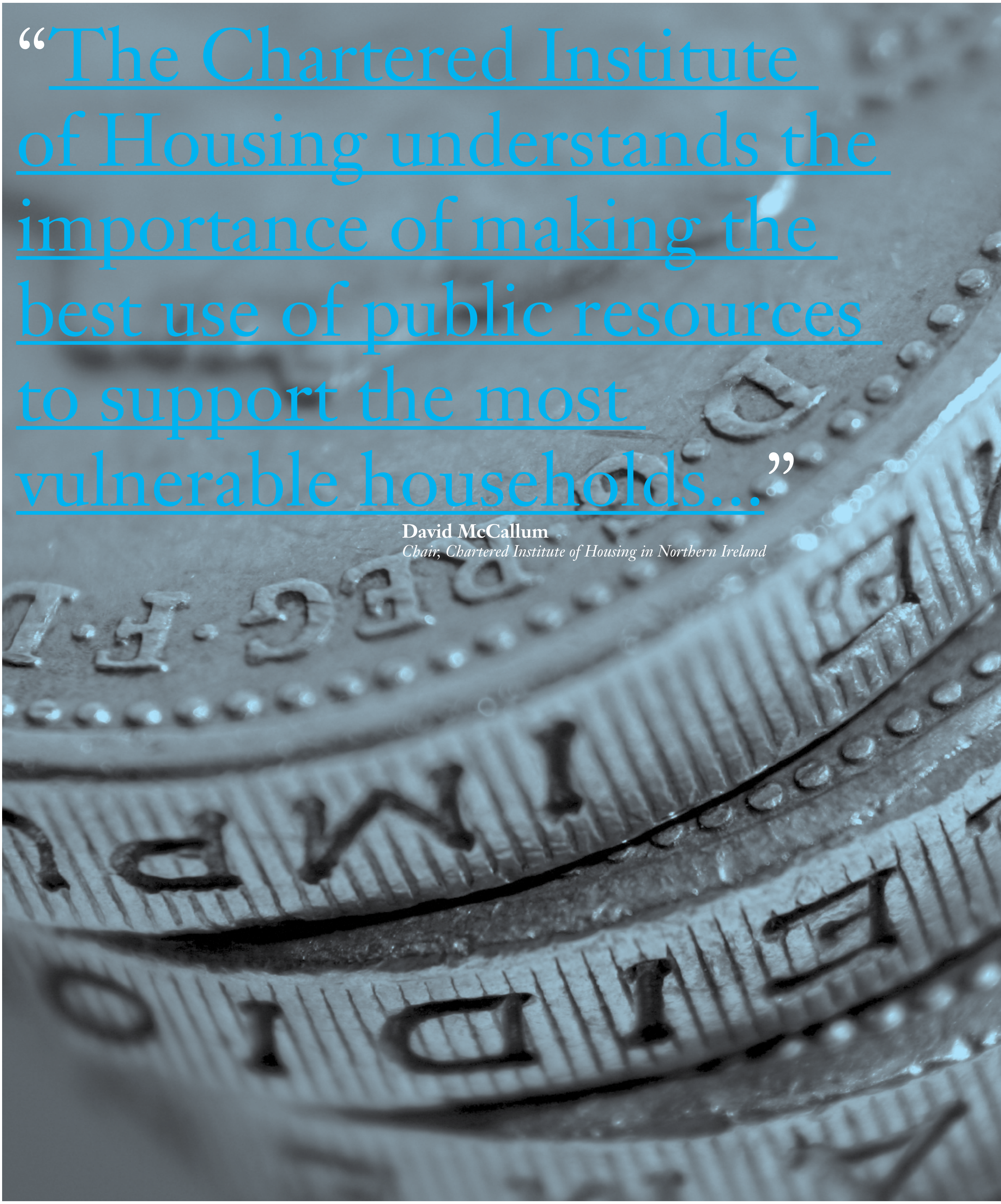
Northern Ireland

A New Way of Helping Homeowners:

Moving from Grants to Loans for Repairs and Improvement Work



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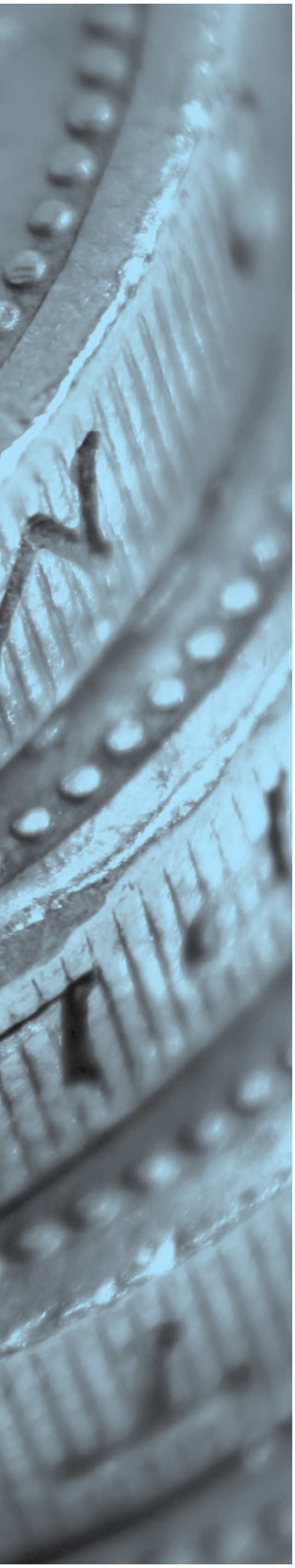
David McCallum
Chair, Chartered Institute of Housing in Northern Ireland



Foreword

Sustainability is a concept firmly embedded in our consciousness these days – we use it in connection to the environment, our communities, technology, building practices and the economy. Whilst sustainability is most commonly associated with environmental and social factors, it is likely to become increasingly important in relation to the economy and financial measures, as the recession continues to bite and the full impact of public spending cuts to reduce the UK deficit start to kick in. Government spending, which in the recent past was plentiful, will now be increasingly constrained and many worthwhile programmes and projects may fall by the wayside unless we are able to be more creative and innovative in the way we use available resources.

The Chartered Institute of Housing understands the importance of making the best use of public resources to support the most vulnerable households and is committed to finding solutions to ensure that housing stock is fit-for-purpose and of a high standard. For this reason, we commissioned Rachel Terry to undertake an examination of alternative approaches to supporting homeowners to repair and improve their properties.

As of 2009 there were 461,000 owner-occupied dwellings in Northern Ireland, comprising 62.3% of the total housing stock. Unfitness in owner-occupied properties is relatively low and the condition of this stock has continued to improve in recent years. However, the fact remains that a quarter of all unfit dwellings in Northern Ireland are owner occupied.

The Northern Ireland Housing Executive has provided an invaluable source of assistance for homeowners seeking to make improvements to their properties through the private sector grants programme. This programme enables homeowners to apply for grants to renovate, repair or improve their homes and also facilitates mandatory disabled adaptations to owner-occupied dwellings. However, it is highly likely that the resources available to fund the private sector grants programme are going to be severely constrained for the foreseeable future, as public expenditure cuts reduce the amount of money available for the housing budget. Conversely, demand for grant assistance is likely to rise. Many homeowners who would previously have accessed commercial lending products for repairs and improvements or used their savings may find themselves increasingly unable to do so. Adaptations for older and disabled people are also likely to become more important in order to meet the needs of Northern Ireland's ageing population and enable older and disabled people to remain comfortably and safely in their own homes.

If this need for assistance is to be met, then new approaches to funding repairs and improvements will be crucial. Even without the existing and imminent cuts to public spending, there would be a case to be made for a more sustainable model of helping owner occupiers maintain their properties. The current model is of necessity only able to help a limited number of people, but there is scope to make securing financial assistance with repairs and improvement work more widely available to a broader range of homeowners.

The Department for Social Development is currently reviewing the private sector grants programme with a view to creating a more sustainable and accessible system of helping owner occupiers maintain their homes. We believe that this paper will make a valuable contribution to that review by focusing on one aspect of restructuring the present system. Rachel Terry has examined the potential inherent in moving towards a loans-based system of providing assistance to homeowners and discussed some of steps that would need to be taken in order to introduce such a system in Northern Ireland.

David McCallum
Chair, Chartered Institute of Housing in Northern Ireland

Introduction

The purpose of this paper is to consider alternatives to the operation of the current private sector grant regime in Northern Ireland. By looking at the types of financial assistance offered in other areas within the UK and Republic of Ireland and considering an alternative approach in some detail, this paper is designed to encourage discussion and debate at a policy level and inform ongoing thinking in relation to private sector grants.

This paper refers only to discretionary or non-statutory grants and does not advocate any change to the way in which mandatory grants, such as the Disabled Facilities Grant, are managed. We would expect any changes to the existing policy on the discretionary grants system to be subject to an Equality Impact Assessment.

The grants system administered by the Northern Ireland Housing Executive has been immensely popular and has undoubtedly contributed to the low levels of unfit housing in Northern Ireland.[1] However, the fact remains that a quarter of all unfit properties in Northern Ireland are owner-occupied. This is why the Housing Executive's grants strategy is so important as it "targets grants towards properties most in need of improvement and repair [and] helps ensure that the 'deterioration flow' into unfitness is more than outweighed by the number of dwellings being brought up to modern standards".[2] However, the grants programme has been significantly affected by the economic downturn and subsequent constraints on the housing budget, with the Housing Executive expecting to have approved only 2,000 grants in 2009/10 compared to the more usual 7,000.[3]

Problems with funding for the grants system arose in late 2008/ early 2009. There was an initial allocation of £20m for 2009/10. This was insufficient to cover commitments, so all discretionary grants were then approved on an exceptional basis only. Monitoring rounds in June and December provided a further £15m and £9.7m respectively, bringing the total spend for 2009/10 to just under £45m for both mandatory and discretionary grants. The 2010/11 budget for home improvement grants, both mandatory and discretionary, is only £30m — so private sector grants are already being significantly impacted by spending cuts.[4] >

1 According to the preliminary findings of the Northern Ireland Housing Executive's 2009 Stock Condition Survey, only 2.4 % of dwellings in Northern Ireland are deemed to be unfit. This is an improvement on 3.4% in 2006 and 4.9% in 2001. This decline in unfitness across all housing stock has been attributed to "the high rate of new dwellings construction, the interest in improving existing homes in the private sector (assisted by grants expenditure), as well as continued investment in social housing in the years 2006 to 2009)". Unfitness in the owner-occupier sector is now down to just 0.9%. http://www.nihe.gov.uk/2009_house_condition_survey_preliminary_findings_feb_2010.pdf

2 Northern Ireland Housing Executive, *Northern Ireland Housing Market Review and Perspectives* 2010-2013, pp.77-78

3 http://www.nihe.gov.uk/index/hig_home.htm

4 *Northern Ireland Housing Market Review and Analysis*, p.33

> As we move towards the Comprehensive Spending Review it is inevitable that difficult decisions will have to be taken with regard to public expenditure. In January, the Finance Minister, Sammy Wilson, confirmed that the Northern Ireland Executive will face spending cuts of £367m in 2010/11.[5] The most recent Northern Ireland Economic Outlook reports that the Northern Ireland economy shrank by 4.5% over 2009. Looking ahead, it notes that public expenditure is falling and anticipates even deeper spending cuts in the next spending review period. The Economic Outlook goes as far as referring to a "public spending crisis" and the "opportunity for radical reform", with the Northern Ireland Executive needing to identify "substantial new sources of income" and to do more with less.[6] Following the 2010 general election, the UK Chief Secretary to the Treasury announced further reductions in the spending of the three Devolved Administrations in 2010/11 or 2011/12 totalling £704m.[7]

Budgetary constraints should not restrict the provision of grants that are mandatory, such as Disabled Facilities Grants and Mandatory Repair Grants. But if Northern Ireland is to continue to offer a service to owner-occupiers and landlords who are unable to access private borrowing streams to repair, renovate and improve their properties, then options other than grant aid will have to be considered. As most homeowners who receive grants for repairs and improvements benefit from an increase in the value of their home as a result of the grant funded work, a different payment arrangement might be acceptable in the future.

In considering other options, it is necessary to recognise how the pressing need to reduce the UK's deficit may affect the acceptability of alternatives. The cash flow of the public sector (and hence its need for net borrowing) seems likely to become a much more significant consideration than in the past. This suggests that any alternative policy would need to concentrate on the financing of works by loans, rather than grants; and that those loans would need to be financed predominantly by the private sector.

There are several key issues that would need to be taken into account when considering whether the replacement of grant aid by loans would be of practical help in the short to medium term. These are:

- Changing attitudes to borrowing for improvement work;
- The basis on which loans would be provided and by whom;
- How soon loans could be repaid; and
- How the change would be regarded in public finance.

This paper will consider each of these issues in relation to Northern Ireland before setting out some findings and conclusions. Much of the analysis is drawn from two research projects commissioned by the Greater London Authority (GLA) in 2007/08 – *Barriers to changing from grants to loans in London* and a feasibility study of *A self-sustaining, pan-London, affordable loan fund*.[8]

"if Northern Ireland is to continue to offer a service to owner-occupiers and landlords who are unable to access private borrowing streams...then options other than grant aid will have to be considered..."

5 http://www.niassembly.gov.uk/record/reports2009/100112.pdf

6 PriceWaterhouseCoopers, *Northern Ireland Economic Outlook*, March 2010 www.pwc.co.uk/ni

7 HM Treasury Press Notice PN4/10, issued on 24 May 2010, downloadable at www.hm-treasury.gov.uk/press_04_10.htm.

8 These reports by Rachel Terry and Richard Gibson have not yet been published, due to the change of Mayor in 2008. However, it is hoped that they will shortly be available.

Northern Ireland Background

The current private sector grants system stems from 2003 when the Housing (NI) Order enacted a number of changes to the existing grants system. Renovation, Replacement and HMO grants became discretionary and the Minor Works Assistance Grant was replaced by the means-tested Home Repair Assistance Grant.

The Northern Ireland Housing Executive reviewed the grants system in 2003 with a view to introducing a more targeted approach to the discretionary grants scheme. Its paper – *Targeting Grant Aid in Private Sector Housing: A Strategic Approach for Northern Ireland* – took note of changes happening across Great Britain with the comment that government was:

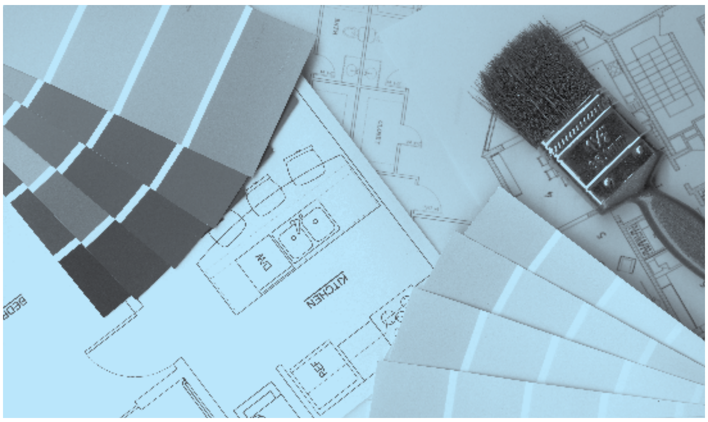
"[…] allowing local authorities even greater discretion over the way in which condition problems are tackled, supplementing traditional grant aid powers with new powers to offer loans and other forms of assistance."

Although cognisant of a growing movement away from grants for discretionary improvements to privately owned properties, the Housing Executive did not discuss these new funding alternatives in its strategic review. One reason for this is that there was no real need to consider a different funding model because the grants scheme had a consistently high level of public funding support, with around £42m/ year allocated to private sector grants. Even in the event of future budgetary pressure, the review suggested that restricting grant aid and/or introducing queuing might need to be considered, rather than addressing other forms of financial assistance. In addition, the Housing Executive review was primarily focused on moving from a mandatory grants scheme to a mainly discretionary model that was more strategic and targeted in its approach. Therefore consideration of loans at this stage would not have been appropriate within the context of the review.

From the review of private sector grants in 2003 to March 2008, grant expenditure remained at over £40m each year, with somewhere in the region of 7,000 grants approved on a yearly basis. There was an internal review of the grants system in 2007 and loans were considered as part of this process; but it was felt at the time that there was not enough information upon which to determine if a loans-based model could be successfully introduced in Northern Ireland.

However, as already mentioned, in 2009 the grants system was severely affected by the economic downturn and the resultant pressures on the housing budget, with applications for discretionary grants being approved only in exceptional circumstances.

The Department for Social Development is currently undertaking a review into the private sector grants system and it is hoped that this paper will be of use to the review process by providing an independent view of possible ways forward in funding repair and improvement works for owner occupiers.



9 Northern Ireland Housing Executive, *Targeting Grant Aid in Private Sector Housing: A Strategic Approach for Northern Ireland*, 2003 p.3

10 Information provided by the Northern Ireland Housing Executive, June 2010

11 Ibid.


I PROMISE TO PAY THE
FIVE POUNDS

What's happening elsewhere?

The power to administer housing grants and loans is in the hands of local authorities in England, with each local authority taking a slightly different approach. Since 2003, these authorities have been relieved of detailed prescriptive arrangements for supporting housing renewal and have been encouraged to devise a wider range of ways of promoting this policy. Responding to financial constraints, there has been a trend of restricting the availability of grants and a search for alternative forms of financial support through loans and equity release. But progress in developing such alternatives has proved slow.

A widespread scheme using private finance is offered by the Home Improvement Trust under the 'HouseProud' name. Borrowers normally receive an interest-only mortgage on which the interest is met by the Department of Work and Pensions, a lifetime mortgage with rolled-up interest, or a standard mortgage with interest payments. The scheme has been in operation for several years, but take-up remains relatively small.

Some local authorities, particularly a number of London Boroughs, offer interest free loans in place of grants. Others have devised loan schemes in which the amount to be repaid when the property is sold is expressed as a proportion of the value of the property; the proportion is based on the amount of the loan as a proportion of the value of the property at that time. Examples of this approach include Kirklees Council, some authorities in the West Midlands and some in the North West.

Kirklees Council, for example, provides Home Appreciation Loans through their Private Sector Housing Unit. These are designed to help homeowners bring their properties up to a decent standard and are open to vulnerable homeowners, such as the over 60s, low earners and those claiming certain benefits, who are unable to access commercial borrowing. The minimum that can be borrowed is £2,000 and the maximum £30,000. The loan is calculated as a percentage of the total value of the house and is repaid when the house is sold.

In the West Midlands, local authorities do not make loans themselves. Instead, ART Homes (a not-for-profit organisation) provides affordable finance for maintenance, repairs and adaptations for low-income homeowners. A local authority will refer a homeowner seeking financial assistance to ART Homes, who will then assess their property, needs, circumstances and suitability for a loan. They will then suggest to the homeowner how much they could afford to spend, by borrowing. The local authority then confirms the work and its cost directly with the homeowner and contacts ART Homes on their behalf if they wish to proceed. Once the loan is confirmed and funds are issued, the local authority arranges the repair work through Home Improvement Agencies or certified builders. The local authority is involved throughout the process, providing a degree of assurance for the homeowner; the loan is provided by a non-commercial lender at reasonable rates through an equity share loan product; and the work is carried out by reputable and approved builders. >

"Responding to financial constraints, there has been a trend of restricting the availability of grants and a search for alternative forms of financial support through loans and equity release...."

12 Office of the Deputy Prime Minister, Circular May 2003.

13 *Loan Finance to improve housing conditions for vulnerable owner occupiers*, Department of Communities and Local Government, April 2007.

14 www.kirklees.gov.uk

15 http://www.mercian.org.uk/pages/art_homes/default.aspx. ART Homes is part of the West Midlands Kickstart Partnership; a regional partnership that supports local authorities in delivering loan based housing assistance. The aim is to address poor housing conditions in private sector housing by using public funds innovative to maximise their impact.. http://www.wmkickstart.co.uk/about_us

> In the North West, some local authorities (such as Oldham and Rochdale) finance loans by a housing association for home improvement work. Repayments are based on the growth in property values, subject to a maximum percentage.

In Scotland, private sector housing grant is being replaced with schemes of assistance set out in Part 2 of the Housing (Scotland) Act 2006. Grants can still be given and are mandatory for providing amenities for people with disabilities. However, owners are now expected to take more responsibility in maintaining their homes and, if applying to the authority for a grant or loan, the applicant must also make a contribution to the work. Owners can apply for assistance, in the form of grants and loans and advice, under the authority's scheme of assistance, but it is no longer mandatory for local authorities to provide a grant and it is up to each local authority to make that decision.

As in England and Scotland, private sector housing renewal in Wales is carried out by local authorities. This is funded through both grants and loans in accordance with guidance produced by the Welsh Assembly Government. Funding is provided for older people and people with disabilities through Care and Repair Agencies.

Local authorities in the Republic of Ireland offer housing grants and financial assistance for those seeking accommodation in the private sector and those wishing to upgrade their homes (within certain categories). Grants schemes and assistance for improvement work are geared towards those who are in most need of support, such as older people and people with disabilities. Loans are available for improvement work to privately-owned homes – up to €15,000 for an unsecured loan and €38,000 if the loan is secured by a mortgage on the house – at variable interest rates.

Although it can be seen that some other jurisdictions have already moved away from funding private sector home repairs and improvements solely through grant aid, Northern Ireland continues to rely predominantly on a grants-based system.

Responding to anticipated pressure to change

"It is highly unlikely that the Northern Ireland Housing Executive will be able to carry on indefinitely providing even the current level of funding for repair and improvement grants..."

The pressure for change in Northern Ireland seems likely to arise from the restrictions the new UK administration is placing on the sums allocated to the devolved administrations. Such restrictions are driven primarily by the need to reduce the UK's borrowing to finance public expenditure. This means that the cash requirement of any future scheme is likely to be much more significant than it would have been in the past. It will be important to keep this in mind. [In the past, the UK's ability to borrow would have been a minor consideration compared with the way in which a particular kind of spending would have been treated in public expenditure.]

The aim of this paper is to consider how it would be possible to move to a loan scheme in Northern Ireland and to make some suggestions as to how that might be progressed. Current and future budgetary constraints on the Northern Ireland Executive as a whole and the reduction in capital receipts for housing point towards the need for a new and sustainable model of government assistance for private sector works. It is highly unlikely that the Northern Ireland Housing Executive will be able to carry on indefinitely providing even the current level of funding for repair and improvement grants, let alone return to the days when £40m was provided for such work each year.

Replacing grants with loans – first steps

The fundamental change that would need to happen, in order to see loans begin to replace discretionary grant aid as an acceptable means of funding repairs and improvements to private dwellings, is fairly obvious – attitudes would need to change. Experience in Great Britain is that many home owners would be reluctant to borrow against the value of their home and would choose to defer works in the hope that the generous grants of the past might return, however unrealistic that hope may seem to housing professionals.

62.3% of the population in Northern Ireland are owner occupiers, equating to 461,000 households. Nearly 1% of those households (4,400) are deemed to be living in unfit properties. These figures are taken from the preliminary findings of the 2009 House Condition Survey and demonstrate that unfitness levels in Northern Ireland continue to fall in the private sector (indeed across all sectors). There are several possible explanations for this:

- the high rate of new build construction in the private sector in recent years; and

- the success of the private sector grants system which has enabled large number of owner-occupiers to make necessary repairs and improvements to their homes in order to make them fit for habitation.

These figures lead to two alternative arguments in relation to grant aid:

- it has clearly had a successful impact on levels of unfitness in the private sector, ensuring that owner occupiers, in particular vulnerable owner occupiers, are able to live in safe, energy-efficient, comfortable homes. Therefore, the government should continue to fund the grants system to as high a level as possible, given the evidence of its effectiveness; or

- the extremely low levels of unfitness among owner occupier households, fewer than 1%, mean that government funding should be targeted at areas of greater need, particularly in a situation when the housing budget is falling year on year and faced with a number of competing pressures.

Both arguments have their merits, but the purpose of this paper is to explore a third way of approaching the economic reality. It suggests a way in which owner occupiers of unfit housing might still be able to improve their homes, but with fewer demands on the public purse. This approach relies on the use of loans to pay for works that would, in the past, have attracted grants.

The freeze on private sector grants in 2009 provoked considerable debate in the media and amongst political representatives about the continued need for this type of funding. The Department for Social Development was placed under considerable pressure to find the money from within its budget to maintain funding of repair and improvement grants. In the end, the Department was able to secure additional funding through in-year monitoring – a sign of the successful lobbying by homeowners, construction firms and MLAs. However, as public spending cuts begin to be felt across the board – in health and education especially – it is unlikely that such a solution could be repeated.

So political representatives, homeowners, and the media, are all likely to be reluctant to accept the need to constrain funding for private sector grants, notwithstanding the tightening of the Northern Ireland Executive's funding and the relatively limited scale of unfitness in owner-occupied housing in Northern Ireland. If repairs and improvements for vulnerable homeowners are to continue to be government-assisted, it will be necessary to offer a fresh approach that makes much less demand on public funds. >

> A key issue to be addressed when introducing a new model is to ensure that it is viewed as a permanent/long-term change. There is evidence that in England many people hold off taking out a loan for repair and improvement work because they think that grants may be reintroduced in a few years. Although housing professionals may deem work to be essential and/or urgent, most owner occupiers believe that, even if significant work is required, it can be deferred until a more favourable means of funding it is introduced. For a loan scheme to be successful in Northern Ireland, it would be vital that all interested parties understand the scheme to be permanent and for the grant regime to be adapted as quickly as possible to work alongside the new loan arrangements.

16 Department of Communities and Local Government, *Loan Finance to improve housing conditions for vulnerable owner-occupiers,* 2007 (paragraphs 6.13 and 6.23)

The most successful model in England is an equity loan, as provided by Kirklees and ART Homes (described above). This product might eventually be close to being self-financing. Although it relies initially on public sector capital for the loans, repayments are uplifted in line with property values. The repayments can be advanced as new loans. An estimate is made below of the time it is likely to take before loan repayments would start to make an impact and so reduce the need for public expenditure for new loans. The drawback, in present circumstances, is that very little of the loans is likely to be recycled in the first few years; so the impact on the UK deficit in the next few years would be very similar to that of providing the same sums as grants.

These equity loans offer homeowners more attractive terms than are available from commercial lenders. So they are also likely to be sought by people who could borrow commercially, thereby increasing their impact on the UK deficit more than absolutely necessary to achieve the level of home improvement work required. If equity loans were pursued in Northern Ireland, it would be important to ensure that they were confined to people who could not borrow commercially, if their cost to the public sector, and their impact on the UK deficit, was to be kept to a minimum.

In London, the GLA found that the main barrier to the use of loans instead of grants was the reluctance of homeowners to borrow against the value of their homes. This is not something confined to vulnerable homeowners who need capital to fund repair and improvement work, it is also a feature of the commercial equity release market. However, a study carried out for the Department of Communities and Local Government did find that although vulnerable homeowners view loans as a last resort they will take out a loan to finance repair and improvement work on two conditions. One is that they deem the work to be absolutely necessary and have no alternative source of funding; the other is that the terms of the loan must be favourable – in most cases this meant that there were low costs and no repayment of the loan required in the homeowners lifetime.[16]


CHIEF CASHIER

How could loans be provided and by whom?

Commercial loans for repair and improvement are normally available to a wide range of homeowners. But some owners are unwilling to take up the loans that are available to them and some other owners are unable to do so, because of their financial circumstances, or the nature of their property.

The unwilling are likely to be older homeowners. They are generally able to secure rolled-up interest loans (a lifetime mortgage loan) from commercial lenders; however, they are often reluctant to take out such a loan because they are unsure how much money will eventually be repayable. Even though the homeowner is assured that the repayment will never exceed the value of the property, there is still a reluctance to use this type of loan product amongst many older homeowners. There is much evidence that lack of trust in the products and/or the providers is an inhibition. The involvement of a trusted body may persuade some of the unwilling to make use of these commercial loans.

Those unable to borrow commercially are likely to include:

- homeowners on benefits or uncertain incomes who wish to carry out work over and above what would be covered by a grant (i.e. essential work that addresses unfitness); and

- homeowners who are unable to offer sufficient security for a loan. This would affect owner occupiers living in a type of property not considered suitable for commercial loans and those who already have large debts secured against their properties.

The costs of setting up a secured loan may also prove problematic for a number of owner occupiers, particularly those in vulnerable groups, although most lenders will agree to these costs being added to the loan. Homeowners who would have applied for a relatively small grant – say less than £5,000 – would have to pay about £1,000 in loan charges to obtain a loan. This would be seen as completely disproportionate by some, despite the value of works often adding to the property value.

Indeed, because of the significant legal costs involved in securing a loan with a mortgage, it is unlikely to be appropriate for small grants to be replaced by secured loans. A new model might take the risk of loans of less than £3,000, say, being unsecured, which would avoid a valuation fee and reduce legal costs.

If loans are to be considered as an alternative to private sector grants, then they must be affordable, given the income of the borrower. Where the borrower is old enough (e.g. over 65) to be able to obtain a loan with rolled-up interest from a commercial lender, there is no call on income because the interest is not repaid until the borrower dies or moves permanently into residential care; so such a loan is affordable. But where the borrower is younger, interest on a commercial loan will be payable out of income and may thus be unaffordable for those on very low incomes. (An exception arises when the borrower is on benefit and the works are deemed 'essential' by the Department of Work and Pensions; in such cases, the borrower receives extra benefit that, broadly, covers the interest.) There are three main ways in which public sector loans could be made more acceptable than commercial loans:

- if they had softer terms – essentially if they cost less than commercial loans;

- if they were more widely available – for instance, if they were an option for people and properties turned down or likely to be turned down by commercial lenders; and

- if there was a reassuring provider – basically if homeowners could feel confident in the organisation providing the loan in a way they might not if it was a commercial lender.

If these three factors could be accommodated and a satisfactory framework put in place, then it is possible that homeowners in Northern Ireland could in time be persuaded to take out a loan for repair and improvement work, so long as they were convinced that no grant funding was in prospect. >

1. Softer Terms

> Loans on offer to homeowners who would have previously applied for grants could differ from commercial loans by:

- offering smaller and larger loan amounts;

- charging a significantly lower rate of interest (or even none at all) or perhaps charging a proportion of the growth in the value of the property when the work is completed; and/or

- charging reduced fees or possibly no fees at all.

Those homeowners receiving benefits, such as pension credit or income support, would not be in a position to pay interest each month, so they would need a loan product that does not require any payments out of income. By repaying a loan from the proceeds of the sale of the property, there are three loan types that circumvent the need for a monthly repayment from a limited income – interest-only loans for qualifying works where the interest is funded by the Department of Work and Pensions in extra benefit, equity share loans and rolled-up interest loans.[17]

Such softer terms would all contribute towards making loans a more attractive and affordable option for many people; however, in order to offer these softer terms the public sector would undoubtedly have to subsidise the loans. The questions to be asked are:

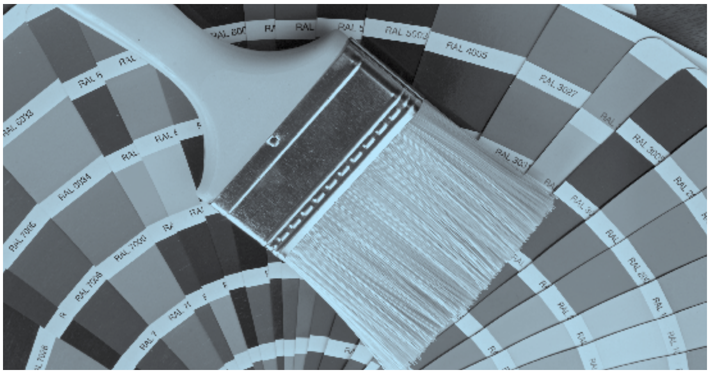
- how much subsidy would be required?; and

- how much would it save in public expenditure compared with the current discretionary grants system?

And, in view of the focus on the UK deficit, it would also be important to ask further questions:

- how much more subsidy would be required if the loan were made by a commercial lender rather than a public sector body?; and

- how much less finance would be needed from the public sector if a commercial lender made the loan (even though it was to be subsidised)?



17 An equity share loan is one under which the amount to be repaid is a proportion of the value of the property, agreed at the outset. Repayment is usually based on the value of the property when it is eventually sold. With a rolled-up interest loan no payments are made during the term of the loan. Instead, interest is added to the amount borrowed each year, on a compound basis, and the loan is repaid when the property is eventually sold.

2. Wider Availability

Ideally, a loans scheme would need to apply as widely as the existing grants scheme. Currently repair and improvement grants are available to those who could not borrow commercially, such as those with a poor credit history or a very low income, and those living in leasehold properties with less than 70 years of the lease remaining. These are both factors that are likely to exclude an applicant from obtaining a loan from a commercial lender, although for a rolled-up interest loan the lender would be concerned only about the age of the borrower and the mortgageability of the property. Depending on how the new loans scheme was financed, lending to such households might have an additional cost attached, if a commercial lender needed either a premium or an indemnity to be willing to widen the availability of loans to such excluded groups. >

3. A reassuring provider

> Some of the commercial lenders who provide the loan products most relevant to vulnerable homeowners are names that might be unfamiliar to people and there may be a reluctance to enter into a loan agreement secured on their property with an unknown lender. This could potentially be an issue for older homeowners who would be looking at lifetime mortgage loans. The organisation providing loans in a new model would therefore have to be one that the vast majority of owner occupiers and vulnerable homeowners could place their trust in.

An obvious candidate would be the Northern Ireland Housing Executive which currently administers all private sector grants. If a loans model is developed to replace some or all discretionary grants such as Renovation Grants, Replacement Grants and Home Repair Assistance Grants, it would run alongside the mandatory grants system which would be unaffected by the loans model.[18] The Housing Executive would continue to fund Disabled Facilities Grants, Mandatory Repair Grants and HMO Grants.[19] It therefore makes sense to keep all the components of repair and improvement to private sector homes under one roof, so to speak. A non-departmental public body, like the Housing Executive, is likely to provide the necessary level of assurance for the majority of owner occupiers in Northern Ireland.

From an applicant's point of view, the question is how such a model might work? From the Housing Executive's point of view, the question is would it wish to become a loan provider, with all the regulation involved, and take on such a role, particularly in light of a period of organisational change? From the Government's point of view, the question is would they be willing to fund it?

If a Housing Executive loan scheme was to be introduced to replace grants, it would need to complement what the commercial market is offering. To succeed in being complementary, it would be essential that it did not offer scope for borrowing to people who could obtain commercial loans; otherwise the limited funds available would not be deployed to greatest effect. The Housing Executive's loans would need to be targeted at those whose income or property value is insufficient for a commercial loan, where a loan type is needed with no commercial lender, or where up front costs are disproportionate to the size of loan required.

As mentioned earlier, there are three types of loan product that seem best placed to deal with the needs of owner occupiers who currently apply for private sector grants. Of these, **interest-only loans** could be provided by mainstream commercial lenders and be indemnified where necessary by the Housing Executive. A meeting with the Department of Work and Pensions would be useful to establish exactly which works would qualify for additional benefit payments for loan interest, so that the Housing Executive could evaluate the importance of having such loans available. A discussion with Treasury would be needed to understand how such indemnities would score in the government's accounts and what impact, if any, they would have on the UK deficit.

Rolled-up interest loans could be provided by mainstream commercial equity release lenders to most older homeowners over 65 without subsidy, but a degree of government/public sector support towards the fees for arranging such commercial loans might be needed to increase take-up.

The Housing Executive would then only need to provide **equity sharing loans**, or provide the capital for such loans to be provided by a commercial lender, and small unsecured loans. The following two paragraphs explain why equity sharing loans cannot realistically be provided by a commercial lender without 100% capital subsidy or revenue subsidy that would be unaffordable. >

18 A new scheme might be only for loans over £3,000, say.

19 Funding for LOTS Grants will transfer to local councils as part of the Review of Public Administration.

"The organisation providing loans in a new model would therefore have to be one that the vast majority of owner occupiers and vulnerable homeowners could place their trust in..."

> An equity sharing loan under which the amount to be repaid on sale is increased in line with the growth in the value of the property seems likely to be acceptable to many lower income households, given experience of such loans elsewhere in the UK. But such terms do not provide sufficient return to attract commercial lenders to offer equity sharing loans. For example, the existing home reversion market, which offers funds on a basis comparable with equity sharing loans, requires payment of a significantly larger proportion of the eventual sale proceeds than the proportion of the property value that it provided at the outset.

So if an equity sharing loan were constrained to require repayment of only the same proportion of the value as it provided at the outset, an unaffordable subsidy from the public sector would be essential. For example, if a commercial lender wanted 30% of the value of the property when it was sold, having lent only 10% of the value of the property at the outset, the public sector would need to stand willing to provide a subsidy, at the time of sale, of the gap of 20% of the value of the property at that time.

There would be two key positive outcomes if the Housing Executive decided to take on the role of facilitator for the first two loan products and lender, or capital funder, for equity sharing loans. The first relates to public confidence and changing attitudes – reluctance to borrow might be overcome if such a reputable and recognisable public body was publicising the availability of these loans. The other is that equity sharing loans would become available in Northern Ireland, provided either by the Housing Executive itself or by a commercial lender with capital funding from the public sector. This latter approach would enable the loan function to be outsourced, saving the Housing Executive from having to carry out the relevant administration and reducing significantly the demanding requirements of the Financial Services Authority with which the Housing Executive would need to comply. Co-branding and retaining overall control would ensure that public confidence was not lessened.

It is also possible that if equity share loans were available through the Housing Executive, private sector landlords would be willing to negotiate a loan rather than wait for a Mandatory Repair Grant (which can take many months). This would mean that there could be savings in mandatory grants, even without any change in the rules governing entitlement to them.

In facilitating interest-only and rolled-up interest loans, the Housing Executive could negotiate with commercial lenders for these products to be packaged and promoted locally for homeowners likely to benefit from either of these products. Housing Executive staff could signpost these products for people enquiring about grants for repairs and improvement to their homes. Charges for setting up these loans could be agreed with the lenders and some of the grants budget could be used to cover the borrower's loan arrangement costs, directly through the lender, if there was evidence that this would increase take-up significantly.

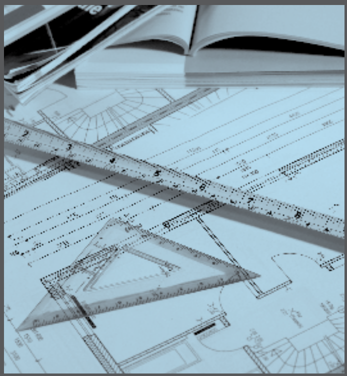
Potential borrowers would need to be advised to seek independent financial advice before entering into any type of loan agreement.

It goes without saying that this restructuring would take considerable re-thinking, effort and resources and involve significant re-branding of products, re-marketing of services and retraining of staff. However, it is a possibility and the challenges would not be insurmountable if the will for change was present across the housing, public and private sectors.

There could also be additional pressure placed on Northern Ireland's two Home Improvement Agencies who currently provide information, advice and practical support to older and disabled grant applicants, as commercial lenders would expect the works to be project managed by an appropriate organisation. There may also be a need for a further HIA to support those homeowners who do not fall into either of these groups, but who would still need assistance in taking out a loan and would want the work on their property to be project managed.

How swiftly might replenishment take place?

If the Housing Executive were to provide funding for equity loans for home repairs and improvements, the eventual repayment of the loans, at their enhanced value, could provide funds with which to finance further loans. Thus, in the medium to long term, the net cost of supporting home repairs and improvement would reduce and may in time become self-sustaining, i.e. require no more public funding. But how long might that take?



Financial modelling for the GLA suggested that, in London, an equity loan fund would have some recycled funds available for new loans within 10 years, but would not be close to becoming self-sustaining (i.e. the amount of equity loan repayments becomes equal to new equity loan requirements) for about 25 years. As Northern Ireland has a history of infrequent house moves, it seems unlikely that its equity loan fund would become self-sustaining any more quickly. Creating affordable loan products means that the loans would not be repaid until the property is sold, which could take many years. For older borrowers the repayment of their loan is primarily determined by their longevity, while for younger borrowers the fact that they have taken out a loan repayable on sale might encourage them to remain in that property for longer. So the replenishment of funds for new loans would not be a speedy process.

As fewer homeowners are likely to take up equity loans than would have taken up grants, the cost to the housing budget would almost certainly be considerably reduced in the early years of a loan scheme.

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How the change would be regarded in public finance

Government is likely to consider any change to the current system by reference to its impact on the UK deficit and not just on how it may be scored in public expenditure.

The options that are likely to have most appeal are those with the least net cash flow from public sector bodies in the next few years.

It would therefore achieve little if grants were replaced, pound for pound, by loans from the public sector. Loans and grants have a similar impact on the net cash flow of the public sector in the short to medium term. The only financial advantage would come from the likely reduced take-up of loans, as compared with grants, and this would mean less improvement work.

The emphasis needs to be on maximising the extent to which the money required for repairs and home improvements is provided by loans from the private sector. This can be done by:

- facilitating and encouraging the use of private sector loans, possibly through some collaboration between the Housing Executive and private lenders aimed at countering the reluctance of borrowers to use commercial lenders;

- using modest amounts of public expenditure to 'lever in' private sector loans by, for example, indemnifying some interest-only loans and contributing to fees for setting up rolled-up interest loans for older homeowners;

- funding equity sharing loans where this is the only loan option, acknowledging that take-up will be less than grants; and

- offering small unsecured loans for minor works on which the set-up costs of a secured loan would be grossly disproportionate.

Findings and Conclusion

The existing policies to support repairs and home improvements in the private sector have been very successful - fewer than 1% of home owners in Northern Ireland live in housing that is unfit. But the funds for sustaining the existing policies have recently declined and it must be expected that financial constraints will become more stringent. It is therefore timely to examine ways in which the momentum of repair and home improvement in Northern Ireland might be maintained in the new circumstances.

The key requirement in the new circumstances is to minimise the impact on the UK deficit. This means looking for solutions that minimise the cash flow out of the public sector in the short to medium term, while maintaining as much repair and improvement in private sector housing as possible.

The best chance of achieving this outcome is to maximise the use of private sector loans for home improvements by owner occupiers. There is scope for greater encouragement of homeowners to use loans, rather than relying on grants. This message might be better received if some contribution to the cost of setting up a loan was to be offered to those who in the past would have been eligible for a grant. As well as providing loans at market rates, there is also potential scope for commercial lenders to offer subsidised loans to targeted homeowners if either the capital is provided from public funds or if public funds are available to bridge the gap between the commercial return required and the return that could reasonably be expected.

But a move from grants to loans must be expected to encounter resistance from borrowers (and probably more widely). Experience elsewhere indicates that many people prefer to defer action, hoping that generous grants will return, rather than borrow to carry out works that seem to them less pressing than they seem to housing professionals. It will be important to consider how to respond to such views. Even among those willing to contemplate borrowing, there is much reluctance to do so; among older people there is often a lack of confidence in the loan products and/or the providers.

Northern Ireland may be better placed to tackle these issues than other parts of the UK. The Housing Executive is a prominent single body whose association with a new policy may give confidence to homeowners. The Housing Executive would need to handle with care any links with commercial lenders. But, if it found a way of doing so appropriately, such a link might be expected to encourage homeowners to give consideration to a new policy. Greater reliance on commercial lenders could increase the pressures on the two Home Improvement Agencies in Northern Ireland, as such lenders would expect, and may require, works to be overseen by a competent body.

"The key requirement in the new circumstances is to minimise the impact on the UK deficit.... minimise the cash flow out of the public sector in the short to medium term, while maintaining as much repair and improvement in private sector housing as possible."

Rachel Terry Independent Consultant

Rachel Terry specialises in housing finance policy issues and project finance.

Having worked in corporate banking and in local government, she has been advising on the raising of private finance for partnership projects and affordable housing for over 20 years.

In 2008, she worked with Richard Gibson (Independent Consultant) on two research projects for the Greater London Authority. The first was identifying barriers to changing from grants to loans for private sector renewal in London. This was followed by a feasibility study into a self-sustaining loan fund for private sector renewal in London.

Rachel is currently working with Richard Gibson on an assessment of equity release pilots in three local authority areas. A Home Cash Plan has been specially designed for homeowners on Pension Credit and the local authorities involved are using well-being powers to give out information about the product. Two commercial organisations are providing the financial advice and the product in the three areas, without any subsidy. The Joseph Rowntree Foundation (JRF) is funding the assessment.

Rachel is also project managing an action-based research project within JRF's young people and housing programme. The aim of this project is to learn more about housing advice and housing choices available for young people. This involves a survey of 16 – 25 year olds and pulling together an Illustrative Practice Briefing of initiatives that have been introduced to improve housing and housing advice for young people.

"Rachel Terry has examined the potential inherent in moving towards a loans-based system of providing assistance to homeowners..."

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