

Impact Assessment of Homeowners Mortgage Support



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Communities and Local Government
Eland House
Bressenden Place
London
SW1E 5DU
Telephone: 020 7944 4400
Website: www.communities.gov.uk

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Tel: 0300 123 1124

Fax: 0300 123 1125

Email: communities@capita.co.uk

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Summary: Intervention & Options

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<http://www.communities.gov.uk/publications/housing/homeownerssupportpackage>

Contact for enquiries: Suzanne Kochanowski **Telephone:** 020-7944-2176

What is the problem under consideration? Why is government intervention necessary?

Repossession numbers are rising as people struggle to meet their mortgage payments in the economic downturn. Repossessing homes imposes significant costs to society, including stress to the families involved, impacts on the wider economy through a fall in consumer confidence, costs to the Government in the form of housing benefit payments for many repossessed households, as well as losses incurred by lenders. There is an efficiency and equity case for Government intervention to reduce repossessions.

What are the policy objectives and the intended effects?

The Government's focus is on preventing repossessions and it has introduced a package of new measures designed to achieve this. The policy objective of Homeowners Mortgage Support (HMS) is to protect a significant number of households, who would not be eligible for Government assistance through the Mortgage Rescue Scheme or Support for Mortgage Interest (SMI). HMS is intended to promote best practice in lender forbearance to ensure that households are protected from the threat of repossession and the adverse social impacts that can follow.

What policy options have been considered? Please justify any preferred option.

- a) Do nothing
- b) Introduce Homeowners Mortgage Support to help ensure households which suffer a temporary income shock are able to reduce their monthly mortgage payments to a sustainable rate. This will allow many households to remain in their home and provides them with a time window to get back on their feet, with the intention that they will eventually resume full mortgage payments.

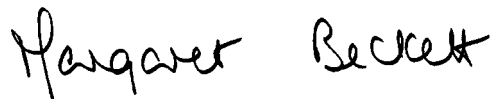
When will the policy be reviewed to establish the actual costs and benefits and the achievement of the desired effects?

HMS will be monitored through monthly reports from its delivery partner. Evaluation will be carried out during the period that the scheme is open to new entrants, in order to review HMS's operation and assess it against intended outcomes.

Ministerial Sign-off For Impact Assessments:

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible Minister:

Handwritten signature of Margaret Beckett in black ink.

Date: 20 April 2009

Summary: Analysis & Evidence

Policy Option: **b)**

Description: **Introduction of Homeowners Mortgage Support**

ANNUAL COSTS		Description and scale of key monetised costs by 'main affected groups'
One-off (Transition)	Yrs	
£2.5m	0	<p>The main estimated present value cost of £34m, if deferred guaranteed interest payments are not paid back, will fall to Government.</p> <p>In addition, there will be administrative costs for both the Government (estimated £2m set-up and £6.5m PV total ongoing costs over 8 years) and lenders (£0.5m total set-up and £1m PV total ongoing costs).</p>
Average Annual Cost (excluding one-off)		
£6.2m	8	Total Cost (PV) £44m
<p>Other key non-monetised costs by 'main affected groups'</p> <p>Lenders will experience a number of other commercial costs as a result of offering HMS. In addition, both lenders and borrowers face the risk of losses in cases where the support only grants a temporary reprieve from repossession and the value gained from the property is lower than at the current time.</p>		
ANNUAL BENEFITS		Description and scale of key monetised benefits by 'main affected groups'
One-off	Yrs	
£0	0	<p>We estimate that the savings to the exchequer from a reduced number of repossessions will total PV £58m over 4 years.</p>
Average Annual Benefit (excluding one-off)		
£15m	4	Total Benefit (PV) £58m
<p>Other key non-monetised benefits by 'main affected groups'</p> <p>There are significant non-monetised benefits as a result of the support offered through HMS and extended lender forbearance. These include avoiding the stress for households of repossession, avoiding negative adverse social impacts (for example, increased debt and disruption to education), boosting consumer confidence in the housing market, avoiding clusters of repossessions and the negative impacts on communities, and raising the profile of the financial support available to households.</p>		

Key Assumptions/Sensitivities/Risks

The results are based on a conservative estimate of lender participation in HMS. A further key factor is the number of borrowers who lenders choose to offer the terms of the scheme to. This will depend on commercial expectations of many uncertain economic variables, including house prices.

Price Base Year 2009	Time Period Years 8	Net Benefit Range (NPV) £6m-34m	NET BENEFIT (NPV Best estimate) £14m
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What is the geographic coverage of the policy/option?	United Kingdom			
On what date will the policy be implemented?	21 April 2009			
Which organisation(s) will enforce the policy?	N/A			
What is the total annual cost of enforcement for these organisations?	£N/A			
Does enforcement comply with Hampton principles?	Yes			
Will implementation go beyond minimum EU requirements?	N/A			
What is the value of the proposed offsetting measure per year?	£N/A			
What is the value of changes in greenhouse gas emissions?	£N/A			
Will the proposal have a significant impact on competition?	No			
Annual cost (£-£) per organisation (excluding one-off)	Micro N/A	Small N/A	Medium N/A	Large N/A
Are any of these organisations exempt?	No	No	No	No

Impact on Admin Burdens Baseline (2005 Prices) (Increase – Decrease)

Increase of £ **0.05m** Decrease of £ **0m** **Net Impact £ 0.05m¹**

Key:	Annual costs and benefits: Constant Prices	(Net) Present Value
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¹ Based on the proportion of lenders likely to represent 50% of eligible households in 3+ month mortgage arrears

Evidence Base (for summary sheets)

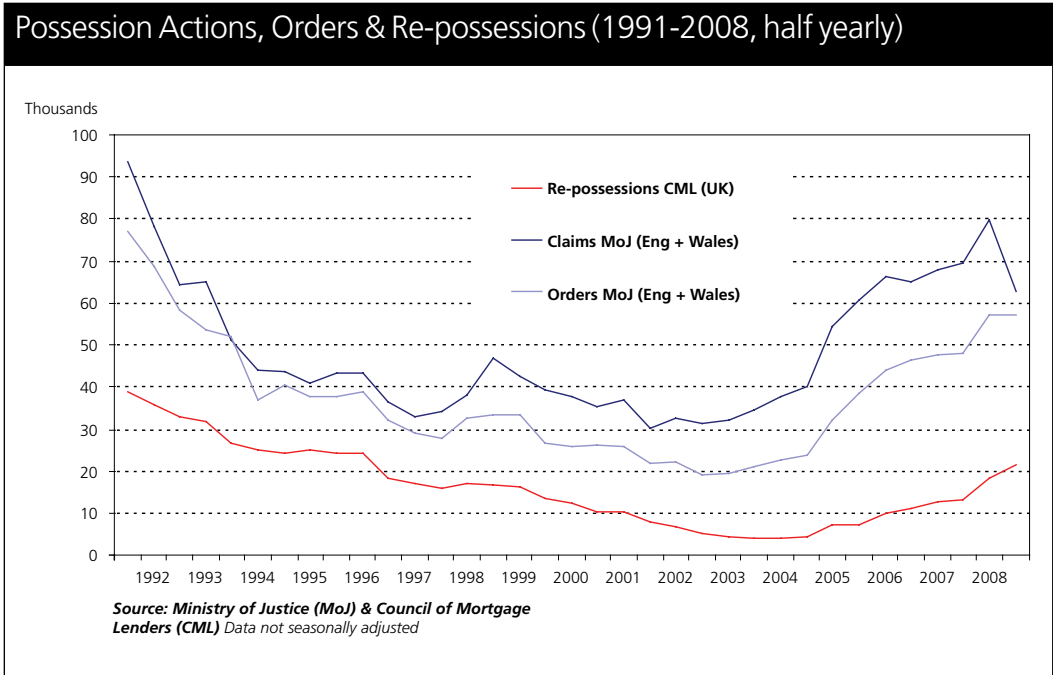
1. Given the urgent need to protect households facing repossession, this Impact Assessment is a final assessment to allow implementation of Homeowners Mortgage Support (HMS) as soon as possible. As the support is dependent upon lender decisions on how many borrowers they will offer the terms of HMS to, it is difficult to estimate with certainty in advance of the scheme opening, the borrower take-up and therefore the costs and benefits. This Impact Assessment makes a conservative estimate at this stage of lenders offering HMS and taking up the option of the Government financial guarantee in order to derive the costs and benefits of HMS.
2. The Impact Assessment does not quantify the benefits from lenders who offer comparable arrangements to HMS and grant extended lender forbearance without taking up the guarantee. The Impact Assessment has been prepared alongside discussion with lenders and other stakeholders on the design and operation of the scheme.

Background

3. Some repossessions are a normal part of the housing market functioning and not all repossessions can or should be avoided. In 1998-99 levels were around 30,000 per year and in the period 1998 to 2007 repossessions averaged almost 20,000 per year. However mortgage repossessions have increased significantly in recent years: 26,200 in 2007 and 40,000 in 2008². The Council of Mortgage Lenders (CML) is forecasting 75,000 repossessions in 2009³, although they have made clear that this estimate is highly uncertain.

² CML data

³ CML data



- The majority of repossessions occur due to a major change in household economic circumstances. The reasons for entering mortgage arrears can include being made redundant, losing pay because of sickness or injury, and reduced income for those who are self-employed, as shown in the table below:

Reason for mortgage arrears, England, 2005/06 and 2006/07 (% of respondents)^{1,2}

A spouse or partner or other contributor left home or died	27%
Someone who had been contributing became pregnant/new baby born	6%
Someone who had been earning, lost pay because they were sick or injured	18%
Unemployment/reduced hours of work/reduced pay/business failure	54%
There was an increase in the mortgage payments	10%
There was an increase in other payments	14%
Other	29%

¹ percentages do not add to 100 as respondents could give more than one reason
² average for 2 year period 05-06 and 06-07 is used due to small sample sizes
 Source: Survey of English Housing, CLG

- Unemployment is currently rising and so we can expect the current economic downturn to be a significant driver of increased rates of repossessions. This is likely to be compounded by the higher numbers of homeowners since 1997 and the recent years of relatively easily available credit and low mortgage rates which may have led to some households borrowing more than they could sustain over the long term.

6. Even with the recent cuts in Bank of England base rates, some borrowers will find it increasingly difficult to pay their mortgages. Significant numbers of borrowers with mortgages outstanding, particularly from non-mainstream lenders, still face high interest rates as some lenders choose to increase margins rather than pass on interest rate cuts.
7. The Government has already done much to deal with the increase in repossessions. In 2008, the Government announced £10m for debt advice services, including funding for a further 74 Court Desks which offer legal advice to households going through repossession proceedings in county courts in England. An additional £15.85m has been announced to extend free telephone and face-to-face debt advice to all consumers across the country. In September 2008, the Government announced the Mortgage Rescue Scheme targeted at the most vulnerable households at risk of homelessness, along with changes to the Support for Mortgage Interest (SMI) scheme to increase support for homeowners with mortgage interest payments⁴. The Government announced further action in December 2008 to protect those households from the threat of repossession who would not be eligible for Government assistance through the Mortgage Rescue Scheme and further expanded SMI scheme⁵.

Policy objectives

8. The policy objective of Homeowners Mortgage Support (HMS) is to protect a significant number of households who would not be eligible for Government assistance through the Mortgage Rescue Scheme or Support for Mortgage Interest (SMI). HMS is intended to promote best practice in lender forbearance to ensure that households are protected from the threat of repossession and the adverse social impacts that can follow.

Policy options

1) Do nothing

9. Without assistance through HMS and the other initiatives cited, CML estimates that 75,000 households could be repossessed in 2009. This would lead to significant stress for the families involved as well as the possibility of negative social outcomes, such as increased debt, worklessness, poor health and disruption to education.
10. A proportion of repossessed households will eventually end up in the social or private rented sectors, increasing the overall costs to the Government through housing benefit payments.

⁴ September 2008 policy statement is available here: <http://www.communities.gov.uk/news/housing/950571>
Impact assessments available here: <http://www.communities.gov.uk/publications/housing/homeownerssupportpackage>

⁵ See: <http://www.publications.parliament.uk/pa/cm200809/cmhansrd/cm081203/debtext/81203-0006.htm>

2) Introduce Homeowners Mortgage Support

11. HMS aims to provide greater assurance to homeowners that they will be able to remain in their homes if they suffer a temporary income shock (for example, redundancy or loss of income for one partner of the family). It does this by enabling eligible borrowers to agree with their lender to defer payment of a proportion of the interest payments on their mortgages for a period of up to two years. Upon exiting the scheme, if a borrower defaults within a four year period, their lender is able to claim back from Government 80 per cent of the deferred interest payments.
12. The guiding principle is that lenders, borrowers and the Government appropriately share the risks:
 - borrowers will be required to consider responsibly their future financial circumstances, and to make a non-deferred monthly contribution (depending on their circumstances) of at least 30 per cent of the total monthly interest payment. Borrowers will be made aware of the risks they face in terms of reduced equity in their homes if they are unable to resume full interest payments after leaving HMS
 - lenders offering HMS will assess the eligibility of borrowers and the appropriateness of the support to household circumstances relative to other forbearance options. For those borrowers who enter the scheme and subsequently default during the four year guarantee period, lenders will be able to claim the costs of up to 80 per cent of the total monthly interest deferred from the Government. They will bear the risk on the remaining 20 per cent of the total monthly interest deferred and 100 per cent of the risk on the interest deferred in the event of default after expiry of the guarantee period
 - the Government guarantee will not exceed 80 per cent of the total monthly interest deferred if an enrolled borrower defaults on their mortgage during the four year guarantee period
13. Some lenders have decided to offer comparable arrangements to HMS and grant extended forbearance to their borrowers. They have however, for commercial reasons, decided not to take up the option of the Government financial guarantee should the borrower subsequently default on their mortgage payments. These lenders will therefore bear the risk on 100 per cent of the deferred monthly interest.
14. A full description of the scheme and eligibility criteria is attached as an Annex.

Costs of Homeowners Mortgage Support

Summary

The main cost falls to the Government by guaranteeing 80 per cent of the interest deferred by borrowers who subsequently default within the guarantee period. We estimate that the present value cost of this, if realised, will be £34m (2009 prices) over 8 years.

In addition, there will be administrative costs for both the Government and lenders. We estimate that the one-off set up costs for Government will be £2m with ongoing costs totalling £6.5m (present value) over 8 years. We estimate that the set up and ongoing costs for lenders will be £0.5m and £1m (present value) over 8 years respectively.

There are a number of potential commercial costs to lenders which we have not quantified given commercial sensitivities. Both lenders and borrowers face the risk of losses in cases where HMS only grants a temporary reprieve from repossession and the value gained from the property is lower than at the current time. HMS has been designed to reduce this risk but both lenders and borrowers will be made aware of the potential risks involved in taking up this voluntary support.

1) Do nothing (baseline)

15. Lenders already exercise forbearance since it is often in their interests to do so because of the high costs they are likely to face when repossessing. The size of the loss varies according to property value and house price inflation.
16. Repossessions are costly for households, the exchequer and lenders. The costs for the exchequer include housing benefit expenditure for those households that need support in the private or social rented sectors following repossession.
17. HMS will result in a decrease in the number of repossessions relative to what would have happened in the absence of the scheme (the baseline) and so the benefits of HMS are the reduction in the above mentioned costs to households, the exchequer and lenders. **Consequently the analysis takes the baseline as zero and assesses the costs and benefits of HMS relative to this.**

2) Introduce Homeowners Mortgage Support

Monetised costs for Government

Overall costs of Homeowners Mortgage Support

18. The main cost falls to the Government as a result of guaranteeing up to 80 per cent of the interest deferred by borrowers who subsequently default within the guarantee period. We estimate that the present value cost of this, if realised, will be £34m (2009 prices) over 8 years⁶. The results are based on our analysis, assumptions (set out in more detail below) and take into account the views of lenders.

19. The costs are based on a central estimate that around 42,000 households could join HMS over the two years of its duration with their lender taking up the option of the Government financial guarantee if they default during the guarantee period. This is based on a conservative estimate at this stage which assumes that such lenders account for 50 per cent of the number of eligible households in 3+ month mortgage arrears. If a higher number of lenders offer HMS and take up the option of the Government guarantee, then it can be expected that a higher number of households will join the scheme with consequently higher expected costs.

20. Since expected costs are sensitive to realised take-up, the table below shows the expected cost in present value terms based on different numbers of households joining HMS:

Possible HMS take-up over 2 years	Expected monetised cost (present value)
85,000*	£83m
42,000**	£45m
31,000	£37m

* Estimate if 100% of the mortgage market is covered

** Central estimate if 50% of market is covered

21. As can be seen above, if lenders representing 100 per cent of the number of eligible households in 3+ month mortgage arrears offer the terms of HMS, then we estimate that up to 85,000 households could be helped by the support.

⁶ A discount rate of 3.5% has been applied throughout this Impact Assessment.

22. Lenders who offer comparable arrangements to HMS and grant extended lender forbearance without taking up the option of the Government guarantee will not bring additional costs. We have not attempted to quantify the impact of this extra lender forbearance, but clearly this behaviour – which has no cost to Government and is likely to prevent additional repossessions – will result in reduced repossessions and in net benefits to the exchequer and to wider society.
23. As HMS is lender-led, all estimates presented are extremely uncertain. Lender decisions will be affected by commercial decision-making and expectations over many uncertain economic variables such as house prices and unemployment. Not all of the eligible households will join HMS as lenders and/or borrowers may decide it is not in their interests to do so.
24. Of those households that join HMS, for many, the two year window of reduced mortgage payments will provide the opportunity they need to overcome their temporary financial difficulties. For example, to find another job and be able to resume full interest payments. These households will be able to stay in their homes on a permanent basis. It is important to note, however, that it cannot be assumed that all of these households would have been repossessed in the absence of HMS, for example, because of the availability of standard lender forbearance.
25. However, some households will find it difficult to be able to meet the full payments on their mortgages after the reduced payment period expires. For these households, some may choose to use the additional time period granted by HMS to sell the property; others may receive further support through Support for Mortgage Interest once they exit HMS which enables them to remain in their home. However, for some households, the scheme will in effect only grant them a temporary reprieve from repossession (albeit one which allows them further time to plan for their future and arrange alternative accommodation).
26. The above cost is based on the estimated number of borrowers that enter HMS and find themselves unable to meet the full payments on their mortgages after the reduced payment period ends but within the four year guarantee period (and where the equity is insufficient to cover the cost including the rolled up interest, and where the lender claims on the Government guarantee). This is multiplied by the average cost per guarantee to produce the total cost of guarantees, which is then added to the start up and ongoing administrative costs to produce the total cost.

Annual costs of Homeowners Mortgage Support

27. The average annual cost (excluding one-off costs) is estimated at £6.2m per year (this includes estimates of the ongoing administrative costs to Government and lenders). However, the realised cost to Government is likely to vary quite substantially year to year over the 8 year period of the scheme duration and guarantee period. As the majority of borrowers who are unable to meet the full mortgage payments will do so after the two year period of reduced payments ends, we estimate that the peak realised costs will be realised in 2013-14 (£10.4m) and 2014-15 (£10.3m) (not discounted). This is shown in the table below:

Profile of costs to Government (not discounted)

Financial Year	2008/ 2009 and 2009/ 2010	2010/ 2011	2011/ 2012	2012/ 2013	2013/ 2014	2014/ 2015	2015/ 2016	2016/ 2017
Gov guarantee cost profile	£0.08m	£0.9m	£2.5m	£6.6m	£9.6m	£9.5m	£8.5m	£3.3m
Total admin ongoing cost excluding VAT	£1.7m	£1.4m	£0.6m	£0.7m	£0.8m	£0.8m	£0.7m	£0.6m
Total Gov set-up cost	£2m	£0	£0	£0	£0	£0	£0	£0
Total cost	£3.8m	£2.3m	£3.1m	£7.3m	£10.4m	£10.3m	£9.2m	£3.9m

28. The total nominal cost to Government of HMS over the nine years 2008-09 to 2016-17, including set-up costs, are estimated to be just over £50m based on our central case of take-up by 42,000 households. This equates to around £44m in 2009 prices (present value).
29. The two main drivers of the monetised cost estimates are:
- i) The estimated **number of households expected to join HMS**, which will drive the number of guarantee claims. The analysis starts with assumptions regarding the number of households in 3+ month mortgage arrears in 2009 and 2010. These are driven by assumptions on several economic variables, including unemployment and house prices, and the arrears figures are consistent with CML forecasts. The number of households is then reduced to take account of those borrowers who are not eligible for HMS, including those with buy to let mortgages and households eligible for Support for Mortgage Interest. The analysis then takes the estimated eligible number of households and uses a combination of the results of a survey of lenders and a high level attempt to model lenders' behaviour. There are many variables affecting the attractiveness of HMS to lenders including expectations of house prices and unemployment. Our analysis suggests that borrower/lender take-up (and hence expected Government costs) are particularly sensitive to changes in house price expectations – for example, expectations of large house price falls reduce the incentive for a lender to enter households onto HMS.
 - ii) The **average cost to Government per repossessions** under the guarantee. A major factor in determining this is the assumed average mortgage rate over the period of the scheme.
30. For the central case, the following assumptions were used to derive the average cost to Government per repossession under the guarantee:
- the analysis uses an average outstanding mortgage of just under £130,000 based on a current average house price of £170,000⁷ and assumes average Loan to Value (LTV) of 75 per cent. The median mortgage taken out in 2007 was just under £150,000 and we believe that of those being repossessed around half will have purchased more than three years ago

⁷ Taken from the February 2009 average house price estimates of £190K (CLG) and £154k (Land Registry)

- the analysis assumes an average percentage of the total monthly mortgage interest that households will defer. Given the 30 per cent minimum borrower payment requirement, we assume that on average 50 per cent of the mortgage interest will remain affordable and the other half will be deferred. This is reasonable if we assume that households have moved from a two to a single earner family, or one or both partners have a significantly reduced level of income⁸
- we assume that 10 per cent of defaulting households will be able to pay the full guarantee from equity even after the sale of the property at auction. Repossessed properties sell at auction for significant discount relative to their market value
- we assume an average household duration on HMS of 18 months. This is a modelling assumption and will depend on the realised unemployment situation
- given the scheme design we assume an average mortgage rate of those on HMS over its duration of just over 5 per cent⁹.

Administrative costs

31. There will be one-off set-up costs and ongoing administrative costs for both Government and the lenders participating in HMS. We estimate that the set-up costs for Government will be around £2m, including the cost of establishing an interim IT reporting system to track entrants onto the scheme and the Government liabilities, as well as the establishment of a delivery body to oversee this. For lenders, the main set-up costs will arise from staff training to explain the eligibility and operation of HMS, as well as amending systems to enable lenders to enter borrowers onto the scheme and provide reporting information. We estimate that this will total at least £0.5m. This is an uncertain estimate given that lenders are still working to make the scheme operational.

⁸ Modelling assumption – assuming that if they can pay a large portion (e.g. 80%) of their interest then the lender won't enter them onto HMS

⁹ This assumption is based on consultation with lenders, our modelling of the distribution of standard variable rates, and an assumption that some high rate borrowers will not be entered onto the scheme because of the cap.

32. The on-going costs for Government include maintenance of the IT system and the potential costs of developing a full IT reporting system. We estimate that this will total around £6.5m (present value) over 8 years. These estimates are uncertain at this stage given that decisions on whether to adopt a full IT reporting system have yet to be taken and in the absence of market price information that will be gained from competitive tendering. A value for money assessment will be undertaken as part of the decision on whether to proceed with a full IT reporting system. For lenders, there will be on-going costs arising from the staff time spent advising borrowers, entering them onto HMS and providing reporting information. We estimate that this will be around £1m (present value) over 8 years. However, this should be seen in the context of staff time that would have been spent advising borrowers on other forbearance options in the absence of HMS.

Impact on administrative burdens

33. We are required to identify any impact of new policies on the Department's administrative burden baseline as calculated by PricewaterhouseCoopers in 2005. For these purposes administrative burdens are defined as the ongoing additional costs associated with demonstrating compliance with the policy, such as form filling, reading guidance or facilitating inspections. It does not include one-off start up costs. Where the information would be needed anyway by a business for internal purposes, a "business as usual" element was deducted from the cost of the identified burden. From discussions with lenders, we understand that most of the information that they will be required to produce will be in the form of weekly and monthly reports to the Government and its delivery partner. This is likely to come under the "business as usual" category and therefore the additional administrative burden of providing that information to Government will be minimal. Our estimates of the administrative burden are based on the proportion of lenders likely to represent 50 per cent of eligible households in 3+ month mortgage arrears (to be consistent with our central estimate).

Non-monetised costs

34. There are a number of potential commercial costs to lenders of entering households onto HMS, including:
- if the lender claims on the Government guarantee, they will pay 20 per cent of the interest deferred by borrowers who subsequently default within the guarantee period and 100 per cent of the deferred interest of those households who subsequently default after the end of the guarantee period expires

- the lender may receive lower repossession proceeds from households who default later than they would have done in the absence of HMS should house prices fall further
 - the potential cost for lenders showing extended forbearance in terms of the capital they are required to maintain. This is because interest deferred under the scheme will be capitalised into the loan principal and this could increase loan-to-value ratios. However, re-scheduled loans placed in the scheme by responsible lenders will be treated as prima facie evidence of the loans being performing for regulatory purposes. All things being equal, performing loans in the scheme should be considered less at-risk than loans in arrears and therefore require far less capital to be maintained against them by lenders
35. We have not quantified these costs given commercial sensitivities. However, given that HMS is voluntary for lenders, it is reasonable to assume that the expected benefits will outweigh such costs (as well as the monetised costs) in order for lenders to offer HMS.
36. Borrowers also face the risk of losing equity in their homes, should house prices fall further and they end up being repossessed despite joining the scheme. HMS has been designed to reduce this risk and both lenders and borrowers will be made aware of this potential risk before taking up this voluntary support.
37. There is a cost of providing the independent money advice that is a key requirement of taking up HMS. We have provided £2.5m to advice agencies to support the delivery of HMS. This is in addition to funding that the Government provides to money advice organisations more generally to support households experiencing financial difficulties. As such, we have not calculated the specific costs associated with providing money advice to those households taking up HMS, who are likely to have sought advice anyway in the absence of the scheme.

Benefits

Summary

The main quantifiable benefits of HMS to Government are from avoiding housing benefit costs incurred by those households who would have been repossessed in the absence of the support and those households granted a temporary reprieve from repossessions. We estimate that these could total around £58m (present value) over the four year guarantee period.

There are a number of other unquantified benefits from HMS and extended lender forbearance, including the benefit to lenders, communities, wider society and the economy of avoiding repossession.

Monetised benefits for Government

38. Monetised benefits of HMS accrue from the prevention of the repossession of households. For the Government, this means the savings arising from households remaining in owner-occupation, rather than incurring housing benefit costs in the social or private rented sectors.
39. We have estimated the average annual housing benefit payments per household per year for both the social and private rented sectors, differentiating between households in London and the rest of the UK. Using these average costs, the estimated number of households expected to take-up HMS, and many of the assumptions used in the cost analysis above, we estimate that the total benefit to the exchequer amounts to around £58m (present value). This could be an under-estimate given the additional housing benefit costs incurred for those households that spend time in temporary accommodation or the private rented sector before entering the social rented sector. This is our conservative central estimate assuming that lenders accounting for 50 per cent of the number of eligible households in 3+ month mortgage arrears offer HMS and take up the option of the Government guarantee. If a higher number of lenders offer HMS, then it can be expected that a higher number of households will take advantage of the support with consequently higher expected benefits. The table below sets out the expected benefits for different numbers of households joining HMS:

Possible HMS take-up over 2 years	Expected monetised benefit (present value)
85,000*	£117m
42,000**	£58m
31,000	£43m

* Estimate if 100% of the mortgage market is covered

** Central estimate if 50% of market is covered

40. The method of calculating these savings involves three steps:

- i) Calculation of annual housing benefit savings per household, for both the private rented sector (PRS) and social rented sector (SRS), calculated separately for London and the rest of the UK. This requires an assumption about the repossessed household's income which has been estimated using data on the average house price, loan-to-value percentage and mortgage rate (consistent with the assumptions made for the costs of HMS)
- ii) Calculation of housing benefit savings per household over time, again for the private rented sector and social rented sector, and for London and the rest of the UK. It is assumed that households will require Government support on HMS for an average of one and half years (consistent with the cost analysis) and therefore there will be an average one and a half year period of housing benefit savings. Rental growth of 0.5 per cent in the social sector and 1% in the private sector is also assumed;
- iii) Calculation of total housing benefit savings for all households. This takes the sum of the number of households who would have been repossessed in the absence of HMS plus the number of households that are granted a temporary reprieve from repossessions, and multiplies this sum by the housing benefit savings per household. This takes account of the different estimated housing benefit savings in London and the rest of the UK and the numbers whom, without HMS, would enter the social sector, private rented sector, return to owner-occupation or stay with family and friends (and thus incur no housing benefit costs). This analysis uses 2007 Survey of English Housing (SEH) data on the housing sector destinations of repossessed households as well as Ministry of Justice data on the geographical location of repossessions (based on court actions). The 2007 SEH data shows that since 2000, of the households that have given up their home due to mortgage repayment difficulties, 24 per cent now reside in the social rented sector, 32 per cent in the private rented sector and 44 per cent go to family/friends/back into home ownership¹⁰.

¹⁰ Survey of English Housing 2007

Unquantified benefits

41. HMS offers a number of further benefits which should be weighed against the costs, even though they are not expressed in monetary terms. In particular, we have not quantified the benefits from lenders who offer comparable arrangements to HMS and grant extended lender forbearance without taking up claiming on the Government guarantee. The impact of such a commitment is very uncertain, but we would hope that it would lead to significantly more forbearance leading to reduced repossessions and savings to the exchequer.
42. As noted above, HMS will result in a lower level of repossessions relative to the do nothing scenario (baseline). Repossessions can be costly for lenders, borrowers and the Government:
 - the most important non-monetised benefit will accrue to households that are able to remain in their homes as a result of support provided by HMS rather than having to sell up and relocate. This will reduce stress and possible ill-health, and disruption to education and employment. An additional two-year period of stability could lead to a more sustainable employment and financial solution being found for households. These benefits will apply to all households receiving support through HMS (whether their lender takes up the option of the Government financial guarantee or not)
 - HMS will reduce the potential costs to lenders of repossessions; this includes the potential failure to recover all the outstanding mortgage, the loss of the interest they would have received if the loan had not failed, and the fixed costs of repossessions proceedings
 - it is also likely that the existence of HMS, and publicity surrounding the Government action to deal with the increase in repossessions, will raise the profile of support available to households. A positive benefit is that this may encourage more borrowers to contact their lender or debt advisers at an earlier stage. This will allow their options to be explored and financial plans put in place, even if the borrower is not eligible for, or advised to, enter HMS
 - although the quantified benefits include the savings to Government through reduced housing benefit payments, there are also costs associated with the provision of social rented sector accommodation. By reducing the number of households potentially in need of social rented sector properties, the Government can expect savings in terms of the number of new units it needs to build, with benefits also for those households currently awaiting a social rented sector property who might otherwise have to wait longer

- HMS can be expected to benefit the economy by avoiding the huge negative publicity associated with a significant number of repossessions. This will increase consumer confidence in the housing market and increase the speed of recovery. By lessening the number of repossessed properties available on the market, HMS will also have a positive effect on house prices for existing homeowners and the wider economy
- By preventing and delaying repossessions, HMS is likely to help in efforts to create more financial stability. Even a slight reduction in the risk of further financial instability offers a sizeable expected benefit
- recent research¹¹ also suggests that avoiding clusters of repossessions is important in preventing neighbourhood decline and the associated social costs on communities. Preventing and delaying repossessions will help avoid costs which occur when:
 - areas become less desirable as a result of properties falling into visible disrepair
 - units are vacant, contributing to blight and attracting vandalism and crime
 - community cohesion is lost because repossessed properties are either empty or used for private renting (with a higher turnover of tenants)

Net benefits

43. Given certain assumptions, we estimate the overall net benefit (present value) to the exchequer associated with the introduction of HMS at £14m. This excludes the many important non-monetised impacts, especially benefits that cannot readily be quantified. In particular, a conservative central estimate of borrower take-up based on lenders offering HMS and taking up the option of the Government financial guarantee, does not include the benefits arising from other lenders who offer comparable arrangements to HMS and grant extended lender forbearance.
44. As noted above, there is significant uncertainty surrounding the likely take-up and costs of HMS given that it is lender-led. We have conservatively provided a central estimate of the number of households joining HMS based on the number of lenders taking up the option of the Government financial guarantee. If a higher number of lenders offer HMS and take up the option of the guarantee, then we can expect the central estimate of borrower take-up to increase and the expected costs and benefits will rise. Alternatively, changing economic variables may persuade lenders to put

¹¹ Schuetz, J., Been, V. and Ellen, I. (2008) Neighborhood Effects of Concentrated Mortgage Foreclosures, New York University School of Law Working Paper 151.

fewer households onto the scheme. Even if far few households are entered we expect there to be positive net benefits to the exchequer. The table below sets out the expected net benefits (present value) for different levels of HMS take-up:

Possible HMS take-up over 2 years	Net benefit (present value)
85,000	£34m
42,000	£14m
31,000	£6m

45. Average mortgage rates are one input variable that can increase costs significantly without increasing benefits, and so are a key variable affecting our estimate of the net benefits. We have therefore illustrated in the following table the sensitivity of net benefits to differing average mortgage rates. While there is the risk that interest rates will increase over the period that HMS is in operation thereby lowering the monetised net benefit, we have made a central estimate that mortgage rates will average just over 5 per cent. This is based on current market expectations of interest rates and because interest rates on the scheme are capped at 8 per cent.

Average mortgage rate*	Net benefit (present value)
4%	£34m
5%	£14m
6%	-£5m
7%	-£20m

*The sensitivity analysis assumes that the mortgage rate stays constant over the duration the borrower is on the scheme.

Monitoring and evaluation

46. Lenders who are eligible to claim on the Government guarantee will be required to enter the details of borrowers joining HMS onto an on-line reporting system. The Government will receive monthly reports from its delivery partner containing information on the number of eligible borrowers and those entering HMS. This will enable the Government to monitor entrants onto the scheme, the eligible borrowers being rejected by lenders, and the liabilities and claims being incurred. The information will also enable the Government to carry out validation and fraud checks to ensure that borrowers are eligible for HMS and that the correct information is being provided.

47. We will constantly monitor lender sign up and borrower take-up to ensure that HMS has the expected impact on repossessions. We will provide reporting information periodically as required. The data to be provided was agreed through consultation with lenders and has been designed to allow the Government to understand the scheme performance, whilst minimising the impact on lenders.
48. We intend to evaluate HMS while the scheme is still open to new entrants in order to review its operation, in particular: take-up, costs, and ease of access both for borrowers and lenders. The evaluation will assess HMS against its intended outcomes in order to determine its effectiveness and whether there is a case for alteration or extension of the scheme. We are also asking lenders who take up the option of the Government guarantee to review each borrower's financial circumstances after one year to ensure that they are still eligible and that HMS continues to offer the best form of forbearance.

Enforcement

49. As HMS is voluntary, the Government will not be required to enforce participation. However, as part of the monitoring and evaluation, we will want to assess that the support is appropriately open to all lenders and eligible borrowers, and that there is compliance with the rules of HMS through validation and audit checks.

Specific impact tests

Competition Assessment

50. HMS will be open to all mortgage lenders and therefore should not distort the market. It is unlikely to limit the supplier's ability or incentives to compete as the scheme will only be applicable to those individuals that opened a mortgage prior to December 2008 and therefore will already have a contractual agreement with that lender. However, it is implicit that HMS will interfere with the normal commercial operation of mortgage lenders by offering support to extend forbearance to individual borrowers. HMS has therefore been notified to the European Commission and approved by them for state aid purposes.
51. There is the potential for some competition effects on the market for mortgage insurance and associated insurance products, for example, protection against unemployment. The introduction of the guarantee could mean that individuals are less likely to take out private insurance in the future on the assumption that there will be Government assistance. However, given that HMS is only open to borrowers with mortgages taken out before 1 December 2008 (who presumably would have already

taken out insurance if relevant) and the relatively low take-up of both mortgage and unemployment insurance¹², we consider that any effect would be marginal.

Small Firms Impact Assessment

52. The Impact Assessment recognises the administrative costs to lenders of participating in HMS. It is likely that smaller lenders will experience a relatively higher administrative burden, for example, because of the costs relative to their overall mortgage lending and also because of particular regulatory reporting requirements. However, it is equally likely that smaller lenders will have fewer staff to train, and therefore could have lesser costs overall than the larger lenders. We have been working with smaller lender representative trade bodies to address particular issues that they may face and will continue to work with lenders to support their participation in HMS. Ultimately, we are not imposing a burden on smaller firms as the support is voluntary and lenders will factor in the costs as well as the benefits in deciding whether to offer HMS.

Legal Aid Impact

53. No impact on legal aid has been identified.

Sustainable Development / Carbon / Other Environmental Impact

54. No impact on the environment has been identified.

Health Impact

55. The support offered by HMS will protect vulnerable households from the negative consequences that can follow repossession, including poor health outcomes.

Race Impact

56. We have considered the possible impacts of indirectly excluding those with Sharia mortgages from HMS given that Islamic law does not permit the payment of interest on loans. While this is not a racial impact per se because it affects members of a faith group, it is likely that the majority of those members are likely to consider themselves as members of an ethnic minority. The Government's intention is that all potential lenders and borrowers are able to access support if necessary and that they are treated fairly under the scheme. We are therefore working with HM Treasury (who lead on this finance sector), lender representatives and the Homes

¹² Mintel's report on 'Mortgages, Finance Intelligence' March 2007 shows that 25% of all new mortgage advances in 2005 were accompanied by Mortgage Payment Protection Insurance. A survey commissioned by the Post Office in November 2008 found that 71% of people do not have any form of unemployment insurance www.news.royalmailgroup.com/news/article.asp?id=2423&brand=Post_Office_network

and Communities Agency to ensure that arrangements are in place to be able to administer HMS to those with Sharia mortgages should lender or borrower demand arise.

Gender / Disability Impact

57. HMS will offer support to all parties the same regardless of gender and disability.

Human Rights Impact

58. No impact on human rights has been identified.

Rural Proofing

59. Published data on mortgage possession orders are only available by county court, where the court has access to the Possession Claims On Line (PCOL) data collection system. A number of rural courts do not have access to PCOL and thus an estimate is made of the missing possession orders from these courts in published national and regional figures. Thus, given the unavailability of local data on possession orders in some areas, it is difficult to accurately estimate the relative incidence or impact of repossessions on rural and urban areas. We will therefore use the information gained through monitoring and evaluation to ensure that HMS does not impact negatively on rural areas.

Specific Impact Tests: Checklist

Ensure that the results of any tests that impact on the cost-benefit analysis are contained within the main evidence base; other results may be annexed.

Type of testing undertaken	Results in Evidence Base?	Results annexed?
Competition Assessment	Yes	No
Small Firms Impact Test	Yes	No
Legal Aid	No	No
Sustainable Development	Yes	No
Carbon Assessment	Yes	No
Other Environment	Yes	No
Health Impact Assessment	Yes	No
Race Equality	Yes	No
Disability Equality	Yes	No
Gender Equality	Yes	No
Human Rights	Yes	No
Rural Proofing	Yes	No

Annexes

HOMEOWNERS MORTGAGE SUPPORT POLICY SCHEME DESCRIPTION

Eligible Group:

The Government guarantee will only attach to loans where borrowers:

- have demonstrated that they have had a temporary loss of household income from employment or self-employment of a scale which affects the household's ability to make full mortgage payments, but which is not expected to be a permanent loss of income. Evidence of income loss must be provided by borrowers for lenders to validate eligibility
- have been making regular payments (but not necessarily in full) in agreement with their lender for at least five months
- the lender and borrower must have discussed alternative forbearance options and, where appropriate, exhausted these before the borrower is entered on to the scheme
- have received debt advice from an accredited debt advisor. Borrowers should receive a Common Financial Statement or equivalent, confirming basic financial information such as income and expenditure that can be shared with the lender. The advice will encourage the borrower to consider the long-term sustainability of the borrower's financial position, and the impacts and potential risks, including to the value of equity in the property, of entering the scheme
- have been assessed as being able to pay at least 30 per cent of the total monthly interest payment at the point of entry on to the scheme. Borrowers will need to continue to pay as much as they can, subject to this minimum amount
- have total outstanding charges against their home no greater than £400,000 (excluding charging orders as they are ineligible for guarantee under the scheme)
- have no savings in excess of £16,000 i.e. the equivalent limit to Support for Mortgage Interest
- be an owner-occupier with the mortgaged property as their sole residence. Shared ownership or shared equity mortgages are covered by the scheme. The guarantee will not apply to buy-to-let or investment properties. A household possessing more than one home would not be eligible for the scheme
- have purchased their property with a mortgage before 1 December 2008. Homeowners will be able to re-mortgage on their existing property the principal outstanding after this date and will still be eligible for the scheme
- are not eligible for Support for Mortgage Interest (SMI)

- have been placed on interest-only terms as part of being qualified for the scheme. Borrowers seeking such assistance must be willing to switch their loan to such terms, as must the lender
- households with a second charge loan or a charge secured against their property may still be eligible for the scheme. The borrower will need to secure the agreement of all lenders with charges against the home (excluding charging orders) to be entered into the scheme. Borrowers will need to pay a minimum of 30 per cent of the monthly interest payment for each loan. Following launch of the core scheme for households, we will also explore options for extending the scheme so that it can be made available to small businesses which have stopped trading

It should be noted that the final decision on eligibility for (subject to the criteria set out above) and acceptance into the scheme remains entirely that of the lender.

Scheme duration:

- the scheme will run for two years subject to review and will be open for new entrants over that period. The deferral period will apply to borrowers for an initial period of up to one year from their point of entry at which point a review of their continuation on the scheme will be conducted
- if during that period the borrower's circumstances improve such that they are able to stop deferring interest, they will be expected to do so and the lender will be expected to require this. Once interest is no longer being deferred, the borrower leaves the scheme and there is no guarantee associated with subsequent payments. A borrower would be able to leave the scheme at any time, pending agreement for a new schedule of payment with their lender. Accurate and full information on their financial circumstances will need to be provided by the borrower to the lender at the one year review point to remain on the scheme
- the lender will review the borrower's eligibility to remain in the scheme after a year. This review will include consideration of the ongoing temporary nature of the borrower's income drop and the borrower's eligibility. The review must be informed by further advice from an accredited debt advisor, including advice for the borrower about the implications of continuing on the scheme and potential other options
- it is possible for a borrower to come back into the scheme, having left it, if they fall back into arrears as long as they meet the eligibility criteria and the lender believes they could benefit from the scheme
- the period in which claims can be made under the guarantee will last for 4 years after the borrower comes off the scheme. As a condition of participation in the scheme, lenders will need to commit to best practice in forbearance

when the borrower exits the scheme, and agree reasonable and affordable repayment schedules, with the aim of keeping any subsequent repossessions to a minimum

- after this, the liability returns to the lender, since it is assumed that a household still remaining in their home for that long will be continuing to make normal payments by that time

The Government guarantee:

- the total amount of the Government guarantee will not exceed 80 per cent of the total interest guaranteed and rolled-up into principal
- if, during the period of guarantee, the borrower defaults, then the Government will pay their lender the equivalent sum of the total amount of the Government-guaranteed interest deferred that is not recoverable from equity in the property (and, in addition, "interest on the interest" to an agreed formula). The Government will only accept a claim on a property that has been repossessed and sold
- the Government will not guarantee any interest deferred on payments made under a charging order. As stated previously however, borrowers with such orders against their properties may still be eligible for the scheme
- the Government will impose an interest rate cap of 8 per cent, benchmarked appropriately to the base rate. Mortgages at rates in excess of this cap could still be included in the scheme but the guarantee would only apply up to the capped rate of interest. Lenders will be required to maintain the borrowers' contracted rate of interest when they enter the scheme at or below the current contracted rate of interest, subject to reasonable changes linked to base rate movements
- the Government will set caps on the liabilities incurred for each participating lender. Allocations will be set according to shares of lending secured against residential property and adjusted to reflect shares of total arrears on a 70:30 basis

Lender forbearance:

- for each month that the borrower remains on the scheme, the lender will add the month's worth of interest deferred to the borrower's total principal mortgage debt
- the lender must conduct regular assessments of the borrower's financial condition including a comprehensive review after the borrower has been on the scheme for a year
- as stated above, lenders will need to commit to best practice in forbearance when the borrower exits the scheme, agreeing reasonable and affordable repayment schedules with borrowers

Borrower assistance and implications:

- borrowers will need to provide proof of loss of income and confirmation that they have received independent debt advice to be deemed eligible for the scheme
- borrowers will need to be deemed able to pay at least a minimum monthly payment of 30 per cent at the point of entry into the scheme to be eligible. In all cases, the borrower should pay the highest level of contribution they are able to pay
- interest payments deferred under the scheme by the borrower will be added to the total amount of their existing debt on a monthly basis. Borrowers will not be exempt from payment, and will simply be deferring payment until their personal situation improves
- application of the government guarantee does not diminish the borrower's existing legal obligations regarding their mortgage

Once the scheme is in operation, the Government will monitor performance and keep the scheme's design under review. Any changes would not apply retrospectively.

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