

Support for Mortgage Interest informal call for evidence: a response from the Social Security Advisory Committee

Introduction

The Social Security Advisory Committee (SSAC) welcomes the chance to comment on the informal call for evidence in respect of Support for Mortgage Interest (SMI).

General Comments

SSAC has previously reported on SMI in December 2009 when it took on formal referral¹ the regulations introducing some changes to SMI, including the shortening of the waiting period, the introduction of time limiting and freezing the standard interest rate. We recommended that the then-Government removed provisions relating to the time-limiting of SMI and that, if they were to go ahead, the Government should review the two-year cut-off by February 2012.

There can be little doubt that SMI has played and continues to play, a very important role enabling many thousands of households to remain home owners. Its existence acts as a strong incentive to mortgage lenders to use forbearance under circumstances in which they would, otherwise, repossess a home. During the current economic downturn, levels of arrears and repossession would have been considerably higher without its existence.

So when considering ways to amend the rules for SMI in pursuit of the objective of ensuring value for money for the taxpayer, it is important that DWP gives due consideration to the considerable costs that arise to the taxpayer of people losing their homes through repossession. The financial costs of repossession and associated social costs of arrears as well as repossession could outweigh any potential savings in SMI.

Consequently, in order to develop a solution which will work for the long term, we believe it is important to consider the policy on SMI from a range of perspectives, not just from the point of view of welfare reform, but taking into account housing policy and the state of the housing market in the owner occupied sector and regulatory policy on mortgage lending and mortgage forbearance.

We would therefore be concerned if changes were being made to SMI while the housing market remains stagnant, many households have negative equity and many are being kept in home-ownership through lender forbearance. These factors have the effect of limiting the options for people who might find

¹ The Social Security (Housing Costs Special Arrangements) (Amendment and Modification) Regulations 2008 and The Social Security (Housing Costs Special Arrangements) (Amendment) Regulations 2009: Report by the Social Security Advisory Committee, December 2009

their entitlement reduced and a shortfall on their mortgage repayments. In such circumstances households lack the option of trading down to a smaller, less expensive property. Again, this may push up the number of repossessions.

We are aware that the Financial Services Authority is concerned about the large number of households being kept in their home through forbearance for whom home ownership is never likely to be sustainable. We therefore recommend that DWP policy on SMI is formulated in consultation with the Financial Services Authority and with lenders themselves, who have been prepared to exercise forbearance with people who have found themselves in arrears. We also suggest that the Department maintains dialogue with the Council of Mortgage Lenders.

We think that there is an ideal opportunity here to address the financial cliff edge when someone in receipt of SMI moves into work. At present there is a four week run on and we think that this should continue. But there is also a need to think more radically about the best way of supporting home buyers who move out of employment and of smoothing their path back into work. This would fit with the policy aims of Universal Credit to make work pay.

Issue 1: Putting a charge on property

- *Question 1: Do you think payments for support for mortgage interest should be recouped from claimants who are in receipt of help on a long term basis?*
- *Question 2: What period of time would represent a long term basis? For example, two years?*
- *Question 3: What are your views on the idea of recouping support for mortgage interest payments from long-term claimants through a charge on their property?*
- *Question 4: Are there other ways that Government could recoup or reduce the cost of long-term SMI claims?*
- *Question 5: Should there be a fixed period of grace before the charge is applied?*
- *Question 6: Once it is applied should it relate to the total value of the support provided?*
- *Question 7: Should the proposal to put a charge on a property be extended to cover all recipients of SMI, effectively abandoning the two year limit in place for claimants who receive SMI with Jobseeker's Allowance or its future equivalent with Universal Credit?*

We consider that there is an argument for introducing a charge on the property, particularly for long-term recipients of benefit, but it is crucial that the design is right.

A charge may be justifiable but should only be levied after a certain period has elapsed, perhaps of around two years, to tie in with the current time-limiting. Moreover, it should be designed in consultation with lenders and the FSA to ensure that forbearance would continue to be applied. A complicating factor however is people who, at the time SMI is being paid, have either negative equity or no equity in their home. Care would have to be taken that as a result of the Government taking a second charge on the property this did not precipitate lenders into repossession.

Issue 2: Standard Interest rate

- *Question 8: Do you think that the current method of calculating the standard interest rate is the fairest and most effective method?*
- *Question 9: Is there another method of calculating a standard interest rate for SMI that may be fairer or more effective?*
- *Question 10: Should any action be taken in respect of the treatment of 'excess SMI' payments – if so, what?*

We agree that it is unacceptable that some people should receive SMI payments that exceed the amount they actually have to repay. On the other hand, we do not think that the solution to this problem should be at the expense of other people experiencing a shortfall on their payments. We would, therefore, like to see a more nuanced approach to the payment rate for SMI, than the one that is currently in operation.

We have commented before that this would reflect the amount of interest actually in payment. We have noted the calculations undertaken by the Council of Mortgage Lenders showing that payment of interest at the rate payable on individual mortgages could save around £26 million². We do recognise, however, that this could introduce additional administrative complexity and on balance we would favour simplification over complexity. To try and balance these two aims we would advocate there being different standard rates for different types of mortgage to help to reduce the potential for large over or underpayments. We wrote to Ministers about SMI when the legislation to introduce the new lower rate of the standard interest rate was brought to the Committee for scrutiny in July 2010³ by the Coalition Government. We recommended that the Department should explore introducing three different average interest rates, to cover fixed rate, tracker and variable rate mortgages. We continue to think that this may be a sensible way to avoid some of the issues inherent in having one interest rate for all, without overly increasing complexity.

² *CML News and Views* February 2012

³ The Social Security (Housing Costs) (Standard Interest Rate) Amendment Regulations 2010

Issue 3: Mortgage Interest Direct (MID)

- *Question 11: Do you think that it is the right policy to move away from the Mortgage Interest Direct scheme for most claimants?*
- *Question 12: If we move away from paying support for mortgage interest by Mortgage Interest Direct, in what exceptional situations should claimants have their mortgage interest payments made direct to the lender and what criteria could be used to determine when this should happen?*

We think that if the Department is to move away from MID, this should be carefully thought out in order to ensure that it did not lead to more repossessions. In our experience, MID has encouraged lenders to show forbearance when there is a shortfall with SMI as all the money is then paid directly to the lender.

We note with interest that the Council of Mortgage Lenders has said that they believe that the removal of MID would lead to an increase in arrears.⁴

Issue 4: The treatment of home improvement loans

- *Question 13: Do you think that the Department should move to a simplified approach for home improvement loans, subject to a cap on the amount of loan on which interest is payable?*

We agree that there should be a simplified approach for home improvement loans. This could be by allowing all home improvements, or by specifying which home improvements could be eligible, for example, only those which make the home safer, drier or warmer. We think that to cap the amount at 70% - 80% would introduce unnecessary complexity.

Issue 5: Linking rules

- *Question 14: Do you agree that the 12 and 52 week rule should be retained for SMI purposes?*
- *Question 15: Do you agree that certain other linking rules should no longer apply as a simplification measure flowing from the introduction of Universal Credit?*

We think it is important to keep the 12 and the 52 week linking periods. We agree that these will need to be adjusted to ensure people who may be lifted off benefit while, for example, on training and employment schemes are protected.

⁴ *CML News and Views* February 2012

Turning to the second consultation question in this section, we appreciate and endorse the need for simplification. We are concerned, however, that certain aspects of the linking rules appear to have been overlooked in the consultation document. Although labelled as 'linking rules' in the relevant regulations, they are in fact rules that treat a claimant as entitled to and/or in receipt of the benefit when they are not. They therefore also serve other functions. It is important to bear this in mind in any changes made to the linking rules so as not to create hard cases and to avoid unforeseen consequences. For example:

- The linking rules allow claimants to retain transitional protection if a claim is broken for a temporary period. There are a number of types of such protection, eg for claimants getting help with a type of housing costs that can no longer be met, or without a limit on the mortgage capital upon which the SMI calculation is based.
- Currently a former member of a couple can be treated as entitled to benefit for the period his/her former partner was entitled to benefit for them as a couple. Likewise, someone who makes a claim as a member of a couple can be treated as entitled to benefit for the period when the other member of the couple was claiming as a single person. The result of this is that the claimant does not have to serve the waiting period (or part of the waiting period) that the former/new partner has already served. Under UC the household is assessed, but we would like to see some protection for couples who may separate.
- Where a claimant has income, such as a non means-tested benefit or part-time earnings, which is higher than the applicable amount without SMI but lower than the applicable amount with SMI, s/he needs to be treated as on benefit in order to ever start, and then reach the end of, a waiting period. Again, account of this will need to be taken in the new rules for SMI under UC.

Issue 6: Time limiting

- *Question 16: Should certain categories of claimants, for example lone parents and people with a disability, moving onto Jobseeker's Allowance (or the equivalent within Universal Credit) be exempt from time-limiting?*
- *Question 17: Should there be a limit on the number of times a claimant can access two years of SMI?*

Time limiting of SMI for recipients of income-based JSA was introduced in January 2009. It does not apply, however, to other recipients of SMI. We did not support the introduction of the time limit when the regulations came before the Committee at the time and we would not support its extension to people receiving Income Support, Pension Credit or income-related Employment and Support Allowance or for recipients of Universal Credit.

At the time we were concerned that the Government had not taken enough account of the continuing stagnation of the housing and labour markets, and that the estimated savings were offset by the potential costs of providing accommodation for homeless families following repossession. We consider that these concerns continue to apply in the current economic situation.

Moreover, if the policy to take a charge against the property is to be introduced we do not believe that a case can be made to time limit claims to SMI even for income-based Jobseekers Allowance recipients. Subject to a period of grace as discussed in our response to issue one, the Government would be likely to recoup any monies paid.

Once again (as discussed above), the DWP should ensure that its policy supports (and does not undermine) the work that the FSA is doing in relation to the exercise of forbearance by lenders.

Issue 7: Waiting period and capital limit

- *Question 18: Have either of these two measures (13 week waiting period or £200,000 capital limit) been effective in reducing the likelihood of repossession? Where possible, please supply evidence to support your response.*

This is another issue which could benefit for consideration alongside the work currently being done by the FSA. In 1995, the waiting period was extended to 39 weeks for all new mortgages and re-mortgages because the then Government believed it would stimulate the private mortgage protection insurance market. In the event, this expectation was not realised. Take up of MPPI has never been high, and has fallen in recent years. There is ample evidence of the mis-selling and unsuitability of MPPI policies, especially because of exclusions which meant that many policy holders could never have made a successful claim on them.

We advised against the lengthening of the waiting time for SMI in 1995, warning that this would lead to more arrears. Subsequent evidence has lent support to those concerns.

The waiting period was reduced in January 2009, in response to the economic downturn, so that currently it stands at 13 weeks. The same regulations also increased the capital limit from £100,000 to £200,000. The SSAC welcomed both of these changes at that time, believing that they would play an important part in containing levels of arrears and repossession.

A DWP research report by Janet Ford et al⁵ suggested that both the reduced waiting period and the increased capital limit have played a major role in

⁵ Ford, J., A. Wallace, M Munro, N. Sprigings and S. Smith, *An Evaluation of the January 2009 and October 2010 arrangements for Support for Mortgage Interest: The role of lenders, money advice services, Jobcentre Plus and policy stakeholders* DWP research report 740, 2011, summary, paragraph 6

holding down arrears and repossessions. For this reason we would not support either the current 13 week waiting period being extended or the £200,000 capital limit being reduced until economic conditions improve. Changing either of these before the employment and housing markets have improved would, inevitably, lead to a large increase in arrears and, therefore, repossessions, with wider consequences for the housing market and the economy more generally.