

Winckworth
Sherwood



Shared ownership reform: question
over viability



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Introduction

Shared ownership was introduced in the form that we know it today in the 1980s via the Housing Act 1980, which incorporated the right to staircase, to help people who were in housing need and could not afford to buy a home outright. It has proven to be a valuable measure to enable more than 150,000 households realise the dream of home ownership. Housing associations have played a key role in the delivery and management of shared ownership property.

The government in 2020 announced major reforms of the shared ownership regime. At the heart of those reforms is a reduction in the minimum equity purchase, to allow staircasing in increments of 1% and, a repairing obligation of ten years on new shared ownership properties.

Whilst the reforms will undoubtedly be welcomed by those wishing to purchase their own home, they have the potential to change the very foundations of the social housing sector.

The reforms are likely to result in a significant increase in the already high administrative responsibilities of affordable housing providers. It is also likely to create an undesirable two-tier shared ownership market, with those on pre-reform agreements treated differently. More worryingly, it may lead to affordable housing providers exiting the shared ownership market entirely.

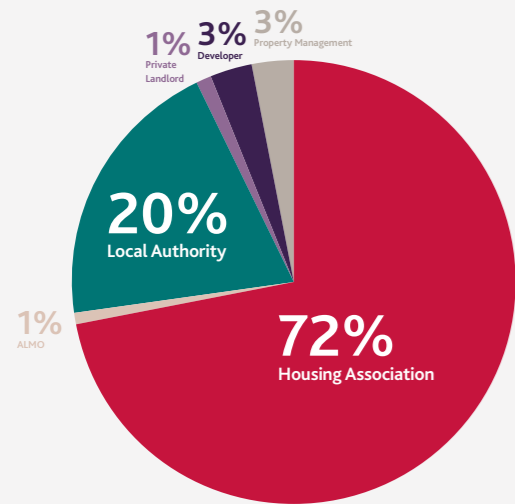
That is why in December 2020 and in January 2021 we surveyed 134 affordable housing providers to explore their views on the proposed reform. We also include the experiences of affordable housing providers asked to trial the reforms and the opinions of lenders and funders that underpin the development of new homes in the sector.

We would like to use our research and this report to begin a wider discussion on the reforms and their impact on the social housing market. We would welcome your thoughts.

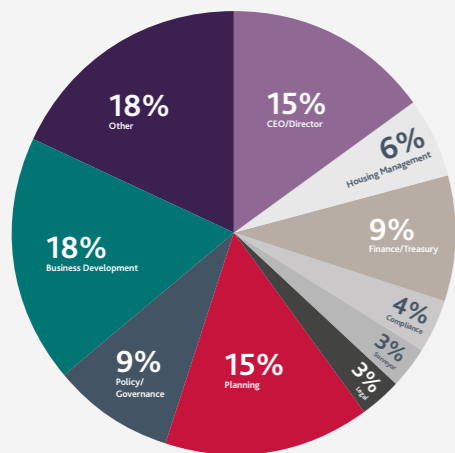
Winckworth Sherwood Social Housing Team

Who we surveyed

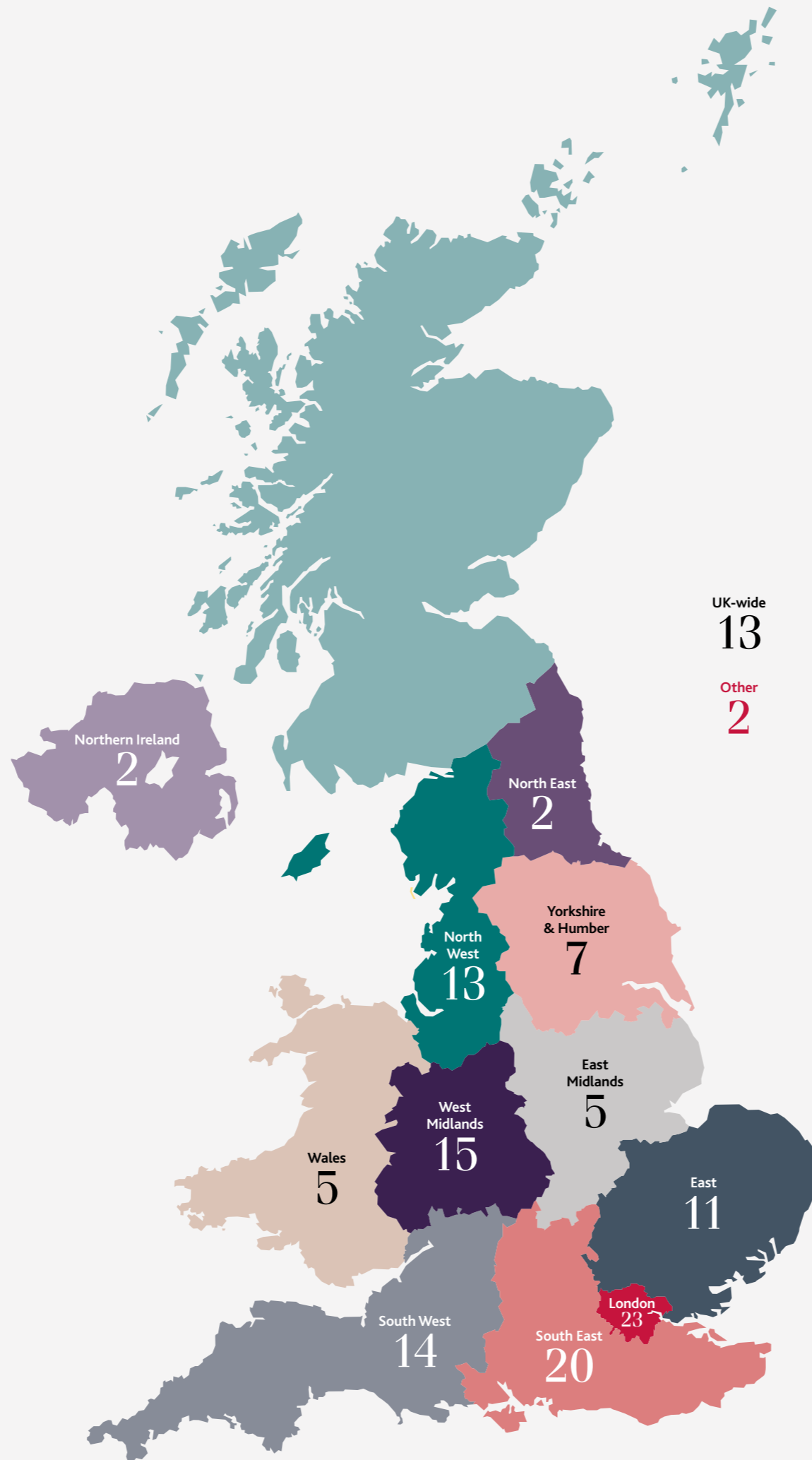
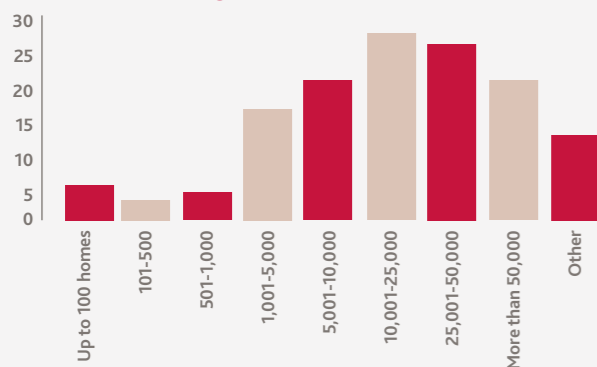
Who we surveyed



Role or position



How much housing stock is held



INSIGHT

Tony Petrou

A SECURITY TRUSTEE'S PERSPECTIVE

Head of New Business, M&G Investments/Prudential Trustee Company

The shared ownership reforms are without doubt great for tenants who would otherwise struggle to get onto the housing ladder, but will be a test for affordable housing providers. "Accurate record keeping will be essential", says Tony Petrou, Head of New Business at M&G Investments.

"Housing associations are incredibly accommodating and will do everything possible to get people onto the housing ladder. But at the moment we simply do not know if tenants will quickly jump in and regularly buy 1% tranches. We will need to wait and see over the next 12-24 months to really gauge its impact.

"We do know, however, that these reforms will add a lot more pressure on housing associations with the need for greater levels of record keeping, and these are costs that cannot be passed on to tenants."

Tony and his team are market leaders acting as security trustee for funders charging large portfolios of housing association assets. He also acts as a representative for investors in the sector purchasing capital market notes or bonds, and is following developments closely.

"A shared ownership portfolio will, by its very nature, diminish over a period of time," explains Tony. "Valuations will fall as shared ownership increases and if

funders see those valuations fall below minimum levels housing associations will be asked to top up security."

"Funders are unlikely to be concerned as long as records are kept up to date, supported by accurate valuations and there is enough security in place."

Tony can see challenges on the horizon, particularly with housing associations providing records to valuers on a timely basis that trustees agree with. A problem that could be compounded further if staircasing happens too quickly, which could leave housing associations in breach of their covenants.

"It all comes back to accurate record keeping," says Tony. "We expect to see annual desk top valuations together with full valuations every three-years."

"It will also increase our own administration as trustees we need to be informed of any changes to shared ownership. Change will happen a lot more often and that means we will be busier."

Shared ownership reforms – what is proposed

The current Shared Ownership model is changing under Government reforms and a new model lease is coming into effect from April 2021. What do we know so far?

A Government consultation which closed on 17 December 2020 put forward the following proposals.

The minimum initial share is to be reduced from 25% to 10%

Purchasers should be encouraged to buy the maximum share they can afford, and providers should ensure they sell flexibly. This is likely to mean, for example, not to the nearest 10%.

Staircasing can take place in tranches of 1% with reduced fees

Purchasers will have the option to buy additional shares in increments of 1% each year with the price based on an estimated valuation linked to the original purchase price, adjusted upwards/ downwards in accordance with inflation. Landlords will not be permitted to charge valuation or administration fees. Gradual staircasing is to be available for a minimum of 15 years.

Landlords will be responsible for repairs and maintenance in the first 10 years

With the intention of bridging the gap between renting and homeownership, shared ownership leaseholders will not be responsible for essential repairs and maintenance in the first 10 years of ownership.

Where work is not covered by the new-build guarantee, landlords will be responsible for the cost of essential repairs that relate to the external composition of the building and external structural parts where the landlord is also the building owner. This will include inside structural repairs to the property such as floors, stairs, walls and ceilings.

Where work is required inside the property, responsibility remains with the shared ownership leaseholder. They will, however, be entitled to reclaim costs up to a maximum of £500 per year from their landlord towards essential repairs and maintenance. Shared ownership leaseholders will also be given the ability to carry over a year's worth of unused repairs and maintenance allowance to the following year.

The 'first 10 years' applies to new-build properties only and will be effective from the date it is built (i.e. practical completion). The repair and maintenance period will then last until the end of the first 10 years or the date the shared ownership leaseholder staircases to 100%, whichever is the earlier. If a property is resold in the first 10 years, the next shared owner will be entitled to benefit from the remaining repair and maintenance-free period.

Nominations period and pre-emption clause

The current eight-week timeframe in which landlords can exclusively market the property and find a new purchaser will be reduced to four weeks, giving shared ownership leaseholders more control when it comes to selling their home.

Introduction of "Right to Shared Ownership"

This will enable social tenants, subject to certain qualifying criteria, to purchase a share in their rented home using the new model.

Lease Term

All shared ownership leases under the new model are to have a 990-year term as standard.

The proposal also includes transitional arrangements to cover situations where land has already been procured by developers and planning applications have already been submitted. Sites that receive planning permission from April 2021, where affordable homes are secured through S.106 developer contributions will be subject to the new shared ownership model.

Many Registered Providers have given feedback on the above proposals since the consultation closed. It remains to be seen what the final form of the lease will look like.

INSIGHT

Geoff Pearce

A SOCIAL HOUSING PROVIDER'S PERSPECTIVE

Deputy Chief Executive-Swan Housing

Swan Housing manages 12,000 homes across London and Essex of which 900 are currently in shared ownership. And whilst its Deputy Chief Executive welcomes any measures to help people onto the housing ladder, he is unsure if these reforms will achieve what the government hopes.

"Staircasing in 1% tranches may sound a good idea but I do question whether significant numbers of people will take advantage of this. Staircasing is a major commitment for home buyers, with mortgage lenders often providing the necessary finance. 1% increases will have to be funded from savings and we just do not know if the demand will be there."

The process and ease of administration will be critical to its success and yet the detail is lacking. Housing associations have yet, for example, to see the new look shared ownership lease, a crucial component of the reforms.

"We don't yet know what the administrative burden will look like or its likely cost," explains Geoff. "It needs to be simple and needs to be coordinated at a sector-wide level, ideally led by the housing regulator. We cannot have individual providers each pursuing their own processes."

Swan Housing does have questions over the impact of the 10-year repair obligations but doesn't believe it will fundamentally change the demand or provision of shared ownership homes.

"The impact of the repair obligation remains unknown. Are we likely, for example, to see a spike in claims immediately before the close of the 10-year window as homeowners look to take advantage of the cover?"

The reforms will inevitably leave providers with costs that it is unable or unwilling to pass on to occupiers. The costs will be factored into site appraisals, grant funding or s106 agreements with developers.

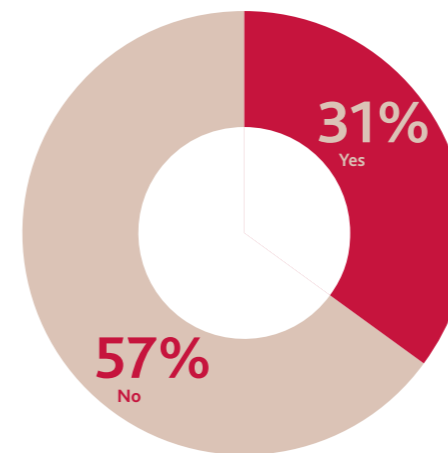
"These reforms are welcome, but we do need to see the detail," says Geoff. "Shared ownership remains an attractive product and the demand is strong, and these reforms are unlikely to change that."

Shared ownership – a reform too far?

The proposed reforms on shared ownership have received a mixed reaction from affordable housing providers, with questions raised on the reduction of minimum equity purchases, 10-year repairing obligations, the practicalities of staircasing in 1% tranches and on fundamental issues of the viability of schemes.

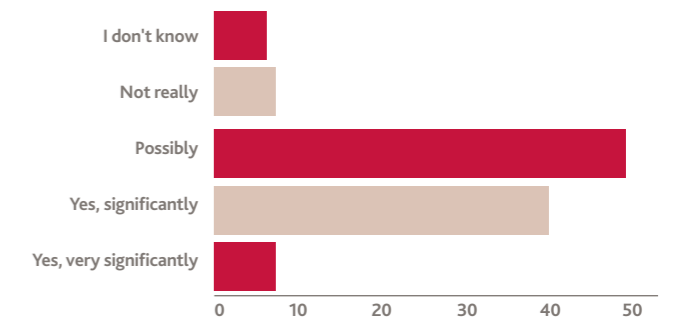
Our survey points to very real concerns, with over half (57%) of those surveyed not in favour of the reforms. Survey respondents told us that “1% staircasing could be an administrative nightmare” and that “it will make organisations have to review finances, possibly making shared ownership less viable”.

Are you in favour of the government's new Shared Ownership reforms?



Housing associations are acutely aware of the impact the reforms will have on their organisation, with 41% saying it will have a 'significant' or 'very significant' impact. A further 42% also recognise that it may have an impact, suggesting that further analysis of the proposed reforms is still needed by a significant proportion of providers surveyed. Providers told us that it will “affect our development capacity” and that it “will significantly affect our appetite to deliver shared ownership”.

Will reforms impact your organisation?



One of the primary concerns of affordable housing providers is the requirement to pay for repairs on the first 10 years of a property, which many believe will impact the viability of shared ownership homes. It is, however, the combination of staircasing in lower increments, the reduction in minimum equity purchase stakes and the repair obligations combined that make these reforms troubling.

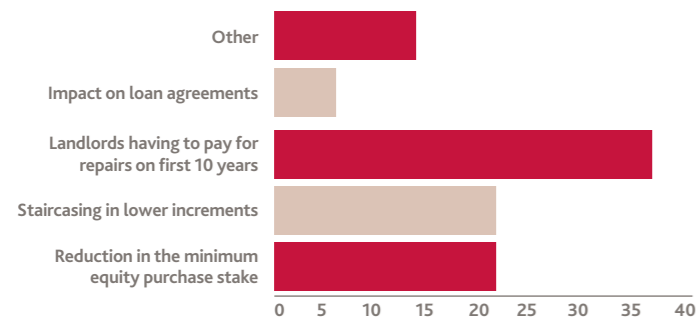
Our survey asked providers how much of an impact will the reduction in the minimum equity purchase (from 25% down to 10%) have on your organisation? Almost three quarters (73%) expect to have some impact, with 40% believing that impact will be 'significant' or 'very significant'

Winckworth Sherwood recommends that housing associations if they have not already done so, model the various scenarios to explore that impact on funding and the relationship with funders, the viability of schemes, planning and S106 obligations, ongoing repair obligations and tenant affordability.

A two-tier market

Housing associations face the prospect of a two-tiered market, and whilst that may not be of concern for developments that sit entirely in one tier or the other, multi-phase developments that straddle pre-

What are your main concerns about the changes?



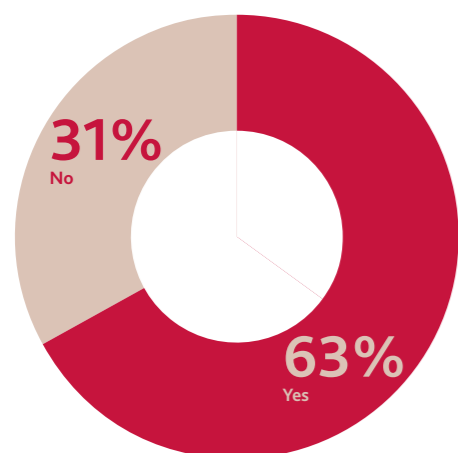
and post-reform will require thought and planning.

How will providers manage, for example, different repairing obligations, and how might that sit with neighbouring tenants potentially under different regimes?

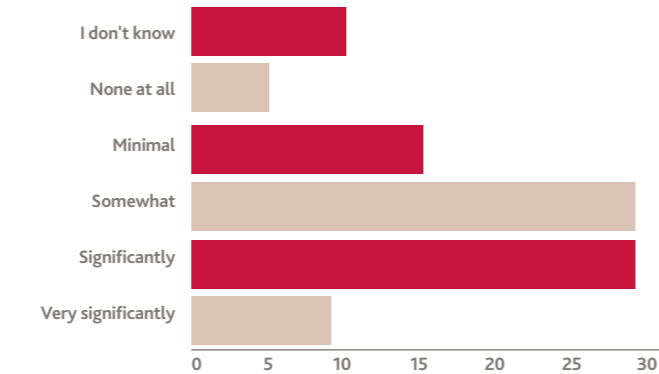
This two-tier market is also likely to require providers to revisit planning and S106 agreements and funding arrangements. The impact of a two-tier market cannot be entirely negated, it will be something affordable housing providers will need to manage on an ongoing basis.

The government proposes to reduce staircasing increments from 10% to just 1%. The impact on registered providers will be significant. Over 50%

Do you envisage the reduction in the minimum equity purchase creating a two-tier market, hindering your ability to sell Shared Ownership homes under the old model?



How much of a financial impact will the reduction in staircasing increments have on your organisation?

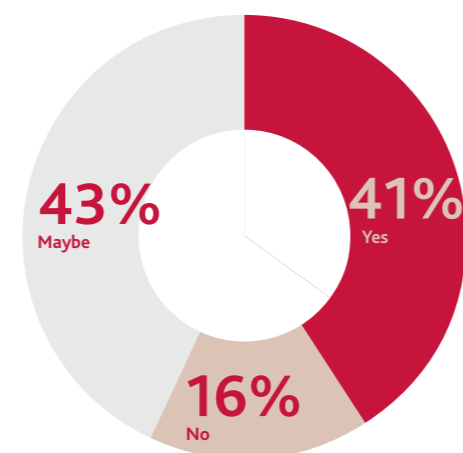


(54%) told us that it will have a 'significant' or 'very significant' financial impact.

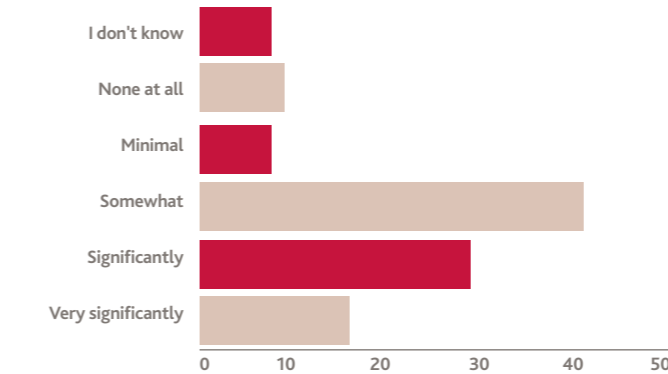
Providers currently do not know how the reforms, when adopted, will work? What appetite will there be from tenants for buying 1% shares in their home for a 1% reduction in their rent? Will housing providers look to pass that cost on to tenants, and how will mortgage lenders respond?

We believe there is likely to be greater interest in, for example, 5% increases with a corresponding 5% decrease in rent, as the cost of staircasing, particularly if passed on to occupiers, is likely to dissuade tenants from regularly purchasing smaller equity stakes.

Do you think the changes will make shared ownership more attractive to potential buyers?



How much of a financial impact will the obligation to pay for repairs for 10 years, have on your organisation



The administrative burden of these changes is not lost on registered providers, with 71% telling us that it will lead to significant additional pressure. Over half (55%) of providers surveyed have yet to put plans in place to manage these additional administrative pressures as detail and guidance has yet to be announced.

New models of funding staircasing may evolve, perhaps the creation of a fund administered by a social housing provider where tenants make contributions that trigger staircasing when contributions hit 5% or 10%.

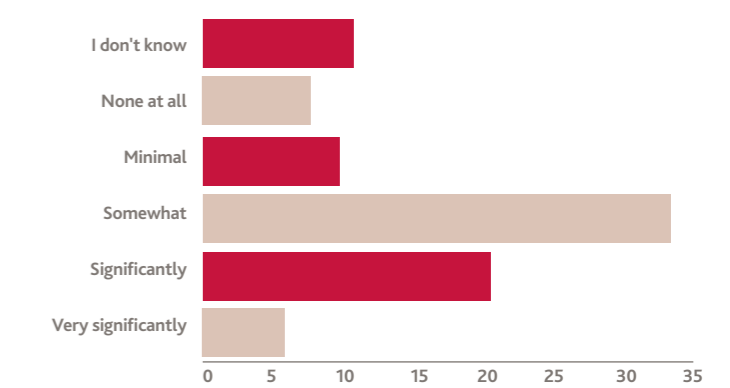
Government intends that staircasing in 1% increments will be simply managed by new and yet to be developed software administered by housing providers, with mortgage lenders offering offset mortgage products. It is hoped that the process will be automatic with no cost and no conveyancing lawyers needed.

The approach adopted will, however, ultimately depend on the detail yet to be published by government.

Repair obligations

The government proposes that registered providers will have a 10-year repair obligation on new shared ownership properties. Putting aside concerns on reinforcing a two-tier market, 42% of providers

Will the Right to Shared Ownership model have a significant impact on your organisation



surveyed tell us this will have a 'significant' or 'very significant' financial impact.

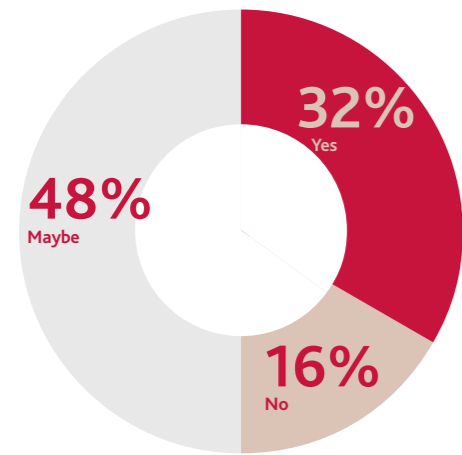
Is the cap now fixed at £500 or is there still scope for it to be reduced?

Where work is not covered by the new-build Guarantee landlords will be responsible for the cost of essential repairs that relate to the external composition of the building and external structural parts where the landlord is also the building owner. This will include inside structural repairs to the property such as floors, stairs, walls and ceilings. Where work is required inside the property, responsibility remains with the shared ownership leaseholder. They will, however, be entitled to reclaim costs up to a maximum of £500 per year from their landlord towards essential repairs and maintenance of certain installations where not covered by guarantee and not the result of normal wear and tear nor required as a result of deliberate or avoidable damage. Shared ownership leaseholders will also be given the ability to carry over a year's worth of unused repairs and maintenance allowance to the following year.

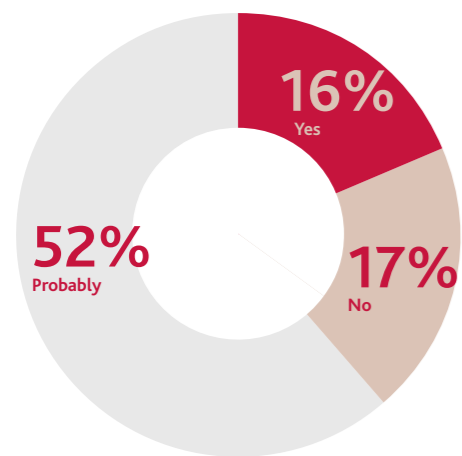
Nomination period halved

Under the proposed reforms, social landlords may see the eight-week nomination period cut in half. This eight-week window has long been a concern of tenants wishing to sell, effectively delaying sale plans. Housing associations will need to have policies in place to address any changes and to reduce the risk of

If First Homes became a mandatory component to the affordable housing offer, would that likely reduce the amount of Shared Ownership homes you bring forward?



Could these Shared Ownership reforms impact your existing loan agreements?



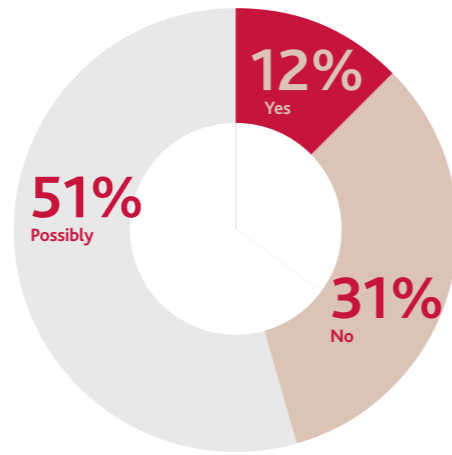
losing affordable units.

With this in mind, our survey asked whether housing associations would be more likely to repurchase a property during this new four-week period?

Almost half, 47%, told us that it will not affect their strategy at all, with 39% say that they would be more likely to repurchase a property.

We recommend that where housing associations do not have a formal policy in place regarding nominations they look to develop and adopt one in advance of these reforms.

Do the changes put HAs in a more attractive position for sales than on the open market?



First Homes

Affordable Housing tenures will continue to change and shift to reflect the affordable housing demographic and those in housing need. The demographic shift will at times also mean the introduction of new affordable housing tenures to address housing need. One such tenure on the horizon is First Homes which was introduced in the Planning White Paper and whilst no date is set for its introduction we anticipate that it will be introduced at some point during 2021.

The nuances of how this will work in terms of delivery and interaction with other tenures such as shared ownership are not yet known but it will have an effect on the amount of shared ownership that will be delivered. The present suggestion is that 25% of all affordable housing delivered by way of s106 agreements must be by way of First Homes. The amount of affordable housing a scheme can deliver will not change but that amount will have to include First Homes. This in turn will likely affect the number of homes delivered by other affordable tenures including shared ownership.

We will be examining the effect of First Homes on the delivery of affordable housing by registered providers in later publications over the coming months but as RPs get ready to adapt to these shared ownership reforms they will also have to consider the effects of First Homes too.

Impact on funding

How funders and valuers will react to the government's proposals is largely unknown. We do, however, explore their thoughts later in this report. Registered providers do expect the changes to impact existing and future loan agreements.

In our survey, 17% of registered providers believe it will have an impact with 53% saying it will possibly have an impact. Two thirds (67%) report, however, that their funders or lenders do not seem concerned by the reforms.

Very few loan agreements have materialised following the government outlining its proposals and it will be interesting to see how they change.

Both funders/lenders and providers eagerly await the detail on proposed reforms with changes to loan and funding agreements inevitable.

A loss of affordable homes

The proposed reform will include a new right to shared ownership, providing tenants renting a home with the opportunity to purchase their property through the shared ownership scheme.

It is a proposal that will, according to 28% of those registered providers surveyed, have either a "significant" (22%) or "very significant" (6%) impact. A further 36% believe it will impact their organisation more moderately.

Funders are likely to find this concerning in terms of security with providers suggesting it may lead to a loss of "precious social rented homes".

Over half (57%) believe it will lead to an overall loss of affordable homes in the sector, with just 12% believing it will have no impact.

The uncertainty surrounding the proposals and the lack of detail has already led some affordable housing providers to look at tenures on future and planned schemes, switching shared ownership homes to social rents. There is a risk that this will gather pace.

We would urge the government to publish as quickly as possible its detailed proposals and guidance to allow registered providers and their funders to prepare in the best possible way.

INSIGHT

Matthew Haycox

A VALUERS PERSPECTIVE

Director of Affordable Housing-JLL

All measures that widen the homeownership demographic must be welcomed but these reforms do come with potential risks, says JLL's Matthew Haycox.

Any reform will create uncertainty and the proposed changes to shared ownership are no exception. Much of the discussion so far has focused on the administrative burden the changes will bring. But as yet, we haven't seen much modelling on the impact of these changes from registered providers.

"That is perhaps because the reforms look to schemes being funded in the 2021-2026 programme and those units won't be on the market for a couple of years yet," explains Matthew Haycox, a director in the affordable housing team at JLL. "RPs do, however, need to get their act together reasonably quickly.

"Modelling the changes is challenging. Whilst it is likely that staircasing in one per cent tranches will appeal in high-value areas, such as London and the South East, the initial equity stakes from homebuyers remains unknown."

Matthew believes that the reforms are likely to affect social housing viability in one of three ways.

"We may see any reduction in shared ownership valuations feed through to the land values RPs pay for a site, or we may see government support the new model with increased grant to plug any gaps.

"The third option is that things are just allowed to happen but that is likely to be followed by questions over the viability of shared ownership resulting in fewer homes delivered."

Matthew remains unsure whether staircasing in one per cent tranches will prove popular.

"The average price of a shared ownership home in the UK is currently £276,000, and with a 10% deposit on 10% equity means that home buyers are often finding a few thousand pounds to get on to the housing ladder.

"The demands on household income from holidays, entertaining and simply kitting out a new home may mean that appetite to staircase at a cost of £2,000 or £3,000 a year may not be as high as the government hopes.

"It may be that homeowners hold off and staircase every three or five years, with the reforms simply replacing a model that already exists."

How we can help

Our team provide advice on all forms of tenure and we are watching the developments of the new model carefully to ensure we provide clients with proactive advice as the final details become clear. As well as providing advice on the general implications of the reforms we can also help clients with more specific elements related to areas including:

- **Staircasing Increments and efficient processes**
- **The New Model Lease**
- **Repairs, Maintenance and Access Rights**
- **Litigation**
- **Finance, Funding and Grants**
- **Viability Assessments**
- **Planning and S106**
- **Tenure Switch**

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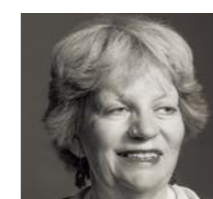
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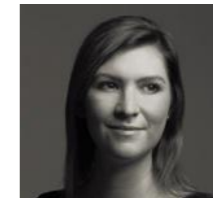
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‘They really understand the technicalities of the affordable housing sector; they are passionate in working with us, and they understand our objectives.’

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