant, or indeed to the actual level of risk to landlords.
The entire architecture of the current system is built around the need to resolve disputes between landlord and tenant. Yet the rate of disputes between landlords and tenants over withheld deposits is pitifully small: current figures show only a 1.6 per cent rate.[31]

Economically speaking, there is a misallocation of resources here. The money sits in agents', landlords' or custodial bank accounts, but is subject to the risk of disputes, fraud and theft. And the excessive transaction costs imposed by the system reduce the efficiency of agents in matching the supply of and demand for rented accommodation.

The existing system not only generates transaction costs which reduce the efficiency of the private rental sector, but effectively freezes billions of pounds for tenants, being eroded by inflation, while earning interest for landlords.

3. Risk of fraud: The system creates a risk of fraud from unscrupulous landlords and agents stealing or misusing client moneys. In 2016, according to a BBC report, more than £1 million was appropriated from deposit schemes by rogue agents.[32] The recent conviction of a letting agent who stole £15,000 worth of tenancy deposits took the total value of deposits that were known to be stolen to £850,000 by the third quarter of 2017.[33] In addition, there is anecdotal evidence of some landlords exploiting their position of power and making unreasonable demands on tenants before handing back only a limited amount of the deposit - demands tenants will agree to given that moving is, as described above, often associated with wider cashflow issues.

3. THE CASE FOR RENTAL INSURANCE

The 2004 legislation made deposit schemes mandatory in order to reduce the risk that a) landlords would set, and keep, excessive deposits and b) tenants would damage landlords' properties. It was also intended to minimise landlords' transaction costs, so as to ensure an adequate supply of private rental accommodation.

Yet given the small number of tenancies that end in dispute (an average 1.6% of deposits in tenancy deposit protection scheme end up in a dispute)[34] this has created an unwieldy sledgehammer to crack a very small nut. Other data however, for example the English Housing Survey, suggests a much higher level of issues around deposits, with only 62% of those surveyed saying that they had their deposit returned 'in full', with 23% having it returned in part, 10% not having it returned and 4% unable to say. This means over a third of tenants did not see their deposit returned in full. This however

31. Tenancy Deposit Protection in England & Wales: a digest of statistics to September 2013.
https://www.thedisputeservice.co.uk/resources/files/Tenancy%20Deposit%20Protection%20A%20Digest%20of%20Statistics.pdf
32. https://www.bbc.co.uk/news/uk-england-cornwall-38958848
33. http://www.dlighted.co.uk/cash-deposits-stolen-letting-agents-landlords-october2017/
34. Tenancy Deposit Protection in England & Wales: a digest of statistics to September 2013.
https://www.thedisputeservice.co.uk/resources/files/Tenancy%20Deposit%20Protection%20A%20Digest%20of%20Statistics.pdf

was under the current system, suggesting that the currently heavily regulated system is not necessarily to tenant's advantage.[35]

The problem is essentially one of asymmetric information. In a world where you know nothing whatsoever about your prospective tenant, it makes sense to demand a deposit up front. But this is not the world we live in.

As of June 2017, one large landlord, Get Living, has scrapped security deposit requirements for new residents – and is also returning security deposits to current residents, in a move that will see around £3 million released.[36]

Launched in May 2013, Get Living is behind the country's largest single-site PRS scheme at the former athletes' village for the 2012 Olympics, now called East Village, E20, and home to more than 3,000 renters in 1,439 homes. The firm has a further 4,000 homes in the pipeline across the UK.[37]

Under the new arrangements, new residents who successfully pass referencing or have a guarantor will have no security deposit to pay. To reward residents who have taken good care of their home, if rental payments are up to date, Get Living will not only refund the deposits, but waive any damage and cleaning costs if they total less than one week's rent.[38]

This is admirable. But it does rely to a large extent on transferring the tenancy risk to guarantors - usually the tenants' parents - who are rich enough and supportive enough.

But what if we turned to the insurance market? Under this system, you could have a variety of options. Either you could pay a higher premium to be covered against any non-fundamental damage to the property and non-payment of rent. Or you could go for lower-cost credit insurance that meant you were still liable for any damage or unpaid rent at the end of the tenancy, but were not required to fund a full deposit when you moved in.

Unlike the current mandatory system, which licences a limited number of deposit-taking bodies, market competition from a number of providers would expand the choice available to tenants and landlords. It is worth noting that this system would not only replace what is currently covered by deposits, but that such insurance could provide property investors with much more comprehensive protection against damage or non-payment of rent than just the limited deposit protection currently on offer, especially with the inherent risk-pooling possibilities of insurance markets.

Furthermore, the sector can be regulated more efficiently and effectively than the current mandatory deposit schemes, by using the Financial Conduct Authority as a proxy.

35. DCLG. English Housing Survey: Private Rented Sector Report 2014-15. https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/570848/Private_Rented_Sector_Full_Report.pdf
36. http://www.getliving.com/pressmedia/major-uk-landlord-scraps-rental-deposits
37. Ibid.
38. http://www.getliving.com/news/no-more-deposits-when-renting-get-living

Some landlords and letting agents are already experimenting with this model. A new company, Dlighted,[39] allows the landlord, agent or tenant to purchase an insurance policy instead of taking a deposit. Another company, Zero Deposit,[40] launched early in 2018, backed by the listed online property valuation company Zoopla.

These schemes allow the tenant to pay a much smaller upfront fee to gain the protections that regulated insurance products provide, typically one week's rent rather than six.

Replacing the current deposit scheme with mandatory insurance, taken out by landlords and/or tenants, will over time result in a truer assessment of the relative risks borne by both parties. Tenants with a track record of prompt payment and limited damage claims could pay lower premiums, as would landlords and agents who managed their properties well.

Table 4 evaluates the cost of this insurance model vs deposits. As can be seen, there is no upfront cost for insurance, unlike the large rental deposit required. We have assumed an average rental deposit value in England and Wales and for the cost of insurance, have used a typical comparison website's average figures, plus inflation as the lost consumption foregone, rather than seeing this as a depreciating asset. As a further incentive to adopt the insurance based-model, it is proposed that the Government could offer an exemption from Insurance Premium Tax, which levies a standard rate of 12% on all transactions.[41]

The headline cost of the insurance model would be approximately £556, assuming no tax was payable on an average content and rental guarantee insurance policy. This is higher than the eventually losses incurred on a deposit,

Table 4: Cost of Insurance vs deposit for private rental tenants

Insurance (£)

	Upfront Cost	Year 1	Year 2	Year 3	Year 4	Year 5	Total
Contents Only Insurance[42]	0	64.51	64.51	64.51	64.51	64.51	322.55
Rental Guarantee[43]	0	60	60	60	60	60	300
Sum of Insurance minus IPT	0	112.20	112.20	112.20	112.20	112.20	556

39. http://www.dlighted.co.uk/
40. https://zerodeposit.com/
41. HM Revenue & Customs. Insurance Premium Tax: guide for insurers. https://www.gov.uk/guidance/insurance-premium-tax
42. Calculations based on quote for Limited Landlord Contents Insurance. HomeLet.
Available at: https://homelet.co.uk/landlord-insurance/products/landlord-liability-insurance
43. Calculations based on average price of rent guarantee insurance. Alan Boswell.
Available at: https://boughtbymany.com/news/article/how-much-does-landlord-insurance-cost-uk/

whether the direct cost in lost interest or the inflation loss due to forced saving. However, the tenant might well be happy to pay this extra amount, especially over an extended period, in order to avoid locking up a deposit of £1041 over the five-year horizon. This is particularly pertinent if at the start of this period, such money is a large sum (which is going to be true if this is paid by someone just starting work) coupled with the risk that the deposit may not be fully repaid at the end of the tenancy.

The insurance scheme has other advantages. Apart from a credit rating and income checks, which are often incomplete, landlords know little about the likely behaviour of tenants. If tenants took out the insurance policy, there could be a rating system similar to the no-claims bonuses in car insurance, which identify and reward good tenants. Being able to identify the best tenants would also reduce the time between a property's release on the rental market and the finding of a suitable tenant. This would improve the cash yield to landlords while making the rental market more efficient and equitable for tenants.

There would also be a broader economic benefit. Many of those in the rental market are currently not registered by credit reference agencies like Equifax, Experian etc – or the data received is only fragmentary. If people want to get on to the mortgage ladder, having a solid record as tenants and rent-payers could greatly help their chances. Currently, however, there is a fragmented market where many systems have been adopted by operators in the PRS, and reporting of rent payments to the reference agencies is not permitted by non-FCA regulated members.

Deposit reform would be low-cost and it would release frozen funds back into the economy. It would require no additional regulatory oversight but improve the current safeguards and would assist landlords and tenants while providing a strong signal that the issues faced by Generation Rent can be addressed with a lightly regulated market-based solution.

Many people would choose insurance over a normal deposit

To test the theory that many people would choose insurance over a normal deposit, we asked YouGov to run polling on the two options, with the insurance costing one week (as is the standard in the current experimental products) and the deposit costing six weeks, but with the deposit being returned minus any damage. We found that 43% of people would prefer insurance, more than the 41% who chose a deposit. If you exclude the 16% who said "don't know" this split was 51-59%.

Given the 4.79 million households in the sector,[45] this means that more than two million of them would choose to use an insurance policy if they could – a massive market and substantial number of people whose needs are not being met at present.

44. Tenancy Deposit Scheme Statistical Briefing: UK Tenancy Deposit Statistics (October 2016). https://www.tenancydepositscheme.com/resources/files/UK%20Tenancy%20Deposit%20Statistics.pdf

YouGov polling data

Imagine that, when renting a home, you have the choice of either paying a deposit to the landlord (usually the equivalent of 6 weeks' rent, which would be returned at the end of the tenancy minus the cost of any damage) or paying for deposit replacement insurance (usually the equivalent of 1 week's rent, where you are still responsible for any damage at the end of the tenancy, but don't have to find the full deposit). Which would you prefer?[46]	
To pay a deposit	*41%*
To pay for deposit replacement insurance	*43%*
Don't know	*16%*

4. HOW CAN GOVERNMENT SUPPORT THIS?

For some tenants, the existing deposit system may work well – and in a free market, there should not be compulsion. But for many, especially new renters, or those who have limited cash available, a deposit is not a helpful way forward.

The Government should therefore support the emergence of a genuine market so that people have a choice between insurance and a deposit.

There are already some firms who are experimenting with such products. But the 2004 Act means that the "deposit replacement" market is still in need of protection and promotion.

For example, as the "deposit replacement" market develops, it could attract unscrupulous operators, who provide products to tenants and landlords that do not come with the protections usually associated with fully FCA-regulated insurance products.

Given the unregulated nature of the letting agent sector, and the implication that unregulated products may offer a more attractive commercial proposition to letting agents and landlords, there is a risk that problems could develop unless the necessary protections are put in place. By ensuring that only FCA-regulated products are permitted, government can go a long way to ensure that a new, sustainable model can be established rather than risking an unscrupulous insurance provider preventing this model growing.

With this in mind, we propose that:

- The Government should champion the option of tenant insurance as a realistic option.
- The Government should look at how it could amend or change the 2004 Housing Act to allow for free-market solutions.

45. https://www.gov.uk/government/statistical-data-sets/live-tables-on-dwelling-stock-including-vacants Table 104
46. YouGov/CPS Survey for this paper Results – Sample size 745 GB Adults who privately rent, fieldwork 11-14th June

- The government could further support "Generation Rent" by offering an exemption from Insurance Premium Tax (IPT) for tenant insurance, which currently stands at 12% on all transactions. This would help create a level playing field between the deposit and insurance options. Because the insurance sector for tenants is so small, the cost of this would be negligible.
- The Government should make access to the Private Sector Rented Guarantee Scheme, which is designed to help lower the cost of capital for those providing "Build to Rent" schemes, contingent on tenants being offered a genuine option of either deposits or private insurance.
- The Government should protect tenants by mandating that new products in the deposit replacement market are fully regulated by the FCA, thereby ensuring that only products with the protection of the Financial Ombudsman are able to be provided to tenants.

The current deposit scheme often ends up costing tenants unfairly and is yet another issue facing "Generation Rent". For many tenants, an insurance-based scheme would be much more attractive – which is why the Government should act on the five proposals above, and promote this as a realistic alternative for tenants and landlords.

THE AUTHOR

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