Summary

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Improving coordination between housing allowance, housing grant and start-up loan schemes
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As the Government made clear in its housing policy white paper (St.meld. nr. 23 "Om boligpolitikken"), facilitating wider home ownership among disadvantaged groups in society is a key policy target. The start-up loan and housing grant schemes are intended to cover part of the cost of buying. The housing allowance complements these policy instruments by enabling households to pay their annual housing expenses and continue to reside in the dwelling.

The Housing Bank commissioned NIBR to review interrelations between the major housing policy schemes. The purpose of the review is to inform action to improve scheme coordination, and encourage local local authorities struggling to help disadvantaged groups in the housing market to make greater use of the schemes to promote home ownership.

The review focuses on the opportunities existing housing policy schemes give to promote home ownership and help disadvantaged people into the ownership market. One of the main purposes of the review was to explore possible incongruities affecting policy mechanisms for different groups in different housing markets. It is necessary to identify which factors are involved when households that are eligible for housing allowance default on their start-up loan payments, also when they are receiving a generous housing allowance. What sort of changes should be made to criteria and rules that would make for improved coordination between the

various schemes? Are the annual adjustments in schemes for providing home ownership sufficient, and what is the scale of the need for the scheme? To what extent does the management of local local authorities' social housing schemes and lack of competence in the relevant fields frustrate closer integration of the available instruments?

To establish signs of scheme disharmony and the impact of amending the rules, we constructed a model with a financing module, a housing allowance calculation module and a module that calculates what's left after taxes, net housing expenses and a minimum amount for subsistence expenses. The calculation is done for different household types in different housing markets. As a rule, the relationship is denoted by the term economic margin. A figure shows how the economic margin varies with income. As eligibility for a start-up loan is indicated by a positive economic margin, we should be able to work out the necessary income level to service a start-up loan in the presence of a housing allowance and housing grant.

To quantify the actual need for start-up subsidies, we analysed data from the 2004 Survey of Living Conditions and investigated how many young people wanted to buy a home but were unable to get a mortgage. We also look at schemes promoting home ownership in the UK and discuss alternatives to the housing grant scheme.

We sought to establish how far management by and competence of local authorities affects scheme implementation by interviewing officials at the Housing Bank's regional offices, in charge of liaising with the authorities locally on matters pertaining to the start-up loan.

How the model performs depends on the assumptions relating to housing standard with corresponding price level, own equity, other loans, interest rate used to factor in future rate changes and subsistence expenses level employed. None of the households in the examples have equity of their own, nor other loans than the start-up loan. We apply a discount rate of 6.5 per cent, as per the recommendations of the Housing Bank. The loan term is set at 20 years as an annuity loan. We use the National Institute for Consumer Research's (SIFO) minimum subsistence scale. This does not include renewal of household equity objects and caution is advised for long-term low-income households, one of the

housing grant's eligibility criteria. With regard to single parents, we made certain assumptions as to the child maintenance sum paid by the non-resident parent. We ran separate estimates for all families with children for those with kindergarten children and those with school children. We took Oslo city's kindergarten fees as our baseline.

We find only a minor level of scheme coordination, a conclusion which remains valid even when house prices are significantly overestimated. It echoes however ECON findings (2005), Østerby (2007) and impressions provided by officials at the Housing Bank's regional offices.

The disparity between the highest income that qualifies for a housing allowance and the income required to service a start-up loan is particularly evident for couples without children and families with two adults. It remains valid also when 40 per cent of the purchase price is awarded as a housing grant. But there is little opportunity for inter-scheme coordination under the current rules for single parents. We only find scheme synchronisation in a narrow income range for young, single individuals and disabled young adults. Young, single individuals falls within the housing allowance's target group only if the income comprises social security benefits or public assistance.

Extending maturity to 30 years reduces monthly instalments considerably while leaving room at the same time for an instalment-free period should the household situation becomes critical. Extending the maturity date has a small positive impact on the synchronisation effect for single individuals and single parents with one child, but the effect is larger for the young disabled.

It is not until extended maturity is combined with changes in the housing allowance scheme that we see substantial coordination benefits. There are several ways to increase the highest income for eligibility for the housing allowance. The current rules calculate the housing allowance as 70 per cent of the difference between what is called "reasonable housing expenses" and "approved housing expenses". The reasonable housing expenses are that fraction of the income which the households themselves should be able to pay for housing; the fraction varies with income level and number of people in the household. The approved housing expenses are supposed to represent the housing expenses of the household and

are based partly on actual expenses and partly on templates for various housing expense components. The housing expense ceiling specifies the ceiling of approved housing expenses. These ceilings vary by number of persons in the household and geographical location of the dwelling.

Higher housing expense ceilings and changes in the formula for calculating reasonable housing expenses, and both in combination, occupy a central position when the rules governing the housing allowance scheme in the model are changed. Examples are given of changes in the housing allowance rules resulting in higher inter-scheme coordination.

In addition to improving coordination between schemes in a start-up phase, changing the housing allowance parameters also increases the housing allowance of current recipients in dwellings they rent or own, and make it easier for other owners and renters to access the housing allowance scheme. We have not tried to estimate the budgetary impact of the changes in the housing allowance rules.

It is difficult, or impossible, to estimate the scale of the need for start-up subsidies. There are some short-term and some long-term needs created by the annual replenishment of the group of disadvantaged persons on the housing market. Recruitment to the group will depend further on changing demographics, habitation patterns and economy. It is a moot point, moreover, whether local authority housing for rent or the rental market more generally should be part of the solution for disadvantaged groups.

Almost four out of ten start-up loan applications are denied. The high rejection rate is caused mainly by an inability to service a loan. Many of the respondents at the regional offices of the Housing Bank think local authorities are too apprehensive about taking risks, and encourage them to relax their rather mechanical application of SIFO's normal subsistence tariff, which indeed the Housing Bank recommends in its guidelines.

Funds for the housing allowance scheme were too low, according to our informants. Small municipalities find it difficult to comply with the Housing Bank's request to provide large housing grants to few applicants. In the opinion of some, the housing allowance has helped promoting home ownership among young disadvantaged

adults. Many local authorities, according to two of the informants, failed to take into account whether start-up loan applicants were eligible for housing allowance prior to their consideration of the start- up loan applications.

The view was relatively widespread that small municipalities have disconnected and uncoordinated social housing schemes, and inadequate inter-agency liaising. Agencies are seldom housed in the same building. Small municipalities also lack expertise for properly assessing start-up loan applicants.

What can be done to improve coordination between the start-up loan, housing grant and housing allowance schemes to promote home ownership among low income groups? As far as loans and credit ratings are concerned, a 30-year term could be justified. It would reduce the savings component of payment of housing expenses while leaving room to temporarily halt payments should the household go through a particularly difficult period. Many recipients of the start-up loan will see their earnings grow with time, making it less onerous to repay the loan. When assessing the credit rating of loan applicants, the minimum subsistence rate then should be applied. The subsistence tariff does not include the savings component allocated for renewal of household appliances. Today, a calculation interest rate of 6.5 per cent below the credit estimate is in force. This should not be lowered.

As specified by the guidelines, only permanently low-income households are eligible for the housing grant. In these cases, local authorities should take care to avoid applying subsistence rates under a certain level, as the household will likely suffer poor economic health for some considerable time. Local authorities in these cases should consider whether SIFO's minimum standards are too low, and carry out a thorough assessment of credit worthiness. What the household over time has paid in the rental market can be a guideline.

Single parents whose children have a kindergarten place are more likely to obtain a start-up loan, according to our calculation formula. Vigilance will be required when the child leaves the kindergarten to start school, insofar as a major income component such as child care benefit may be discontinued.

A better procedural system could help local authorities understand the possibility of running the schemes in concert and also indicate when a start-up loan can be given without having to provide a housing grant. It would allow local authorities to target this scarce resource to the people who need it – and the system could work out the appropriate housing grant percentage of the house price.

When assessing housing grant eligibility, one should remember that the grant in certain circumstances will have a significant impact on the economic margin due to the tax system's design. In other situations, the effect of the housing grant may cause approved housing expenses in the housing allowance scheme to fall below the housing expense ceiling, which would depress the housing allowance to the household.

The Housing Bank wants local authorities to make more use of the start-up loan scheme than is currently the case. Since local authorities record small losses on the scheme, they should arguably accept a wider risk and offer the loan to more applicants.

The wish to extend the start-up loan scheme needs elaboration. First, losses sustained by local authorities will also mean that the borrower will lose out if the dwelling is sold under foreclosure. In this situation, re-establishing oneself as a home owner at later point in time may prove difficult. It would be very unfortunate indeed if wider use of the start-up loan scheme resulted in losses for the authorities and more foreclosures.

Some local authorities refuse loans to households with the capacity to service a start-up loan. Perhaps the local authoritie's eligibility criteria are too narrow, or they fail to make a more individual assessment of the applicant's credit worthiness. But changing practice here too could lead to more foreclosures and leave a larger number of indebted households in its wake. Local authorities will have to weigh the benefit of helping a larger number of people against the risk of undesired consequences and higher foreclosure rates. At the same time, it concerns the sort of help local authorities can offer people whose circumstances have take a turn for the worse.

Further to the project we look at fresh issues worthy of consideration.

How appropriate is the housing allowance scheme in a start-up phase?

If the housing allowance scheme is to have an effect for more people setting up a house, a thorough overhaul of the regulations will be needed. The question is whether the housing allowance scheme should target first-home owners alone or help others on the first rungs of the housing market. This brings us to the next issue.

Should the housing allowance scheme or housing grant scheme compensate regional housing market disparities?

Today, one is encouraged to provide substantial housing grants in high-demand areas, at the same time as differentiated housing expense ceilings are supposed to extend the housing allowance scheme to slightly higher earning households in the same neighbourhoods. If the purpose is to target subsidies at home ownership, additional spending should be settled on the housing grant budget.

The role of the housing grant scheme in housing policy

Consideration should be given whether to change the housing grant to a fixed period interest and instalment free loan, 10 years for instance, after which the household's eligibility for a further period of interest and instalment freedom could be re-assessed. Alternatively the housing grant can be given as a loan with means-tested interest subsidies. This would widen the scope of the scheme and improve its legitimacy, but without changing loan service capacity or economic margin as estimated above for the first year. Lessons of schemes like the UK and Irish HomeBuy and Shared Ownership, which facilitate wider home ownership, should be considered in this connection. "Shared ownership" is a possible alternative to promote home ownership without changing the housing allowances scheme.