POLICY NOTE

THE REDEMPTION OF HERITABLE SECURITIES (EXCLUDED SECURITIES) (SCOTLAND) ORDER 2018

SSI 2018/376

The above instrument was made in exercise of the powers conferred by Section 93 of The Housing (Scotland) Act 2014. The instrument is subject to negative procedure.

Policy Objectives

1. The Heritable Securities (Excluded Securities) (Scotland) Order 2018 exempts the securities described in articles 2 and 3 from section 11 of the 1974 Act. The right to redeem at year 20 is removed from the securities granted under the named schemes in paragraph 2(2) both before and after the Order comes into force. This right is removed from securities granted under the named schemes in paragraph 3(2) after the Order comes into force only.

2. The Scottish Government operates a number of shared equity schemes that make loans to borrowers which are linked to the property's value. These loans are secured by way of a standard security. In the early 1970s, finance for home ownership centred around traditional repayment or interest only mortgages. Section 11 of The Land Reform (Scotland) Act 1974 ('the 1974 Act') gives borrowers the right to redeem their security when the 20 year point in the loan term has been reached. From this point onwards borrowers are able to redeem their securities on repayment of the loan balance together with any interest and fees due. This is commonly known as 'the 20 year security rule'. One of the main purposes of the 1974 Act was to prohibit the creation of new feuduties (a fixed annual payment granting the owner of the property the right to use the land that the property was situated on). The 20 year security rule was introduced to ensure that landowners could not seek alternative sources of income through the introduction of ground rents or interest paid on long-term standard securities.

3. The provisions of section 11 of the 1974 Act do not fit well with modern financing arrangements for home ownership on a shared equity basis. This is because the 20 year security rule overrides any contractual provisions put in place as part of the shared equity agreement. Prior to the introduction of the Help to Buy (Scotland) Scheme shared equity agreements for the Open Market Shared Equity Scheme and the New Supply Shared Equity Scheme operated by the Scottish Government were arranged with a break clause at year 19. This ensured that the Government was not exposed to the financial risk that borrowers would be able to redeem their security at year 20, at the value of their original equity loan, rather than the market value of the equity stake at the date of redemption. Scottish Minister had intended replicating this approach for the Help to Buy (Scotland) Scheme in 2013. However, changes to the Financial Conduct Authority guidance around affordability tests and mortgage duration made the Council of Lenders and some members unwilling to participate in the scheme with the break clause in place.

4. To ensure lender participation continued across all of the Scottish Government's shared equity schemes the break clause was removed on 1 April 2014. Help to Buy (Scotland) was launched on 27 September 2013 with no break clause in the legal documentation.

We understand that the right to redeem a security at year 20 could be viewed as a possession at for the purposes of Article 1 of the First Protocol to the European Convention on Human Rights (ECHR). Scottish Ministers have therefore informed all shared equity purchasers, from the 1 April 2014 onwards, of their intention to bring forward legislation to exclude their shared equity schemes from the effects of 'the 20 year security rule' which would remove purchasers right to redeem at year 20.

Consultation

5. Since October 2014, Scottish Ministers have undertaken a number of public consultations on the proposal to exempt certain heritable securities from 'the 20 year security rule'. The first consultation, which ended in February 2015, enabled organisations and individuals to express their views and opinions on the broad principles of the proposed approach and to highlight any local shared equity schemes which should be considered. 14 responses were received and all agreed with the principle of bringing forward legislation to mitigate the financial impact of 'the 20 year security rule'. A further consultation was undertaken with those respondents who submitted schemes for inclusion in the Order.

6. As the formal consultation was completed several years ago and the Order could not be pursued at this time, Scottish Ministers have undertaken a further informal consultation with Local Authorities and Registered Social Landlords. This further consultation period at the start of 2018 gave respondents the opportunity to submit any new schemes for consideration and to ensure that any previously notified schemes were still relevant. These responses have informed our decisions on the local shared equity schemes which are included in the Order.

Impact Assessments

7. A partial Equality Impact Assessment (EQIA) was undertaken in 2014 which built upon the findings from the EQIA which was undertaken on the Housing (Scotland) Bill 2013. This partial EQIA was included in the consultation (which closed in January 2015) to ascertain views on the equalities impact of the proposed approach to exempt certain heritable securities from the effects of 'the 20 year security rule'. We concluded that there are no equality issues which arise as a result of the proposed approach.

Financial effects

8. A full Business and Regulatory Impact Assessment (BRIA) has been completed and is attached. Dis-applying the 20 year rule ensures that the bodies operating the shared equity schemes named in the Order receive an adequate return on their shared equity stakes over time. The majority of organisations affected are Registered Social Landlords and they are likely to use any resulting receipts to re-invest in affordable housing. Detailed information on the potential scale of the lost receipts is contained in the BRIA.

9. The Scottish Government plans to review the Order every 5 years to ensure the necessary schemes are included.

Scottish Government
Directorate for Housing and Social Justice
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