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Stage 2 of Finance Research
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Intermediate Housing Options, particularly the First Time Buyers Initiative

DTZ Pieda is undertaking a piece of work for the Westminster Housing Commission which analyses intermediate housing provision and the future requirements in Westminster. The research indicates that there are a sizeable population of households in Westminster in the income bracket of £35,000 - £50,000 who can afford more than social rents but cannot afford to buy in Westminster. Often these households do not qualify for some of the existing intermediate market products, or find that they do not meet their needs, for example in terms of flexibility.

In addition, DTZ Pieda is researching innovative funding mechanisms for affordable housing in Westminster.

This paper is intended to inform discussion on potential ways that Westminster City Council or The Dolphin Square Foundation ("the Foundation") could be involved in offering intermediate housing products.

Background

Current products making up low cost home ownership are vast and somewhat complicated, including:

- Homebuy
- Shared Ownership
- Key Worker Living Homebuy
- Key Worker Living Shared Ownership; and
- Cash incentive scheme

Other initiatives which will soon be launched will include the revamped Homebuy (which will have three subsets - Social Homebuy, New Build Homebuy and Open Market Homebuy) and the First Time Buyers Initiative (FTBI) to be offered via English Partnerships.

First Time Buyers Initiative

The exact structure of FTBI has not been finalised but it will be offering a shared equity product, with the minimum buyer equity share of 50%. The buyers will be able to acquire more equity from EP in minimum of 10% tranches.

The buyer pays a charge on the un-purchased equity only after the first 3 years, then stepped from 1% pa in year 4 to 3% pa in year 7. The buyer will be able to staircase up to 100% ownership of the property.

Half of the new homes built under this initiative will be targeted at key public service workers, with Regional Housing Boards determining the eligibility criteria for the remainder and the scheme will be administered via the existing Zone Agents programme.

The procurement of the new units will come from EP's current programme, surplus public sector land, and with private sector schemes.

A role for WCC / The Foundation

There is potential for a scheme along similar lines to be developed in Westminster.

It is assumed that provision arising as a result of direct intervention of WCC/the Foundation should be ring-fenced from the normal delivery mechanisms for affordable housing within the borough. No genuine additionality would result from a scheme which simply replaced the affordable housing provision already delivered through planning gain, or by the direct development or procurement by the RSLs operating within the borough.

The advantage of a bespoke scheme for WCC/the Foundation is that it could be tailored to a wider audience and take account of the high value housing market in the borough.

To establish an appropriate mechanism, the following issues would need to be addressed:

- Should properties be affordable in perpetuity? Effectively grant funded, shared ownership schemes enable full staircasing so the unit thereafter could trade on the open market.
- Would WCC/The Foundation wish to have a continuing stake in the properties?
- Should the properties meet traditional criteria for "affordability"?
- Which market segment the scheme would be aimed at – How to balance the trade-off between the maximum number of units effectively subsidised and the mix – family accommodation would require more subsidy but would provide stock which would be otherwise difficult to access.
- Whether stock will need to come from the open market or whether the council can identify surplus sites or redundant buildings.

One option to consider would be to identify new or nearly constructed schemes within Westminster. In these cases, the planning process would have already invoked a percentage of affordable housing on the site, or if it had been proven that this would not be feasible, the borough would have taken or accepted an off site provision contribution from the developer.

Developers are often prepared to sell multiple units at a discount of between 10-15%, dependent on market conditions. However, the market in Westminster remains strong and the supply of new units relatively small so in order to achieve scale, WCC/the Foundation might have to consider investing in second hand properties.

Illustrative Mechanism

One possible structure is outlined below. The features of this are:

- 20% of the property is effectively retained by WCC/The Foundation.
- Individual purchasers buy a percentage of the property – say 50% - funded by a traditional shared ownership mortgage lender such as Nationwide on the basis of a bespoke mortgage product. It is likely that this could be structured so that a deposit is not required.
- The balance (in this example 30%) is effectively funded by a wholesale lender either by mezzanine bank debt or, dependent on the size of the portfolio, by a bond issue. The impact of this intermediate level is that it leverages the WCC / Foundation contribution, enabling it to be spread over a broader portfolio of properties, including a range of property types and sizes.
- A charge would be made on mezzanine debt of, say, 6% p/a.
- A variety of staircasing options could be offered, from mandatory fixed price RPI linked steps to say 10% steps at market value. The advantage of fixed RPI linked steps is that, because of the certainty of the cashflow and because of the appetite for RPI linked assets, the financing rate would be keener. There will need to be some form of incentive to staircase in order to create a reasonably robust cashflow for the mezzanine lender.
- As well as retaining a 20% share, WCC / the Foundation could provide flexibility for the household by subsidising financing charges or staircasing.
- The individual owner could never staircase to more than 80% of the property. The lease could provide restrictions as to whom the 80% interest could be sold. Alternatively, WCC/The Foundation could have pre-emption rights to buy in the property.
- Care would need to be taken with regard to tax liabilities and the charitable status and objectives of The Foundation.
- WCC/The Foundation would need to decide whether it would require to see a running return on its equity investment. The value of the investment would in any case benefit from house price inflation but any gain would be difficult to realise.

The advantage of the 20% held by WCC/The Foundation is that it brings more properties into reach for those in the £35,000 to £50,000 target market, There is evidence that a significant number of new private sector properties are not lived in or are let to private renters with little long term stake in the community. Such a mechanism would ensure that the properties are not left empty and are lived in by households with a medium to long term interest in the property.

Depending on a final structure, the saving on a £300,000 property would probably be in the region of £4,000 per annum to the individual purchaser.

Below is a structure chart showing the various property interests under this illustrative mechanism. If WCC/The Foundation were able to give further guidance on the issues raised in this note, some detailed modelling and examples could be prepared.