LUHC Committee Shared Ownership Inquiry

Building Societies Association Response

14 September 2023

Introduction

The BSA represents all 43 building societies, as well as 7 larger credit unions. Building societies serve almost 26 million consumers across the UK and have total assets of nearly £500 billion. Together with their subsidiaries, they have helped over 3.6 million families and individuals to buy a home with mortgages totalling over £366 billion, representing 23% of total mortgage balances outstanding in the UK. They are also helping over 23 million people build their financial resilience, holding over £342 billion of retail savings, accounting for 18% of all cash savings in the UK. With all of their headquarters outside London, building societies employ more than 51,500 full and part-time staff. In addition to digital services they operate approximately 1,300 branches, holding a rising share of financial services branches in local communities.

Many of our members play a significant role in the Shared Ownership market and are committed to supporting and improving the scheme to best serve their members, particularly first-time buyers struggling to access the property ladder. Accordingly, the BSA welcomes the Committee's inquiry and its focus on improving the Shared Ownership market for consumers.

Response

Do the schemes Shared Ownership and Right to Shared Ownership provide good value for money for the potential users of the scheme?

In general our members agree that Shared Ownership provides good value for money for scheme participants. [1] To that end, it is fulfilling the intended goal of reducing the deposit required to purchase equity in a home and thereby providing quicker access to the property ladder to first-time homebuyers that would otherwise be priced out of the market. By way of illustration, the average home price in England now exceeds £300,000 (ONS May 2023). Based on average monthly savings targets for first-time buyers of £200 (as reported by our membership), saving for a typical deposit of 10% could take at least 12.5 years. Purchasing a typical 40% share in a home would reduce the deposit required and shorten that savings period to five years. Additionally, rental rates for the unowned share provide further cost savings. Rent typically starts at 2.75% of the share owned by the landlord. For instance, a purchaser with a 25% initial share (£100,000) of a $400,000 property will pay £8,250 per year in rent (£300,000 x 0.0275). This is significantly lower than average mortgage rates. These cost savings – coupled with the assumption that incomes will rise over time – are designed to enable participants to buy further shares in the property and eventually achieve full ownership. Even for those participants who are not able to or do not wish to staircase to higher ownership, Shared Ownership provides inherent value in the form of property security that participants might not otherwise be able to achieve.

Of note, however, the value determination is often made at the point of the initial share purchase. As with other tenures, this initial value could be eroded over time. In the Shared Ownership context this could prevent participants from staircasing upward. For instance, unforeseen rises in service charges, repair costs, or lease extension costs could affect share owners. A lack of understanding around the staircasing process and high processing costs have also deterred consumers from purchasing additional shares. Recently, high inflation and rising interest rates have added burdens to households. All of these contingencies and potential

[1] Our members have had limited experience with the Right to Shared Ownership scheme. Our responses are thus limited to Shared Ownership.

impacts on future ownership should be thoroughly explained to prospective shared owners to ensure the scheme is right for them both at the point of purchase and a sustained basis.

How can the Government ensure that Shared Ownership and the Right to Shared Ownership remains an affordable programme in light of rising provider costs and inflation?

The affordability of the scheme can be viewed from the perspective of either the shared owners or providers. These interests are related as maintaining the scheme's viability for providers affects affordability for owners. Government needs to strike the correct balance between these interests, allowing providers to recoup their costs whilst keeping charges to consumers at a level that allows them to increase equity (if they wish) and fulfil the larger ambition of the scheme.

Each provider's commercial objectives are impacted by rising costs. Whilst these are potentially covered by service charges, the consumer would argue that inflationary cost increases should be covered by annual rent increases. Shared ownership rent reviews allow only for upward increases based on the Retail Price Index.[2] Moreover, in some cases service charges, what they cover, and how they may change are not fully explained to consumers. This harms the consumer perception of the scheme and whether it provides value for money.

Greater standardisation in the regulation of shared ownership could help remedy this by ensuring consumers understand the potential future costs of remaining in the scheme and that these costs are fair and proportionate. Government could also obtain a better understanding of the rising costs faced by providers and how inflation affects these costs.

What support can be offered to Shared Ownership tenants given the impact of leasehold properties?

Due to the high proportion of first-time buyers in the scheme and the complexity of the leases, Shared Ownership leaseholders typically require more support than other leaseholders. Education and understanding of the scheme should be improved for both prospective shared owners and throughout the lifecycle of being a shared owner.

Our members report an imbalance between the support provided for consumers at the point of sale as compared to ongoing support. This varies significantly by provider, but often the post-sale support does not match that provided during onboarding. A greater emphasis should be placed on support throughout the entire lease.

At the time of purchase, consumers need a better understanding of the terms of their leases and potential future implications. In some cases, the buyer's conveyancer will explain the lease terms sufficiently, but this is not always true, particularly for those not using a specialist Shared Ownership conveyancer. Variation between leases also complicates matters, meaning that advice cannot be one size fits all. Local authorities may have a role to play here by ensuring that leases for a given area are fit for the local population.

There is also an opportunity here for the broader sector to work together – including lenders, providers, and intermediaries – to improve support and the consumer experience for shared owners. To that end the BSA and its members are currently involved in work being conducted by Professor Peter Williams, departmental fellow at the Department of Land Economy at the University of Cambridge, to create a cross-industry Code of Conduct to improve standards.

[2] The use of RPI should be revisited as the proper metric for assessing rent increases. The ONS has characterised it is 'a very poor measure of general inflation, at times greatly overestimating and at other times underestimating changes in prices.' Shortcomings of the Retail Prices Index as a measure of inflation.

What impact, if any, are changing sector regulations having on the Shared Ownership and Right to Shared Ownership Scheme?

Our members welcome the changes brought into force under the Affordable Homes Programme 2021-2026 (AHP), which demonstrate the ability of regulation changes to improve the scheme. Many of the changes should improve the experience of Shared Ownership leaseholders who enter into one of these leases. This should help ensure the continuing viability of the scheme. However, one side effect of the improvements may be to disenfranchise shared owners who have leases under legacy programmes. The issues resolved in the AHP may still exist for those consumers. Whilst prior leases cannot be changed, consideration should be given to these shared owners and how best to explain the differences in lease terms.

Additionally, one area of the new regulations that may benefit from further consideration is that requiring new sales documents to be generated by housing associations. Our members have anecdotally heard from providers that these are time consuming to create and are not necessarily achieving the intended outcomes.

Is there a lack of mortgage providers for Shared Ownership properties?

Our members consider the Shared Ownership market to be well-served by lenders. Shared Ownership transactions comprise a relatively small portion of the overall property market. However, many banks and building societies offer Shared Ownership lending products within their standard range or on a bespoke basis. The number of mortgage providers has increased recently with approximately 20 lenders currently in the market, providing consumers greater choice. This includes more offerings at higher loan-to-value ratios at up to 95%. Better regulation and standardisation could induce more lenders to enter the market. However, the complexity of this area (systems, training, process, etc.) and capital requirements required for higher loan to share transactions may continue to prevent further entrants.

What challenges are associated with repair costs being covered by those utilising the Shared Ownership schemes?

As noted, potential future costs to consumers for maintenance and repair are often not clear at the point of sale. This can be a challenge when unexpected costs arise. Greater information provided to a prospective buyer as to the potential liabilities and responsibilities could again prove useful.

Consumers and consumer groups often view the cost allocation as unfair as they are typically liable for 100% of costs despite owning less than a full share of the property. There may be a better way of allocating costs for essential repairs, recognising that shared owners and providers both have an interest in maintaining the property. A risk with this approach, however, is that any shared costs could merely be charged back to consumers through increased service charges.

The issues around repair costs have been mitigated somewhat by the AHP lease. For instance, the new 10-year initial repair period is a welcome change that will limit liability and provide greater certainty to shared owner leaseholders. Pre-2021 leases, however, allow providers to pass on all repair costs to consumers regardless of the share owned. This could also disenfranchise shared owners who have incurred repair costs that would be covered under the new standard lease terms.

How viable is full ownership through the Shared Ownership scheme and/or the Right to Shared Ownership Scheme?

Our members believe full ownership can be viable for many consumers, though we understand from conversations with providers that many consumers do not staircase beyond their initial share. We would note, however, that shared owners have different objectives and that full ownership may not be the ultimate goal for some. For those seeking full ownership, there are multiple ways to achieve this.

First, shared owners may increase their equity through staircasing. The data on staircasing is limited, though although we expect that some who choose not to staircase are content with the initial share purchase due to the security of tenure that it provides versus the private rented sector. Regardless, some improvements may increase take-up. Providers' processes for staircasing can be time consuming, costly and opaque. Improving these areas and providing better consumer education could lead to more staircasing.

Recent changes to the Shared Ownership the AHP lease may also boost staircasing. Consumers can now staircase in increments of 1% (though at least one housing authority offered this option before 2021). These equity share purchases do not require new valuations, which add costs for consumers. These reforms will likely make staircasing attainable for most customers. It remains to be seen, however, whether these changes will induce more staircasing. The effects could be modest as the 1% increase can only be used annually for up to 15 years. The result would be a relatively modest increase of 15% ownership that would be accompanied by a small reduction in rental payments. This may be insufficient to drive greater staircasing.

As an alternative to staircasing, shared owners may use the growth in value of their equity share to serve as a deposit for a move into a standard residential property. There is a similar lack of data on how common this practice is. Further work could focus on this segment of the Shared Ownership market.

Does the Right to Shared Ownership policy in its current form reduce homeownership risks for individuals from lower income backgrounds?

Our members do not see the Right to Shared Ownership scheme as a tool for reducing home ownership risks. Participants in the scheme are still subject to risks that are applicable to all homeowners such as unexpected repair costs. Whilst the new AHP model lease offers some protection against these risks by way of the 10-year initial repair period, more could be done to educate prospective buyers on the broader risks of home ownership.

What more can be done to secure the Shared Ownership scheme as an affordable route into home ownership?

Continued funding from Government will ensure that the grant-funded Shared Ownership market continues to develop and grow. We would caution that, without an increase in overall housing supply, competing schemes such as First Homes risk cannibalising Shared Ownership delivery. Whilst alternative schemes may meet some buyer's needs, Shared Ownership has proven effective at overcoming the deposit hurdle for first-time buyers.

There are other reforms that could help better support shared owners and the market. As mentioned, improved regulation and standardisation could provide value to consumers and allow the market to function more smoothly. Guidance could also provide standards for better communication to consumers at the time of purchase regarding lease terms, future service costs (even if on an indicative basis), and implications of the lease.

Shared owner leaseholders could also be protected better and treated more akin to traditional leaseholder rather than assured tenants. This comes into play, for instance, with lease extensions where shared owners only enjoy a statutory right to extend the lease if they have staircased up to full ownership.

Some within the sector have floated the idea of further lowering the initial minimum share purchase. The AHP model lease allows for a 10% initial share. Lowering this threshold will further reduce the deposit hurdle, but risks drawing in customers who are not able to staircase further or move into a mainstream tenure.

How does the variation of costs from Housing Associations and other providers impact the Shared Ownership Scheme and the experience of tenants or potential buyers?

As lenders, our members typically do not have visibility into providers' costs. We would assume that different providers face different costs based on a variety of factors. Shared owners may thus be charged different amounts. Providers, however, should be able to justify any differences to ensure fair value across the market. This lack of uniformity also makes comparisons for potential purchases challenging. Providers could be required to provide more transparency upfront. For example, they could disclose known charges at the time of purchase similar to the requirement for lenders to disclose costs that customers may face throughout the life of a mortgage.

One additional issue arises with the cost to shared owners associated with selling their shares. Some will seek to lever equity from their share to move into full ownership of a standard residential property. However, this re-sale process is often costly (relative to income) and not straightforward. A more centralised approach to marketing these properties could reduce these costs and allow shared owners to retain a greater proportion of their equity.

What should be done to improve the Department for Levelling Up, Housing and Communities' data collection regarding Shared Ownership and the Right to Shared Ownership?

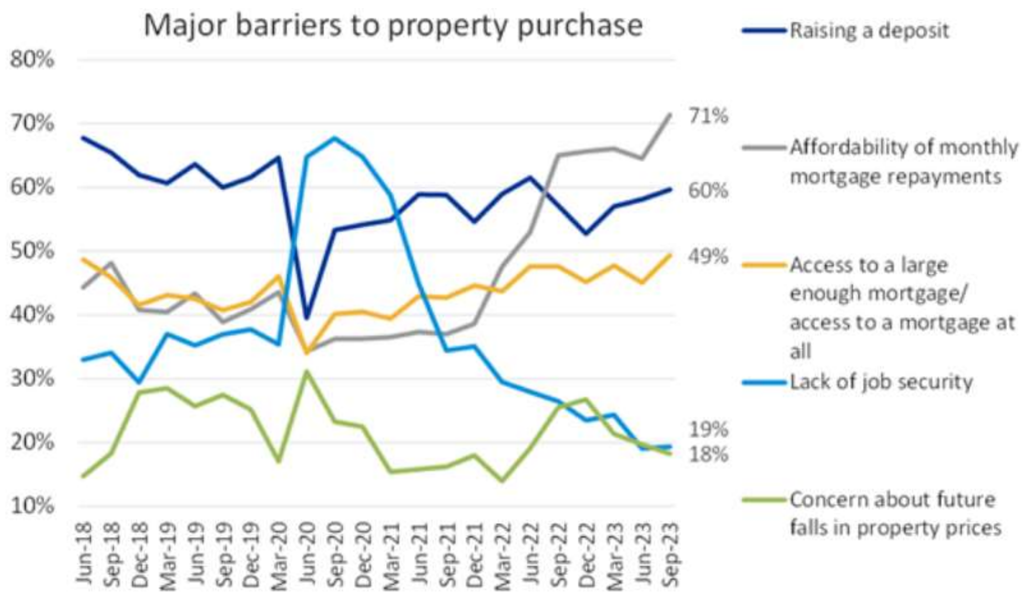
At present, data on Shared Ownership is extremely limited. This stands in contrast to other schemes such as Help to Buy and First Homes where data on market size and characteristics is widely available. Government should consider mandating data reporting in the same manner as lenders are required to report other loan data. This would enable lenders to better understand the market and customer profiles of shared owners, allowing existing lenders to better serve the market and encourage others to enter.

Are alternative schemes such as 'Rent to Buy' viable and do they offer more value for money?

The viability and value for money of alternative schemes will depend on the details of the particular schemes. Any alternative schemes such as Rent to Buy will have different target markets than Shared Ownership. Prospective buyers should be given information to understand the differences between various schemes and which may suit them best. To this end, Government could create a central information hub for first-time buyers to allow for comparison of affordable housing options.

What more should be done to support first time buyers and those from lower hold incomes onto the property ladder?

In the near term, the key challenges for first-time buyers and lower income household will likely be the ongoing cost of living crisis and interest rate rises. These are captured by the BSA Property Tracker, which shows that mortgage affordability has now outstripped raising a deposit as the largest barrier to purchasing a home.



These challenges may be difficult to overcome without a reduction in house prices or large scale wage growth.

In the long term, we encourage Government to deliver on its manifesto commitments to increase the supply of residential homes. Affordable housing will necessarily be delivered as part of any new developments, giving prospective buyers more options. Growth in overall housing development will also increase the number of social and affordable rented properties. This may not immediately result in greater access to the property ladder, but the discounted rent associated with these properties would provide the potential to save for a deposit.

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The Building Societies Association (BSA) is the voice of the UK's building societies and also represents a number of credit unions.

We fulfil two key roles. We provide our members with information to help them run their businesses. We also represent their interests to audiences including the Financial Conduct Authority, Prudential Regulation Authority and other regulators, the Government and Parliament, the Bank of England, the media and other opinion formers, and the general public.

Our members have total assets of over £481 billion, and account for 23% of the UK mortgage market and 18% of the UK savings market.