DHLUC Consultation: The finances and sustainability of the social housing sector

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Introduction

This response includes observations that address the Committee's questions about shared ownership housing (question 8) and cross-subsidy models (Question 5) as well as institutional investors (Question 6). The key point of the submission is to consider the occupier outcomes when considering the finances and sustainability of the social housing sector. Consumer outcomes should be front and centre of deliberations in this space and that we should avoid constructing finances in such a way that the end housing offers prioritise the needs of providers at the detriment of tenants and residents.

The submission is from the Centre for Housing Policy, a research unit within the School of Business and Society at the University of York. The Centre has been established for 30 years and addresses policy driven impactful research across the housing system. Dr Alison Wallace, is a Senior Lecturer who has been at the Centre for 22 years, focussing to a large degree on low-income homeownership. Alison undertook doctoral study on housing markets and culture, but more recently has focussed on issues relating to low-income homeownership supported by finders that include the Joseph Rowntree Foundation, Abrdn Fair Finance, Lloyds Banking Group and DCLG. Alison has given evidence to Lord Best's HAPPI shared ownership for older people inquiry (2022/2023), the Greater London Authority examination of shared ownership (2020), has presented at shared ownership and leasehold sector conferences (regularly between 2008-2023 forthcoming) as well as being cognisant of trends and evidence on social and private housing drawn from other research studies undertaken as well as reading for teaching purposes.

The evidence contained in this submission is based upon four empirical studies in particular that are set out at the end. These studies are based on large numbers of qualitative in-depth interviews with shared owners, providers' staff, lenders, other stakeholders and observation of provider practices, as well as secondary analysis of large-scale datasets.

The key point being made is that the sector needs to remain focussed on consumer outcomes when considering how these products and social housing are funded and be satisfied that the offer can be further improved to rebalance the risk and reward between providers and consumers in shared ownership housing under any pivots towards alternative funding streams.

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Question 8: The Affordable Housing Programme includes a high proportion of shared ownership properties. To what extent is this form of tenure desirable for potential purchasers and for social housing providers.

- The shared ownership product and the finances derived from this tenure are central to the cross-subsidy model, producing income from first tranche-sales, staircasing (where purchasers increase their share of the property), from the rental stream on unsold equity, and perhaps to a lesser extent, from lease-extensions, fees, permissions, and management costs on service charges etc. In the face of reduced grant funding, the tenure's prominent role in cross-subsidising other housing provider activities has meant the providers' needs dominate in the shaping of the tenure and proposals for reform.

- In buoyant markets, shared ownership has often been oversubscribed, although sales may have slowed more recently as it is a pro-cyclical product that moves with the housing market cycle. Shared ownership offers an opportunity to have an equity stake in the property market, to be able to call themselves a 'homeowner' when this is valued as what a good citizen might be and considered an achievement in life (rightly or wrongly), and provides independence and relatively good quality, secure and affordable housing. This is especially the case when contrasted to most shared owners' previous residence in the private rented sector (PRS), that they consider to be precarious, and poor value for money when the costs are weighed against the quality of property and management, they frequently receive in the PRS. In these circumstances shared ownership appears an attractive proposition.

- Resident satisfaction in shared ownership is however poor. Internal housing association surveys demonstrate this, and the Tenant Services Authority (2008) found satisfaction to be lower among shared owners than for general needs tenants. More recently, 79% of general needs tenants are satisfied with their home compared to 56% of shared owners, reinforcing a Housemark study that found 57% overall satisfaction among shared owners compared to 83% among general needs tenants. Shared ownership satisfaction falls over time. Initial contentment of being able to access a form of ownership gives way to frustration with rising costs, an inability to staircase, and the imbalance of responsibilities in the management of the homes.

- Rising costs are associated with shared ownership, derived from over-inflation annual rent rises, using an outmoded higher definition of inflation (RPI not the lower CPI as used in general needs housing), repair costs and poorly controlled service charges especially related to flats.

- Estimates in my work and by Savills show that rising rents (often above the private rented sector over the market cycle) mean shared ownership costs converge with, and then would surpass, open market purchasers' housing costs over the long term (c.15 years) for a fraction of the equity benefits. Initial costs of entry to ownership are not sustained, and this is poorly understood by purchasers as no projections of medium- or long-term costs are provided at the outset even under the new model lease. When Government recently proposed a cap on general needs' tenants rents to limit the impact of high inflation, there was a sense that as costs had risen for general needs' provider expenditure and would not be covered by a lower rent increase, these shortfalls could be mitigated by shared ownership rent rises, for which there is no expenditure as repairs costs are recharged to shared owners. In the event shared ownership rents were capped at 7% the same as for general needs tenants. Nonetheless, this initial response emphasises the products' use to generate income potentially at the detriment of shared owners.

- These inflationary rents could be reformed as they can exert financial pressures on shared owners, but they make the product attractive to institutional investors and providers as a low yield-low risk investment who bring much needed funds into the sector. Institutional investors' main interest has to date focussed on shared ownership with the 2022 RSH Sector Briefing Notes illustrating how the number of for-profit providers has expanded rapidly and their holdings accelerated over the last five years. Whether this interest and investment would be maintained if the shared ownership product were more equitably devised is unclear.

- Over-inflationary rents were part of the original model of shared ownership as a push to transition to full ownership, by taking equity gains as a deposit on the open market or by staircasing in-situ. In the face of the decoupling of (stagnating) wages from house prices and low inflation the context in which purchasers achieved the transitions has gone. The proportion of staircasing is now low, Savills estimate around 3% per annum, and shared ownership has become a long-term permanent tenure for many purchasers rather than a transitionary product. The promise of full homeownership is an important hook at purchase, but people can often only do this if they move to lower cost markets, become a couple thus increasing household income, or by having a rapidly rising career and salary, events hard to control in policy terms. Failure to achieve full ownership can sit uncomfortably with many shared owners. By way of contrast, the new First Homes product, a discounted sale model based on a purchase of 70% of the home value, does not offer staircasing which is understood at the outset, but lower initial entry costs are maintained throughout. The drawback being that entry costs for First Homes are higher but consistent.

- Service charges are also problematic for many shared owners, and a source of frequent frustration. Providers pass on all management costs of the developments to shared owners regardless of the proportion of home purchased and so there are few incentives for associations and management companies to control costs with frequent complaints about apportionment/demises. Third-party management companies where providers are not freeholders complicate these scenarios further as they are unregulated and often do not provide regular accounts. Shared owners also have weak legal positions in multi-owned third party provided developments, with their lease being subordinate to the freeholder and providers' head lease resulting in shared owners' frequent exclusion from membership of management companies and the ability to have influence over how their homes are managed.

- The 100% repair costs incurred by shared owners regardless of the percentage of equity owned is a long-standing source of friction. Little appreciated at the point of purchase, over time that associations do not pay their own share of the upkeep of homes is a cause of shared owners' frustration. Providers' initial reactions to the fire safety crisis where they expected shared owners to meet 100% of the remediation bills highlights this imbalance in responsibilities. That this changed and shared owners were then expected to only pay their share in line with their proportion of purchased equity is official recognition of this problem. The new model lease rows back on minor repair costs in the first ten years, in the context that developers' defects periods and then insurance warranties would address significant issues. Associations were resistant to this modest reform as it would require greater funding, or more subsidy, without which they could build fewer homes. This is further illustrative of the way that beneficial consumer reforms can conflict with the cross-subsidy model and provider interests.

- The recently reformed model lease for shared ownership was however welcome. The model lease acknowledged that greater transparency was required about costs at the outset, that the repairs responsibilities were imbalanced and that lease lengths were too short, meaning that shared owners regularly incur more costs with lease extensions that could be avoided with longer leases. Unfortunately, this reform did not go far enough to restore the imbalance of risk and reward between shared owners and housing providers. For example, the key information documents do not contain long term costs, do not spell out the implications of the insecurity of equity if the home is repossess for rent arrears and the repairs payments in the first ten years may be more attractive for initial marketing than for the duration of the lease, and could disadvantage existing shared owners on old leases when selling their home.

- Shared ownership is based on leasehold and intersects with problems in that tenure. While 7% of open market homeowners are leaseholders, 100% are leaseholders. Leasehold is poorly understood with only a fraction of shared owners recognising themselves to be leaseholders in the *English Housing Survey* and so the provisions of a landlord-tenant relationship assured tenancy with the provider conflict with their sense of being owners.

- Shared ownership contains more lone parents, disabled people, women and single people for whom access to open-market homeownership is more constrained. Analysis of the Financial Conduct Authority's *Financial Lives Survey* shows that a greater proportion of shared owners are vulnerable to financial harm (53% compared to 37% of other mortgagors), considering themselves to be less financially confident, knowledgeable, savvy and with fewer resources and or greater debts to provide a financial buffer against income shocks or rising costs. Affordability pressures are reduced for people buying shared ownership in London and the South East rather than on the open market, elsewhere, where incomes are lower, 31% of shared owners have housing costs that form more than 35% of their incomes, compared to 17% of other mortgagors. Associations do well to support people and help those struggling financially to sell up to avoid formal repossessions, but the product could be reconstructed to alleviate some of these pressures forming. More affluent than general needs tenants, nonetheless shared owners are price sensitive and not uniformly a group that transition to full ownership quickly, navigate a complex financial product and bear any associated rising costs.

Conclusion

For the reasons set out above, shared ownership is appealing as it provides a low-cost entry to a form of ownership. It is an enduring product with much sector expertise and some (growing) consumer awareness. Shared ownership has been subject to reform but the main imbalance of risk and reward for purchasers and providers over time remains. The new lease has made a welcome but modest contribution to rectifying this. The cross-subsidy model means that providers have been slow to affect the changes required as in the current funding climate they are reliant on the funds generated from the product. To date there has been a narrow focus on sales and the entry into ownership and limited focus on consumer outcomes over time. A wider set of indicators are required to understand what the sector achieves for purchasers in the long run. Reducing their reliance on the income streams from shared ownership may open up space to think more closely about purchasers’ long-term outcomes and rebalancing the sector. Whether a reformed sector may be attractive to institutional investors as it is now is uncertain however, but when considering new financial regimes for social and affordable housing the consumer interests must also be represented.