

Starter Homes Regulations

Response by the Council of Mortgage Lenders to the Department of Communities and Local Government technical consultation

Introduction

1. The CML is the representative body for the residential mortgage lending industry that includes banks, building societies and specialist lenders. Our 135 members currently hold around 95% of the assets of the UK mortgage market. In addition to home ownership, CML members also lend to support the social housing and private rental markets.

2. We welcome the opportunity to respond to this technical consultation. Enquiries on the content of this consultation should be sent to jennifer.bourne@cml.org.uk

Executive Summary

3. We accept and are supportive of the policy intention of the starter homes scheme, but would like to draw attention to the potential for certain unintended consequences. Our response includes a number of proposals which we hope will help improve the operation of the scheme; and which will encourage the greatest level of participation from all parts of the mortgage market. These are summarised below:

- We support a restriction period that would prevent starter homes being sold at no more than 80% of full market value, followed by a period during which a taper would be applied to enable the starter home to be sold at an increasing proportion of market value, stepping to 100% over time.
- To ensure some lender participation, the 'static' period should be at least three years, followed by a taper period of at least five years. **The longer this period of discount is, including taper, the greater lender participation would be.** There is probably a cut-off around the ten year mark as lenders also recognise the challenge with a lengthier discount in terms of enabling people to move on. It remains the case that some lenders would prefer an in-perpetuity discount, although they expect that this is not politically acceptable.
- We support an approach whereby a starter home is sold at full market value, with the seller receiving the share of the value that they are due and any residual discount is returned to Government. This has a number of advantages, including simplifying valuation, and providing a revenue stream to support scheme administration.
- If there is a centrally-set percentage requirement, we suggest 15% should be the maximum percentage requirement. There is no preference for where the requirement is set.
- A scheme administrator is fundamental to the success of the scheme and will perform a key monitoring and administrative role which will assist all stakeholders.
- Overlaying starter homes with other government schemes creates challenges for monitoring and lender systems. It could potentially rule out a significant number of lenders from offering mortgages, reducing the overall availability of mortgage finance.

General Comments

4. As we have stated, CML is supportive of the policy intention to deliver a greater supply of affordable housing for first time buyers, through the starter homes scheme; but we are mindful of the potential for unintended consequences given some of the scheme features and the scale of the scheme. We have welcomed and continue to welcome close engagement with DCLG and wider government as the Housing and Planning Bill has progressed; and as the detail of the Regulations to support the Bill are developed.

5. The starter homes scheme has generated considerable discussion and varying views amongst our membership. Core concerns raised by our members which need addressing are:

- The scale of the scheme, the size of the discount and the consequential potential for market distortion
- Customer understanding of the scheme and restrictions, not just at the point of sale but throughout the life of the scheme
- The valuation challenges presented by the scheme
- Managing and monitoring the scheme
- The long-term market impact
- Overlaying the scheme with other government schemes

Lenders have differing views on these issues and the scheme overall, in part depending on their current and future plans for lending on new build and affordable housing. Many will want to see the final detail of the scheme, especially in relation to the nature and length of the discount period, before making a decision about whether to lend on starter homes.

The scale of the scheme

6. We have previously commented on the challenging target of delivering 200,000 starter homes within the life of a Parliament, especially in combination with other stated targets for new build, such as the target for 135,000 more shared ownership homes to be built in the life of the Parliament. In the context of overall new-build housing, the scheme would represent a significant proportion of all new-build; and that presents a market distortion risk. Taking the DCLG's quarterly statistics for the 2015 calendar year (142,890), the combined target for both starter homes and shared ownership could represent around 78% of all new build completions per year over the next three years, unless all goes into additional supply, not just substitution. That is a very improbable outcome.

7. These figures, if achieved, will have an inevitable impact on the wider new build market, and implications up the housing chain – moving on from a starter home with sufficient equity will provide a benefit to the homeowner and support future purchases, but this will require sustainable property prices, which we discuss in more detail below.

8. A less ambitious target would, in our view, lead to a more successful scheme. The scheme would then complement, rather than potentially challenge, the government's other housing initiatives such as increasing the shared ownership tenure and providing more custom-built homes.

Scheme combinations

9. While this consultation does not directly refer to the layering of Starter Homes with other schemes such as the Help to Buy: Equity Loan scheme, the majority of our members, in terms of market share, have raised concerns about scheme combinations.

10. The main concerns are firstly, that layering of schemes presents a complex proposition for buyers, in terms of understanding what their equitable interest and obligations are in the property. This may lead to unintended consequences such as raising conduct risk issues for lenders, for example.

11. Secondly, combining schemes also provides significant value to potential house buyers over a short period of time, which would likely stimulate excess demand. This could exacerbate the potential for driving up house prices, which may be unsustainable in the long-term. This could present a risk for the buyer, mortgage lenders and the government, where, for example, they have provided an equity loan on the property.

12. Finally, some lenders' mortgage platforms may not be able to cope with overlaying schemes which contain restrictions outside of existing models, without risk of error, poor customer experience, and substantial IT development costs.

13. The combination of these concerns would potentially rule out a significant number of lenders from offering mortgages if Starter Homes were overlaid with other schemes, reducing the overall availability of mortgage finance.

Restrictions on sales and lettings of a starter home

Discount period

14. We support a restriction period during which starter homes would be sold at no more than 80% of full market value, followed by a period during which a taper would be applied to enable the starter home to be sold at an increasing proportion of market value, stepping to 100% over time.

15. As a minimum, to ensure some lender participation, the 'static' period should be at least three years, with the taper period being as a minimum a further five years. **The longer this period of discount is, including taper, the greater the lender participation would be.**

A taper period

16. We welcome the fact that Government is prepared to consider a taper period. A taper will avoid a 'cliff-edge' scenario where an equity windfall can be achieved 'overnight' in the case of a straight removal of the restriction, which could lead to a glut of properties on the market; and heightened competition for properties on sale near the end of restriction period, creating risk of significant market distortion.

17. The majority of our members would prefer a taper period which starts after a defined period of ownership (we put forward a minimum period of three years or above), as opposed to a taper which begins from the first year of ownership, which is more likely to encourage speculative purchasers, who may be keen to realise an early equity windfall. While there is no general consensus as to the length of taper, the longer the period, the greater the likelihood of lender participation. Some members do recognise the challenge with the period of discount lasting beyond a maximum of around ten years in terms of enabling people to move on; others still have a preference for an in-perpetuity discount.

18. A taper is not without challenges, particularly on how to value the property during the taper period as the element of equity increases over time. We have commented on ways to mitigate this further below, with regard to valuation issues.

Valuation issues

19. There is consensus among members that the scheme will present valuation challenges.

20. The existing challenge of valuing new build property and judging the market value (factoring in the 'new build premium', for example) may be further amplified by seller and buyer behaviours under the scheme. Large sites for example, may suffer simultaneous "feast and famine" – too many households chasing starter homes and a dearth wanting to pay market price for other properties.

21. Using independent valuers to an agreed method of valuing would help reduce the potential for disputes. We are supportive of RICS-led guidance for valuers. Lenders will continue to use their existing valuation processes should they choose to offer mortgages under the scheme, but would not want to have the role of 'policing' valuations under the scheme.

22. Valuing a property over a taper period is an acknowledged challenge. At the least, within the existing valuation process some rules or guidance will be required as to the point at which the remaining discount is calculated and hence how to determine the valuation. RICS guidance should assist with this.

23. Our members support an approach whereby the property is sold at full market value. On completion, the seller receives the share of the value that they are due and any residual discount is returned to Government to support the development of further affordable housing (similar to Help to Buy: Equity Loan). This would have two advantages: it would make valuation much simpler; and provide a stream of income back to government to help support administering the scheme and supporting additional affordable housing.

24. On this approach, additional restrictions as to who the property is sold to (e.g. another qualifying first time buyer) would not be needed, though, as an alternative, we suggest that any such

restrictions should only be applied during the initial 'static' period, and not the taper period, to minimise complexity.

25. We have responded to the valuation questions relating to the impact assessment below.

Restriction on resale

26. As we note above, if the property is sold at full market value, and the residual discount goes to government, then there would not, in our view, need to be an additional restriction of selling to another qualifying first-time buyer.

Restrictions on letting

27. We support restrictions around letting and are keen to understand how the government foresee the policing of this aspect of the scheme. Our members are clear about the need for a scheme administrator to police this, either in partnership with or resourced for local authorities, as it is not clear how local authorities would fund and police this aspect within their current resource.

28. We recognise that there is a need to fund the scheme administrator and we suggest that this could be achieved by recycling the subsidy back to government upon sale of the starter home, to help finance, through sales during the restricted period. This would be as an alternative to having the restriction administered by way of a s106 agreement.

Restrictions on age

29. Lenders are broadly comfortable with the proposals around the minimum and maximum age requirements. We note that lenders will not wish to be a gatekeeper for checking various aspects of customers' eligibility e.g. age, as this would add an additional administrative burden. We would see a scheme administrator performing these checks as per the Help to Buy Equity Loan Scheme.

The starter homes requirement

Percentage requirement

30. While there is no particular preference for either centrally, or locally-set requirement among lenders, we are sympathetic to the arguments raised by others for a regionally-set minimum requirement, which gives local authorities the ability to set the requirement in response to local need.

31. If there is to be a nationally-set requirement, we would prefer to see the percentage requirement set lower than the 20% proposed in the consultation and suggest 15% should be the maximum percentage requirement. This would, we believe, better enable a mix of affordable housing tenures to exist on sites, especially given that DCLG analysis shows that commonly 20% is the entire affordable housing proportion on site and therefore would constrain other tenures. It would also lessen potential market distortionary effects.

32. We recognise that having a percentage site requirement of 15% would have an impact on the minimum threshold for site size in relation to unit numbers, as there would need to be a 20 unit minimum to allow for a whole number calculation (i.e. 15% of 10 is 1.5 units, whereas 15% of 20 units is 3 units), and we suggest that the minimum unit size is amended to 20 units.

Minimum threshold for residential developments subject to the starter homes requirement

33. We would prefer to see, at most, a percentage requirement of 15%, which has an impact on the minimum threshold of site size of 10 units, as proposed in the consultation. We propose that this be increased to 20 units, as explained above.

Exemptions to the requirement

34. We support a general viability exemption where the requirement would render sites unviable. It is for others to comment on the most appropriate viability test.

35. We agree that other exemptions should include specialist housing developments such as dedicated support housing and student housing; and developments which support a high proportion of alternative affordable housing tenures such as shared ownership and affordable rent.

36. The government's stated desire to build 135,000 shared ownership properties by the end of the Parliamentary term may otherwise be jeopardised by a compulsory starter homes requirement (and target of 200,000 starter homes by the end of the Parliamentary term). We have already commented on the ambitious targets and the impact on new build generally.

37. For custom-build, viability issues may arise. For example, the different development funding models that exist for custom build as compared with standard new build is such that imposing starter homes requirements on these types of developments may create challenges and unintended consequences. For this reason it may be justifiable to exempt group custom build developments, especially as there is a separate aim to increase the custom-build market.

38. We are supportive of exemptions for developments with high levels of other affordable housing.

The starter homes requirement and off site commuted sums

39. We have no strong views on the proposals around off-site commuted sums.

Monitoring and reporting

40. We note and have no strong views on the proposal for Local Authorities to provide reports, as part of their existing report framework, which will allow the government to identify the number of starter homes either in progress or completed.

41. However, we would also like reassurance that the government will put in place requirements to monitor the wider policy intention of the scheme, to ensure that the potential benefits intended are realised without unintended consequences and in particular, to monitor any housing market distortion.

42. Information about the homes being sold under the scheme such as sale price, customer characteristics and type of properties being sold under the scheme will be important measures to help gauge the impact of the policy. The impact on other affordable housing tenures should also be monitored, given the other policy imperatives around other forms of affordable housing, such as shared ownership. This could be collated and monitored by a scheme administrator.

Transitional provisions

43. We have no strong views on whether a transition provision is required as other stakeholders are better placed to respond to this.

Equalities considerations

44. We have no comments on this.

Assessment of impact

45. The potential impact of starter homes on the housing market is significant. We have responded to the specific questions below.

Questions:

Q1: Do you support restrictions on the sale and sub-letting of starter homes for 5 years following initial sale? Do you support allowing individuals to sell at a higher proportion of market value as the number of years they have lived in the home increases? If not, what other approaches can we adopt to meet our objectives?

We support restrictions on the sale and subletting of starter homes and there is broad consensus among our members that there should be a static period following initial sale where set restrictions

apply. Rather than a specific length, we have indicated a range of lengths of discount period which will enable some lender participation. We support a follow-on period of a tapering of the sale discount which enables the starter home to be sold at an increasing proportion of market value, stepping to 100% over time. We have suggested more detail as to how this might be achieved in the body of the response.

Q2: Do you agree that flexibility over the age 40 restriction should be given when joint purchasers are looking to buy a starter home, one purchaser being under 40 years old but the other older than 40?

We are broadly comfortable with the proposal to provide flexibility in this instance.

Q3: Do you agree that there should be an exemption from the age 40 restriction for injured military services personnel and those whose partner has died in service?

We are broadly comfortable with the proposal to provide flexibility in this instance.

Q4: Would a site size of 10 units or more (or 0.5 ha) be an appropriate minimum threshold for the starter home requirement? If not, what threshold would be appropriate and why?

See our response to Q6.

Q5: Should the minimum percentage requirement be applied uniformly on all sites over 10 units to provide a single requirement across the country?

We do not have a particular preference, however we are sympathetic to the argument for a locally-set minimum requirement which gives local authorities the ability to set the requirement in response to local need. We recognise that a nationally-set requirement will reduce delays which may arise in arriving at a locally-set requirement.

Q6: If so, do you agree that 20% represents a reasonable requirement for most areas?

While we do not have a preference for having a single requirement across the country, we suggest that a minimum requirement of at most, 15%, will better enable a mix of affordable housing tenures to exist on sites; and lessen any market distortionary effects. To work with the minimum site size threshold, that threshold should be raised to 20 units, to allow for a 'whole number' site calculation.

Q7: Do you support an exemption from the Starter Homes requirement for those developments which would be unviable if they had to deliver any affordable housing including Starter Homes? If so, how prescriptive should the viability test be in the regulations?

Yes. We have no comments on the viability test.

Q8: Do you support the proposed exemptions from the starter home requirement? If not, why not?

Yes, in the main.

Q9: Should group custom build developments and developments with a very high level of affordable housing such as estate regeneration schemes be exempt? If not, why not?

For custom-build, viability issues may arise. For example, the different development funding models that exist for custom build as compared with standard new build is such that imposing starter homes requirements on these types of developments may create challenges and unintended consequences, especially as the government are seeking to increase this type of new-build. For this reason it may be justifiable to exempt group custom build developments. We are supportive of exemptions for developments with high levels of affordable housing.

Q10: Are any further exemptions from the starter home requirement warranted, and why?

No comment.

Q11: Do you support the use of commuted sums to deliver starter homes where the local planning authority agrees?

We do not have strong views on this.

Q12: Do you support the proposal that private rented sector housing (for institutional investment) and specialist older people's housing should meet the requirement through off-site contributions?

We do not have strong views on this.

Q13: Do you agree that Starter Homes monitoring reports should be an annex to the Authority Monitoring Report?

Yes, in principle.

Q14: Do you agree that these reports establish the key actions taken to support starter home delivery and the outcomes in terms of permissions granted and completions?

We think that these reports are only part of the picture in terms of monitoring the success of this scheme. See paragraphs 38-40 above.

Q15: Do you agree that April 2017 is a reasonable date for the first report to be published? If not, do you have alternative suggestions and why?

Assuming that there have been starter home starts by then, then it may be reasonable – but it is more for others to comment on.

Q16: Do you support a transitional provision for the starter home regulations?

This is a matter for local authorities to comment on.

Q17 Is there further evidence we should be considering in our assessment of equalities implications?

None of which we are aware.

Q 18 (i): How do you anticipate the open market value of Starter Homes would compare to other affordable housing products such as social rent, affordable rent and affordable home ownership?

We believe the open market value of Starter Homes would be higher than other affordable home-ownership products because of the nature of the restriction and the likely demand for such properties. It is difficult to anticipate the value of a starter home against social rent and affordable rent tenures as these are typically not available on the open market.

(ii): How do you envisage the market value of Starter Homes when compared to the market value of full priced new build homes bought by first time buyers?

We anticipate that the market value will be difficult to establish on sites where a significant proportion of starter homes are being sold. The potential attractiveness of the scheme may lead to “feast and famine” – too many households chasing starter homes (and pushing up prices for them) and a dearth wanting to pay the market price for other properties.

Unsustainable prices for Starter Homes may initially be supported, creating a longer-term problem for owners, mortgage lenders and the government. This would be mitigated by adjusting the target number of homes downward, and reflecting that in the scheme design, i.e. reducing proposed percentage site requirement.

(iii): What is your view on the proportion of sites that would be able to deliver 20% Starter

Homes without viability being affected? How would this affect other developer contributions?

We have proposed a smaller percentage requirement, however others are better placed to provide a view on viability and developer contributions.

(iv): Do you agree that in most instances s106 negotiations occur on residential sites of 10 or more units, regardless of whether a s106 agreement is ultimately put in place? And do you agree that before the April 2015 pooling restrictions on Section 106, infrastructure contributions (as a proportion of development activity) tended to be higher in authorities that secured relatively low s106 affordable housing contributions?

We have no view on this.

(v) To what extent do you think the starter home requirement and associated exemptions will affect site viability, if at all?

We have noted that group custom build developments may have viability challenges if they are not exempted from starter homes requirements. Others are better placed to provide a more general view.

(vi) We would welcome (a) any estimates of the costs incurred by developers in negotiating s106 agreements on sites of different sizes, for example time costs, consultants or legal fees, and (b) views on the extent these costs might change as a result of the 20% starter homes requirement.

We have no view on this.

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