Provision of Local Authority Debt Facilities to Registered Providers of Social Housing

Background

Many Local Authorities (LAs) are currently considering the benefits of providing debt facilities to Registered Providers (RPs). These loans are primarily used to facilitate area regeneration, in particular new affordable housing, which can provide a significant boost to the local economy.

Such arrangements are particularly attractive to RPs, many of whom, following the banking crisis, are finding it increasingly difficult to raise funds from traditional lenders. Most banks at present only offer 5-year loans, which is a further barrier for RPs who are planning to undertake long-term investments.

The value of loans issued by LAs to RPs ranges from £5million to £60million. The return made by the issuing LA has typically been between 1% and 1.5% of the loan value.

These loans need not necessarily be provided to fund specific projects but can be used to provide finance to facilitate wider regeneration programmes. They are therefore not restricted to developments within the LA area and can be used to stimulate housing investment within the broader region.

Counsel opinion recently obtained from a leading QC specialising in this field confirmed that LAs have the powers to provide such loan facilities, provided that the deals are structured correctly to comply with financial regulations and avoid state aid.

Financial Considerations

The key requirements for LAs are that the loans provide a commercial rate of return and that the RP provides sufficient security to minimise risk. This is achieved by:

- The LA agreeing a facility with the RP that can be drawn down as required over a set timeframe (usually 5 years). It is the margin, not the actual rate that is fixed at the time the facility is contractually agreed, thus protecting the LA from any losses resulting from changes in interest rates. At this point, a one-off Arrangement Fee is paid to the LA.
- When a drawdown is requested, the LA borrows from the Public Works Loan Board (PWLB) at the prevailing rate and then lends on to the RP, usually over a 25 year term. The underlying interest rate will vary according to the PWLB rate at the time each drawdown is made.
- The loan is secured by way of a charge on the RP's properties with the LA having first charge on the secured assets.

Resource Implications

Typically the LA's legal and due diligence costs in relation to setting up and the on-going monitoring of the deal will be borne by the RP. KCL's role has typically encompassed the following:

1. Review proposed contract structure of the Development Facility Agreement.
2. Advice on state aid considerations
3. Legal brief and liaison with Counsel to obtain an Opinion as to the legality of the proposal
4. Review of Treasury Management Strategy and advise on changes required
5. Assistance with key Heads of Terms.
6. Assistance with any Authority approvals (together with external audit)
7. Appointment briefs for legal, financial and technical advisers
8. Assistance with final commercial negotiations to conclude the contract
9. Ongoing monitoring requirements.