HOME BUILDERS FEDERATION

June 2010

Supporting Economic Recovery and Meeting Home Ownership Aspirations

Budget Submission June 2010

The Home Builders Federation (HBF) is the principal trade association representing the interests of private homebuilders in England and Wales. Our membership, which includes companies ranging from major national firms, through regional companies to smaller local companies, is responsible for more than 80% of the new homes built every year.

1. EXECUTIVE SUMMARY

Given the importance of home building to the economy and jobs, it is most important that the Government does not do anything in the Budget to destabilise the housing market recovery or set back the nascent recovery in home building which remains fragile.

The Government should continue to encourage lenders to increase lending, and it should seek to avoid a sudden withdrawal of Treasury and Bank support for **mortgage funding**, a move that could abort the housing recovery.

A positive rate of **VAT on new homes**, even at a low rate, would be very damaging for home building and would almost certainly result in a net loss of revenue for the public sector.

Until mortgage funding returns to more normal levels, we believe **HomeBuy Direct** should remain a form of Government support for first-time buyers.

There must be robust transitional arrangements in the move to an incentives-based **planning system** to avoid a damaging hiatus and further loss of housing output and jobs.

Modest public sector funding for **Kickstart** schemes will lever in substantial private sector investment and generate rapid increases in housing output and jobs. We would urge the Government to fund as many uncontracted Kickstart schemes as possible.

The proposed rise in **capital gains tax** could have a very detrimental impact on residential land availability unless there is some form of taper relief for non-business land owners.

The Federation continues to have serious concerns about HM Treasury's and HMRC's proposals for changing the **tax rules relating to self-employment** in construction and would therefore ask the new Government to reconsider the original proposals and agree not to pursue them.

2. THE ECONOMIC IMPORTANCE OF NEW HOUSING

New home building accounts for approximately 8.5% of Gross Domestic Fixed Capital Formation and 1.5% of Gross Domestic Product. Prior to the downturn the industry employed an estimated 335,000 people, with up to four times as many jobs in the wider economy dependent on home building.

Home building is important for Britain's economic recovery not just because of its direct contribution to GDP, but because of its rapid reaction time and because it generates local jobs across the country to reflect the widespread distribution of housing developments. Home builders are able to respond very quickly to an upturn in demand or to a Government stimulus such as Kickstart, immediately creating economic activity and jobs.

In addition to the economic benefits of new home building, there are enormous social benefits. Or put the other way round, the long-term undersupply of housing in Britain has major social consequences.

Britain has suffered from a persistent and serious undersupply of housing for several decades. This was well documented in the 2004 Barker Review. In the eight years 2000 to 2008, annual additions to the housing stock were 40,000 per year below annual household growth, clearly an unsustainable gap in the medium to longer term.

Housing completions fell to a post-war low in 2009: 118,000 in England, or approximately 142,000 in Great Britain which is the lowest peacetime total since 1923. Although the market has shown some modest improvement, this is from an extremely low base, forecasters expect a subdued recovery in home building over the next three years, and the recovery remains fragile.

The industry has suffered a large-scale loss of capacity since the second half of 2007. Based on the steep fall in housing completions since 2007, along with individual company announcements, it seems likely that somewhere between 100,000 and 150,000 house building jobs were lost during the recession.

The cumulative cost impact of policy and regulation, which has escalated dramatically over the last decade or more, means many housing developments are not viable. Without a substantial reduction in the regulatory burden, the sharp increases in costs from the steps to zero carbon in 2013 and 2016 will further damage viabilities - unless a sharp rise in house prices is assumed over the next few years, a highly undesirable basis for Government policies.

For all of the above reasons, it is most important that the Government does not do anything in the Budget to destabilise the housing market recovery or set back the nascent recovery in home building. This would be damaging not just for home builders, but for the wider economic recovery – and ultimately for the Government's efforts to control the fiscal deficit.

3. SUSTAINING THE HOME BUILDING RECOVERY: BUDGET MEASURES: DEMAND CONDITIONS

A firmly-established recovery in the wider economy and in housing demand is a pre-condition for a sustained recovery in home building.

3.1 Mortgage Finance

The Government should continue to encourage lenders to increase lending, and it should seek to avoid a sudden withdrawal of Treasury and Bank support for mortgage funding, a move that could abort the housing market recovery.

The supply of mortgage finance on affordable terms remains a serious constraint on new home demand. HomeBuy Direct, along with house builders' own shared-equity schemes and other sales incentives, have helped home builders during the last 12-18 months. However these can only ever be temporary measures. We need a return of higher LTV mortgages, at more affordable rates and charges, to facilitate a sustained increase in home building. We should also note our continuing concern that many lenders offer less favourable terms (e.g. lower LTVs) for new home buyers than for those buying second-hand homes.

While we understand the desire of the Treasury and Bank to remove support for mortgage lending, we are concerned that the lending industry's need to refinance some £300bn of publicly supported lending, plus the need to refinance a substantial volume of mortgagebacked securities, must risk further constraining mortgage availability over the next two or three years and aborting the housing recovery.

In our submissions to the recent FSA and Treasury consultations on mortgage regulation, we stressed that any tightening of regulation must take account of its potential impact on the new homes industry. In particular, regulation of buy-to-let and second-charge mortgages could have a disproportionate and unintended negative impact on new home sales. We have begun discussion with the FSA on second-charge mortgage regulation and will seek to discuss the industry's needs with officials at HM Treasury.

3.2 VAT on New Homes

A positive rate of VAT on new homes, even at a low rate, would be very damaging for home building and would almost certainly result in a net loss of revenue for the public sector.

New homes represent only 10-12% of total housing market sales, so that home builders are price takers. New home prices are largely set by prices in the second-hand market. If home builders tried to add 5% or 8% VAT to sales prices, new homes would be rendered uncompetitive with comparable second-hand properties, so that sales of new homes would fall dramatically.

Therefore, because in practice VAT could not be passed on to new home buyers, it would in effect become an additional development cost.

In the short to medium term, for homes built on land already purchased by home builders, the cost of VAT would have to come out of home builders' profit margins. As the industry is only beginning to rebuild profits after weathering the worst housing downturn for decades, this would produce further losses, with potentially serious implications for some companies.

In the longer term, however, most or all of the cost of VAT would have to be absorbed by residential land values. This would have many adverse consequences:

- It would inevitably lead to a steep fall in private new home building from today's already historically low levels as many sites would be rendered unviable;
- With a corresponding collapse in new Affordable Housing supply through the S106 link to private housing development;
- Leading to further job losses in the home building industry and dependent industries and sectors;
- With a damaging impact on house builders' profits in the short-medium term at a time when the industry is struggling to recover from the deepest recession for decades;

- It would further exacerbate the already serious undersupply of housing and worsen Britain's affordability crisis;
- To restore viability, local authorities would have to reign back their demands for planning obligations (Affordable Housing, community infrastructure);
- So that levying VAT would not result in any net additional revenue for the public sector (in effect the Treasury would gain at the expense of local authorities);
- And in fact the fall in home building and employment would cut Treasury tax revenues and adversely affect local government finances;
- Harmonising the VAT treatment of new homes and housing repairs and maintenance would do little to address the multitude of different taxation, policy and regulatory treatments of the two activities.

3.3 Supporting First-time Buyers

Until mortgage funding returns to more normal levels, we believe HomeBuy Direct should remain a permanent form of Government support for first-time buyers.

First-time buyer numbers are at historic low levels.

The fall in the overall rate of owner occupation in the last decade has been very dramatic among younger and middle aged households (see table below). Yet according to a new study by the National Housing and Planning Advice Unit (NHPAU), there has been no erosion of people's aspiration to home ownership: 82% of adults see owning a home as their ideal long-term tenure. Three quarters of 25-34 year olds who are not currently home owners and who think they will be renting in the next three years would like to buy a house but cannot afford to.

Owner occupation by age of household reference person (%)

Age of households	2001-02	2008-09
16-24	23	14
25-34	60	51
35-44	74	67
45-54	80	74
55-64	74	79
65+	64	75
All households	**70**	**68**

There are two solutions to the affordability crisis. First, we must see a restoration of affordable mortgage funding at higher LTVs. But in the longer term, the only solution is to bring housing supply and demand into better balance by increasing the rate of new home building.

Given the restricted supply of mortgage finance, and the extremely limited availability of higher LTV mortgages, HomeBuy Direct (HBD) has been a very positive support for new home sales to first-time buyers during the recession.

However first-time buyers are going to need continuing assistance in the recovery. It is going to take time – possibly some years – before higher LTV mortgages allow first-time buyers to buy without a very substantial deposit. House prices are still very high in relation in average earnings, despite the fall in prices during the recession, so that the average first-time buyer is going to require a large mortgage. Many first-time buyers already have sizeable student debt even before they contemplate taking out a mortgage to buy a home. And employment of young people has been particularly hard hit during the recession, so that many potential first-time buyers are going to take longer than in the past to achieve the higher income they will require to buy a home.

We strongly urge the Government to make HBD a permanent form of support for first-time buyers, or at least until the mortgage market fully recovers.

4. SUSTAINING THE HOME BUILDING RECOVERY: BUDGET MEASURES: SUPPLY CONDITIONS

4.1 Planning and the Supply of Viable Permissioned Residential Land

There must be robust transitions arrangements in the move to an incentives-based planning system to avoid a damaging hiatus and further loss of housing output and jobs.

We were most concerned at the Secretary of State's letter to local authority Chief Planners of 27th May. This had an immediate detrimental impact on local authority planning. Local plan preparations have been delayed, sites previously allocated in plans have been de-allocated, some local authorities are now refusing to determine planning applications, and some major sites have been refused on the basis of the letter.

While we understand the Government's intention to withdraw Regional Spatial Strategies and RSS targets, and we support the move to an incentives-based planning system, it is absolutely critical that the Government introduces comprehensive transition arrangements as we move to the new system. There must be interim targets – a plan-led system cannot function without local housing targets – and the match-funding incentives must be introduced immediately, along with the presumption in favour of sustainable development.

We would also urge the Government to undertake a thorough review of the cumulative cost burden of policy and regulation on residential development. This is having a major impact on development viability and will hold back the recovery in home building. We are especially anxious that the Government should reach an early decision on the definition of zero carbon that promotes the most cost-effective and economically efficient housing and energy solutions.

4.2 Kickstart: Supporting the Recovery

Modest public sector funding for Kickstart schemes will lever in substantial private sector investment and generate rapid increases in housing output and jobs. We would urge the Government to fund as many uncontracted Kickstart schemes as possible.

We fully appreciate the Government's need to make very difficult decisions about public spending. However spending cuts should be concentrated in areas that pose least risk to the economic recovery. If the recovery falters, tax receipts will fall and the deficit will worsen.

Kickstart schemes provide a very cost-effective mechanism to promote private economic output and jobs. Each pound of public funding will produce a much greater level of private funding, while most of the public money going into Kickstart sites will feed back to the Government in due course. Because Kickstart sites are, by definition, ready to go, public funding will have a rapid impact on output and jobs, thereby supporting the economic recovery.

4.3 Capital Gains Tax (CGT) and Residential Land Supply

The proposed rise in CGT could have a very detrimental impact on residential land availability unless there is some form of taper relief for non-business land owners.

The proposed increase in CGT will, we understand, apply to non-business assets. Our concern is that this could act as a serious deterrent to private land owners selling their land to housing developers. Either the owners would not be willing to sell because of the new significantly higher rate of tax, or they would seek to cover the additional cost of the CGT by increasing the price at which they would be willing to sell their land. In the former case, clearly no housing would be developed. In the latter, this would add very significantly to the price of land, in effect imposing a substantial increase in residential development costs. Given the already serious viability problems created by the cumulative cost burden of policy and regulation, CGT would render many more sites unviable unless some other areas of regulation were reduced to compensate. However, as with VAT (discussed above), any reduction in other regulations would mean that there is likely to be very little net gain to the state from levying CGT.

The CGT increase, as proposed, would have a particularly detrimental impact on smaller developers who are more likely to buy relatively small sites from private land owners. These same developers are already likely to be adversely affected by the recent change to PPS3 to stop so-called “garden grabbing”.

The obvious way around this problem would be to allow relief based on the time the land had been owned.

4.4 False Self-Employment

The Federation continues to have serious concerns about HM Treasury’s and HMRC’s proposals for changing the tax rules relating to self-employment in construction.

The Treasury and HMRC published a summary of responses in March to the consultation conducted in 2009 on their proposals that workers in construction should be deemed to be employed for tax purposes unless they qualify for one of three possible exemptions. We are concerned that this summary document still proposes to pursue a change to the tax rules on broadly the lines originally proposed - which it is acknowledged would have an adverse effect on the industry’s costs and flexibility.

Given that the evidence base used to justify these proposals is in our view questionable and insufficient (the impact assessment previously undertaken was we believe flawed) and any change of this nature might well have much wider ramifications for the employment market. To pursue something like the original proposals would be inconsistent both with the recognition of the need to tackle the increasing burden of regulation on home builders and the principles of better regulation. It would also be difficult to reconcile with the Government’s wish to reconsider IR 35.

We would therefore ask the new Government to reconsider the original proposals and agree not to pursue them in the light of our genuine concern.

John Stewart
Director of
Economic Affairs