

REPORT TO RESOURCES PDG

REPORT OF: HEAD OF FINANCE

REPORT NO: HOF 186

DATE:

TITLE:	Local Authority Mortgage Scheme – Local policy for scheme eligibility	
KEY DECISION OR POLICY FRAMEWORK PROPOSAL:		
PORTFOLIO HOLDER: NAME AND DESIGNATION:	Cllr Mike Taylor Assets and Resources Portfolio Holder	
CONTACT OFFICER:	Daren Turner d.turner@southkesteven.gov.uk 01476406310	
INITIAL IMPACT ASSESSMENT:	Carried out and Referred to in paragraph (7) below:	Full impact assessment Required:
Equality and Diversity		Yes
FREEDOM OF INFORMATION ACT:	This report is publicly available via the Your Council and Democracy link on the Council’s website: www.southkesteven.gov.uk	
BACKGROUND PAPERS	Sector State Aid Paper Sector Accounting Principles Paper Sector Risk assessment	

1. RECOMMENDATION

Resources PDG is asked to consider a local policy for scheme eligibility based on detail in Section 7 of this report. The key criteria being:

- The area of the district, determined by postcode, to be covered by this scheme.
- The maximum loan size to be supported (i.e. 95% of house value).
- Confirmation of first time buyers only.
- The size of the initial scheme (i.e. £1m)
- The preferred initial partner(s).

2. PURPOSE OF THE REPORT

- 2.1 The purpose of this report is to propose the local policy in respect of the introduction of the Local Authority Mortgage Scheme in South Kesteven.

3. BACKGROUND

- 3.1 At its meeting in December 2011, Cabinet agreed to:
- 3.2 recommend to Council participation in the Local Authority Mortgage Scheme (LAMS), initially in partnership with a recognised national provider for £1m;
- 3.3 recommend that Council approve plans to extend the scheme across other lenders as they enter the scheme, or with Lloyds plc, up to a total value of £5m subject a full analysis of impact against priorities of the first £1m;
- 3.4 ask that the Resources PDG undertake initial development of a local policy for the scheme eligibility for Council approval;
- 3.5 Delegate to the Strategic Director (corporate services) the authority to investigate and where required execute the required legal documentation in order to satisfy scheme participants.
- 3.6 Whilst gathering information to form the priorities Council became aware of the plight of home buyers in the district, particularly first time buyers, as a result of the economic down turn and the increasing requirement as regards deposits by mortgage providers. This was leading to growth in the Councils own housing register and stagnation at the lower end of the property market in the district. This is in turn could be inhibiting key works staying in or moving to our district and also young families staying in the area.
- 3.7 House prices nationally have continued to fall over the last 12 months, and the outlook remains uncertain. This pattern is followed in our district. The lack of buyers, together with the ongoing lack of mortgage availability means house prices are likely to continue to slide. Nationwide Building Society predicts house prices in 2011 to stay weak as a result of the uncertainty surrounding the economy and the Government's massive spending cuts.
- 3.8 Appendix A gives detail of house sales and values across the district. Members may wish to consider this information when forming policy on the size of mortgage to support and the areas of the District where the scheme should operation.
- 3.9 Appendix B gives detail of average sale value across the district.

4. Local Authority Mortgage Scheme

- 4.1** Sector Treasury Management services (the Council's treasury advisers) have developed a national scheme, initially in conjunction with the Lloyds banking group, to allow Councils to provide support to first time buyers. The scheme is aimed at first time buyers providing help for potential buyers who can afford mortgage payments - but not the initial deposit- to get on to the property ladder. There are 6 providers currently listed as "providers" in the scheme, they are Lloyds PLC, Leeds BS, Furness BS, Teachers BS, Saffron BS, and Leek BS (clearly the Council would look to a partner with a presence across our District to ensure maximum participation and impact)
- 4.2** The scheme operates as follows:
- 4.2.1 The Council would specify the qualifying characteristics for those who should qualify for a mortgage under the scheme (see section 5 below). The Council would also specify whether there would be a maximum loan value, and the total level of support offered by the council;
- 4.2.2 Potential Buyers would approach the lender directly and the lender would deal with the Council. The Council will not know the identity of the individuals concerned, and have no role in approving individual mortgages;
- 4.2.3 The Bank will assess the buyer against its own credit criteria, as well as the Council's criteria;
- 4.2.4 If a potential buyer meets the strict credit criteria applied by the lender, and meets the criteria set out by the Local Authority to qualify for a mortgage under the scheme, the Local Authority will provide a top-up indemnity to the value of the difference between the typical Loan to Value (LTV) ratio of around 75% and a 95% LTV mortgage. The potential buyer will thereby obtain a 95% mortgage on similar terms as a 75% mortgage, but without the need to provide the substantial deposit usually required;
- 4.2.5 The Council will deposit a sum with the bank equal to the total value of the overall indemnity offered (assuming cash backed lender requirement – see section 4.3);
- 4.2.6 The bank would lend all the money agreed under the mortgage to enable the purchase to be made;
- 4.2.7 The buyer would make repayments to the bank, and liaise with the bank on all issues relating to the mortgage; and
- 4.2.8 The indemnity provided by the Council will last for 5 years. After this time the sum deposited with the bank is returned to the Council with interest.

4.3 The scheme can be supported by the Council in two ways, in that the indemnity is either cash backed or unfunded as follows:-

4.3.1 If the indemnity is un-funded, the Local Authority will receive a premium a fixed amount of the value of the indemnity actually provided, typically in the region of £500 per mortgage.

4.3.2 If the indemnity is “cash backed”, i.e. supported by a deposit, the Local Authority will be required to place a 5-year deposit at the start of the financial year to the full value of the indemnity being offered. The deposit will be in place for the term of the indemnity – i.e. 5 years (with the possibility of a further 2 year extension if the mortgage is in arrears at the end of the initial 5 years) - and may have conditions / structures attached. The Local Authority will receive a 5-year commercial deposit rate + a premium of 0.70% from the first lender to join the scheme, other lenders will offer similar terms.

4.3.3 In accordance with the legislation, the lender will not have a legal charge over the deposit. In the event of an indemnity being called and an amount being payable by the Local Authority to the lender, a request for payment would be made by the lender. The Local Authority will undertake to settle the amount payable within 30 days.

4.4 The indemnity would only be called upon, leading to a cost for the Council, if a loss is crystallised by the lender. This would require a default by the buyer, repossession by the bank and then the property to be sold for less than the value of the mortgage.

By way of example:

4.4.1 Property valued at £100k, mortgaged at £95k (funded Local Authority indemnity £20k, Bank Mortgage £75k), was subsequently sold for £70k, the bank would request the full £20k indemnity from the Local Authority. In this case the value of the property would need to have fallen by 30% from the original valuation;

4.4.2 If the property was sold for £90k the bank would request £5k from the Council. In this case the value of the property would need to have fallen by 10% from the original valuation.

4.5 The Council will only face costs if both these situations arise – that there is default, and the subsequent resale value is less than the value of the mortgage. Such costs would be funded from the interest gained in depositing the indemnity funds. Information from the Council of Mortgage lenders indicates that the number of repossessions by first charge mortgage lenders in 2010 was 0.3% of all mortgages. Over the five year period, the following would need to happen for the costs to the council to exceed the interest income (assuming a cash backed scheme):

- 4.5.1 Defaults to be ten times higher than the 2010 level indicated by CML; AND
- 4.5.2 Property prices to drop 10% from the level at the time the mortgage is approved
- 4.6** The scheme was initially launched through Lloyds Banking Group, however it is anticipated that more mortgage lenders will be invited to join the partnership as it progresses (six are currently on the list). Sector has been in discussions with the FSA approved mortgage lenders in the UK to raise awareness of the scheme. The scheme will operate on a nationwide basis and there will be no restrictions on the type and number of banks who will be entitled to participate (providing they have the necessary authorisation to offer residential mortgages in the UK).
- 4.7** Cabinet has recommended that Council should initially approve £1m (cash backed) of indemnity to support the scheme with a recognised national provider. It should be noted that the scheme with Lloyds does not currently cover new build properties Lloyds may review this in time, other institutions offer this facility. It is further recommended that this is extended up to a maximum of £5m, following a review of the success of the initial £1m indemnity, as follows:
 - 4.7.1 Extending the scheme to cover other lenders as they enter the scheme, providing additional choice locally. Sector are currently in discussion with a number of lenders about entering the scheme, including lending on new build properties;
 - 4.7.2 Increasing the indemnity if the first tranche of funding is exhausted and the scheme has delivered the outcomes required.
 - 4.7.3 Extending the indemnity to £5m does not alter the financial risk profile. Whilst the possible sums payable following default could increase, so does the interest income to cover this.
- 4.8** Sector Treasury Services will undertake an annual audit of the scheme to ensure both parties are fully compliant with the agreement. The Council will agree with the provider a monthly performance report, so that it is able to demonstrate clear links to strategic objectives and also review the performance of the scheme in relation to its investment.

5. Legal position and local eligibility policy

- 5.1** Sector Treasury Services have sought Counsel's opinion on the legal basis for Councils to be able to support this scheme, along with the position regarding state aid. The Council continues to seek advice from its own legal advisers prior to formal adoption of the scheme

5.2 The Housing Act 1985 (as amended) provides the statutory framework for the scheme. The Act allows Local Authorities to “advance money to a person for the purpose of acquiring a house” (section 435 of the act). Section 442 of the act allows a local authority to grant an indemnity to a lender to enable the lender to give the potential buyer a mortgage.

5.3 In order to participate in the scheme on this basis, the Council will need to develop a local policy for scheme eligibility. Resources PDG have been asked to undertake some initial work in this respect once the overall principle of participating has been approved. The key elements of the policy will be to confirm the scheme as being cash backed, the areas of the District to be covered and the size of mortgage to be supported. The PDG may also consider the success factors for decision making on the additional £4m. The Council will then need to incorporate the policy into the local housing strategy and the ¹treasury management policy, which will also need to be approved by Full Council as part of the Major Policy Framework. It is recommended that this is undertaken in time for consideration by Council at the meeting of March 1st 2012. Once the policy is approved, and associated legal agreements completed, the scheme can be launched.

¹ The Council's TM policy has been adapted, and approved by Council, to allow for a LAMs Scheme to be launched should Council choose to make formal on 1 March 2012

6. Differences to Government Scheme

6.1 Following the release of the National Housing Strategy and the government's announcement to provide Mortgage Indemnity Guarantee insurance to enable 95%LTV mortgages on new build it is worth considering how this affects the introduction of the LAMS scheme

6.2 On the face of it the government scheme appears to be similar to LAMS. However, there are some very important differences, and based on the limited detail available on the government scheme so far the main differences are set out in the table below, assuming the new scheme is broadly similar to the existing FirstBuy scheme.

6.3 The government scheme is available for new build only (like FirstBuy) and requires a contribution from developers (like FirstBuy). LAMS is available on any type of property, and there is no complicated system of means testing, referrals and vetting. LAMS is operated on a commercial basis, where the lenders pay the Local authority a premium to off-set defaults.

6.4 Finally, a survey of 3,000 potential first-time buyers by property website Rightmove found 34.1 per cent said that FirstBuy would make no difference to them because they don't want a new property, and 21.8 per cent said it would make no difference because the scheme is not attractive. And the purchase of one new build property will only generate one move in the housing market,

whereas the sale of an existing property will generally create a chain of 4 – 5 transactions.

6.5 Key features and differences between the two schemes (assuming similar to FirstBuy):

FEATURE	GOVERNMENT SCHEME	LAMS
Who?	First and second time buyers with income below £60 000	Any first time buyer
Property?	Designated plots from participating house builders – NEW BUILD PROPERTIES ONLY	ANY property in the LA area
When?	Announced in outline Nov 2011 – could be a year before any completions take place (CLG confirm much work to be done)	LAMS up and running NOW and growing fast
Application process?	Get approval to view from a the regional homebuy agent, view permitted properties, apply for a mortgage, get mortgage offer approved by the regional home buy agent, complete within one month	Apply to any participating lender in the normal way Full stop
State aid issues?	Questions will have to be answered about MIG fee and its adequacy	State aid compliant

7. LOCAL POLICY DETERMINATION

7.1 Some operations policy issues must be discussed and determined in order to have a comprehensive policy document. These will be discussed at the PDG Meeting.

7.2 Key elements for determination are:-

7.2.1 The area of District to be covered.

- Data enclosed in the appendices give details of property sales by volume and value for the different areas of the district.
- Options to be considered are whether to be specific about an areas of the district to support (based on a specific need) or to have a scheme that covers the whole of the district.

7.2.2 The size of the individual mortgage to be supported:

- The value of size and type of property across the district varies considerably (see appendices) e.g. Grantham and Stamford. Entry level

properties vary to such a degree that the scheme may have different impacts across the district.

- Options would be to set a limit based on the value of entry level properties or another criteria such as the lowest level of stamp duty (currently £130k). A further option could be to have a different level of support for different areas of the district. However, this may be extremely difficult to administrate and monitor.

7.2.3 The size of the overall indemnity.

- Cabinet have suggested a unified £1m with a further contribution of £4m subject to success criteria and impact. Members should remember that the money will not be 'spent' but put aside with view to receiving a return (much like a Moneymaker Instant).
- Options would be to increase or decrease this amount subject to parameters and limits agreed with the Council's Section 151 Officer.

7.2.4 The preferred partners

- The scheme's currently being used by Authorities who have already launched it in partnership with Lloyds PLC. The Lloyds scheme is limited to existing properties only i.e. not new build. Clearly the council could need a provider with a local presence to ensure maximum coverage and impact.
- The list of providers currently supporting the scheme is growing, however, only Lloyds and the Leeds Building Society have a presence in our area.
- Options would be to limit the scheme to Lloyds initially, or to go with Lloyds and the Leeds Building Society, or perhaps anyone on the selection list to give the widest coverage.

8. OTHER OPTIONS CONSIDERED

To be considered further in policy development

9. RESOURCE IMPLICATIONS

Discussed in main body of the report.

10. RISK AND MITIGATION (INCLUDING HEALTH & SAFETY AND DATA QUALITY)

11. ISSUES ARISING FROM EQUALITY IMPACT ASSESSMENT

12. CRIME AND DISORDER IMPLICATIONS

None

13. COMMENTS OF FINANCIAL SERVICES

The scheme will commit, initially, £1m of the councils funds that would ordinarily be invested. Research tell us that at any one time the Council has in excess of £10m that is always invested in the markets and therefore not required for daily, weekly and monthly funding of services. This would reflect the level of reserves and balances the council carries. At present the Council is recouping 1.58% on longer term deposits, investment rates have seen dramatic falls since the onset of the economic downturn in 2008. The treasury management strategy approved by Council in December 2011 provides the framework for the introduction of the scheme.

14. COMMENTS OF LEGAL AND DEMOCRATIC SERVICES

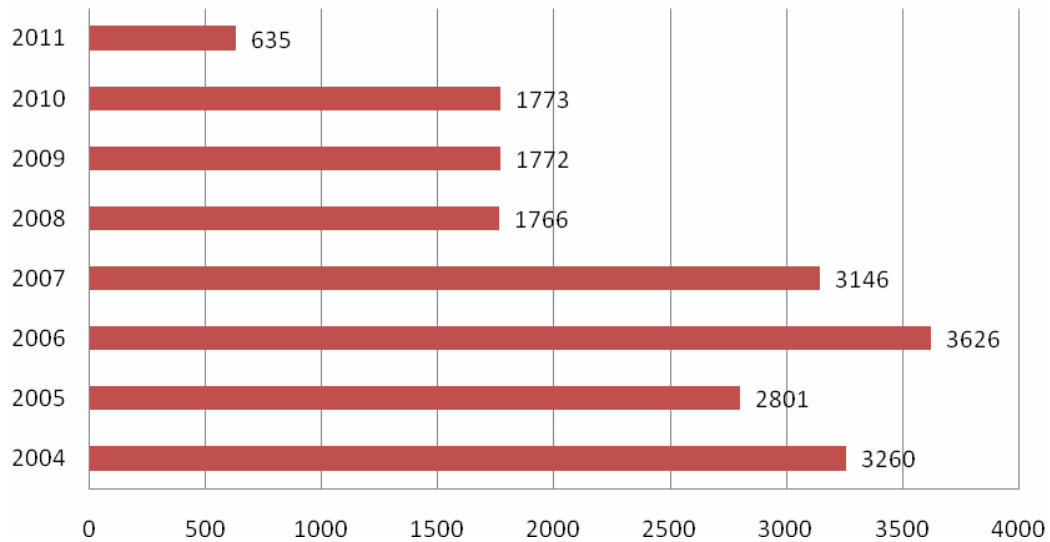
Local authorities have the power to provide the indemnity referred to in this report in accordance with s. 442 of the Housing Act 1985 (as amended). The indemnity in the scheme proposed requires the deposit of security with a bank. Individual indemnities will be required in respect of legality. That legality will depend on the policy created to adopt the scheme, how that policy will contribute to the Council's strategic objectives and priorities, the process for financing the scheme, the eligibility criteria and, generally, how the policy will be implemented. The PDG are asked to consider the options available for such a policy

15. APPENDICES:

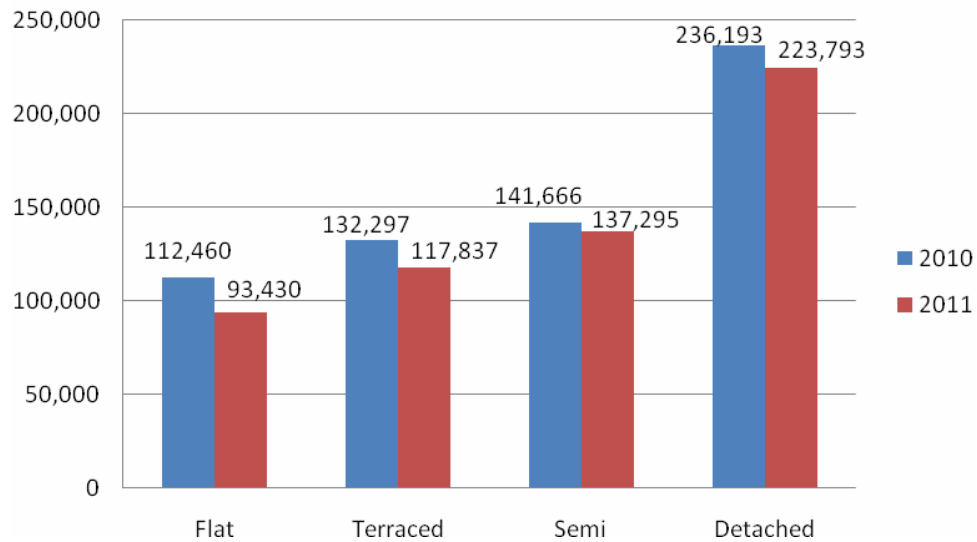
Please see following pages.

Appendix A

Annual Sales Volumes

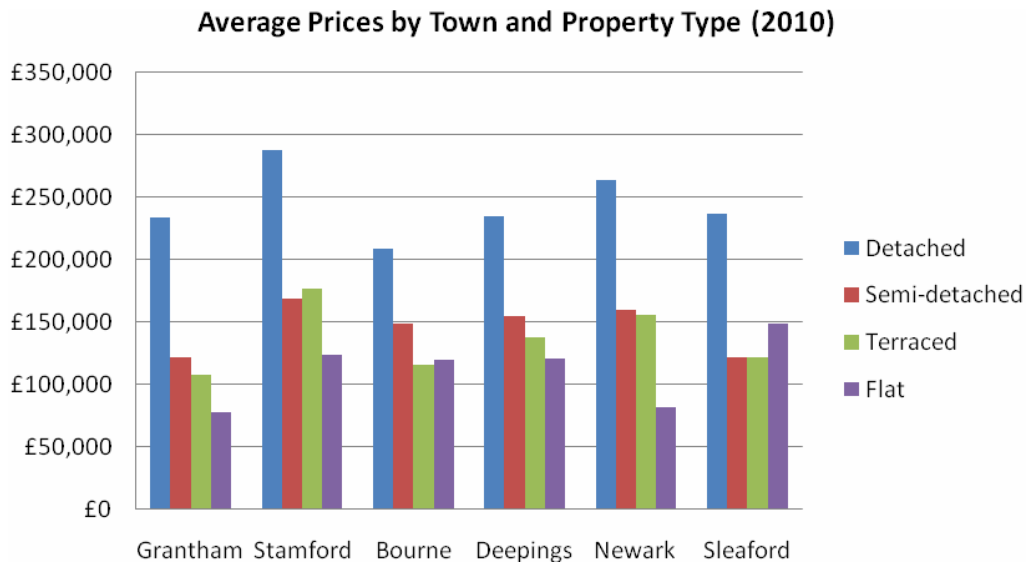


Average Sales by Property Type



Source: Land Registry House Sales (Hi4em)

Appendix B



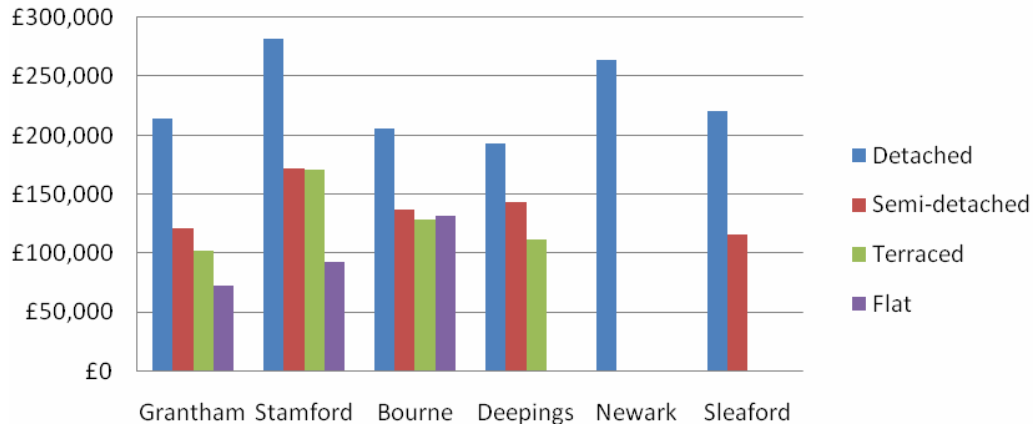
Average House Sale Prices 2010	Detached	Semi-detached	Terraced	Flat
Grantham	£233,526	£121,875	£107,377	£77,493
Stamford	£286,916	£168,677	£176,576	£123,512
Bourne	£208,062	£148,511	£115,388	£119,441
Deepings	£234,062	£154,651	£137,720	£120,750
Newark	£263,335	£159,825	£155,083	£82,000
Sleaford	£235,967	£121,728	£121,500	£148,498

Lower quartile 2010 house prices

Terraced Properties	£94,000
Semi Detached Properties	£110,000

Source: Land Registry House Sales (Hi4em)

Average Prices by Town and Property Type (2011)



Average House Sale Prices 2011	Detached	Semi-detached	Terraced	Flat
Grantham	£213,945	£120,776	£102,042	£72,381
Stamford	£282,344	£171,825	£170,498	£92,192
Bourne	£205,757	£136,274	£128,084	£131,072
Deepings	£192,728	£142,734	£110,899	£61,000*
Newark	£263,941	£155,000*	£120,000*	-
Sleaford	£220,375	£115,750	-	£110,000*

Lower quartile 2011 house prices

Terraced Properties £76,000
 Semi Detached Properties £108,500

Source: Land Registry House Sales (Hi4em)
 *Only one house sold
 For 2011, figures shown are from Jan to June - these are latest available