

# Cabinet Report



Listening Learning Leading

Report of Strategic Director

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To: CABINET

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## Long term loan to Soha Housing

### Recommendations

- (a) that Cabinet recommends Council to approve the addition of £15,000,000 to the approved capital programme to provide long term funding to Soha Housing for the purpose of providing additional social housing in Oxfordshire;
- (b) that subject to Council approving the addition to the capital programme, Cabinet:
  - (i) agrees to provide a long term loan to Soha Housing for the purpose of providing additional social housing in Oxfordshire, on the terms set out in the report of the strategic director; and
  - (ii) delegates authority to the strategic director to negotiate and agree the final terms of the loan agreement and to enter into the loan agreement and any ancillary documents on behalf of the council.

### Purpose of Report

1. Officers have negotiated the terms of a possible long term loan to Soha that would provide a long term investment income stream to the council whilst giving Soha access to lower cost borrowing to fund social housing schemes locally. This report summarises the arrangement and enables the cabinet to recommend the loan to full council.

### Corporate Objectives

2. The council has a strategic objective of 'meeting housing need' and corporate priorities under that to:

- work with developers to overcome obstacles to development
  - ensure that new developments include a range of different types of affordable housing to meet local needs
3. The council also has a strategic objective of 'effective management of resources' and a corporate priority under that to 'agree prudent and sustainable medium term financial plans and strategy'.

## Background

4. Officers have been reviewing options for investing some of the council's substantial financial balances in the medium-to-long term to contribute to the housing priorities, without adversely impacting on the council's financial standing, security and liquidity. Given the ongoing need for additional rented social housing, officers have approached Soha, the largest provider of rented social accommodation in the district to discuss its needs.
5. Soha is about to go to the financial market to fund its next programme of future development. Soha is interested in borrowing from the council if that provides cheaper finance. Officers have negotiated a loan arrangement that Soha is agreeable to. The funding must be used purely for social housing in Oxfordshire and will therefore have a direct impact on increasing the number of properties available for social rent in and around the district. This report sets out the details of the loan in order for Cabinet to decide if it wishes to recommend it to council.
6. Soha owns and manages around 5,800 properties, all within 1 hours drive of Didcot. They have a substantial development programme that currently exceeds 200 new units per annum. They are recognised as one of the best social landlords in the country and are financially strong. They have a strong commitment to, and record in, meeting housing and community need in South Oxfordshire and the surrounding districts with an emphasis on providing excellent customer service and involving residents. Their objectives, therefore, dovetail with those of the council.
7. Housing officers continue to pursue many other options which contribute to the above strategic objective and priorities. Finance officers continue to discharge the council's medium term financial plan and treasury management strategy, which includes looking for investment opportunities that balance security (risk), return and liquidity.

## Options

8. This loan arrangement is a compromise between the two strategic objectives above (housing and finance), which provides the flexibility to contribute to both. The negotiations which led to the final proposal covered many different aspects of lending including term, interest rate, arrangement fee, security, etc. Therefore many other lending **options** were considered but rejected as being either unacceptable to the council or commercially unacceptable to Soha.
9. The council has no statutory duty to lend to housing associations and can choose not to pursue this lending opportunity, in which case Soha will borrow from the market at commercial rates.
10. If the council chooses not to pursue this option it will make less contribution to its housing objective and will have to rely on other initiatives.

## Financial Implications

11. Under the council's treasury management policy the council can lend up to £20m to any single counterparty. The council regularly lends up to £5m in short term deposits to single counterparties (other councils and financial institutions) and has lent £7m in one instance.
12. This loan to Soha would be the highest value loan ever advanced by the council (£15m) over the longest repayment term (20 years).
13. The advance uses 12.5% of the council's currently available £120m cash balances which would be unavailable for other uses until the loan is repaid after 20 years. This could restrict future capital and revenue plans if remaining balances were to be fully exhausted.
14. In order to be financially attractive to Soha, a preferential fixed rate has been negotiated. Over the 20 year term of this loan it is likely that the council could achieve greater returns from other financial investments. However, this loan represents lower risk, being fully secured against rent-generating property, and makes a major contribution to the council's housing strategic objective.
15. Due to the preferential interest rate being offered by the council, this loan would fall outside the treasury management policy and, instead, would constitute capital expenditure for which council will need to approve an addition to the approved capital programme. This report suggests that the cabinet recommends an addition to the approved capital programme to full council.
16. The details of the loan are commercially sensitive and are summarised in a confidential appendix to this report.

## Legal Implications

17. As this is the first time the council has considered lending to a housing association we appointed Trowers and Hamlins LLP, an external firm of experienced lawyers to advise the council, particularly on the vires (legal authority) and state aid compliance issues.
18. Trowers and Hamlins have confirmed that the council has power under section 24 of the Local Government Act 1988 and in compliance with general consent C under section 25 of that Act to make this loan to Soha to build social homes. Trowers and Hamlin have also confirmed that the loan does not breach State Aid laws because it meets the 'Services in the General Economic Interest' (SGEI) requirement of state aid compliance. Provisions have been included in the loan agreement to ensure continuing compliance throughout the term of the loan.
19. The lawyers have highlighted that the loan terms, whilst being legal and state aid compliant, are less onerous than a commercial loan arrangement and it would be in the council's financial interest to try to improve them. As this arrangement is not intended to compete with a commercial loan and it would make the loan unacceptable to Soha, this advice has not been followed.

## Risks

20. All loans carry some risk. The borrower may default on the loan causing an unexpected cost to the public purse. A fixed interest rate might be exceeded by variable market rates, effectively causing an opportunity cost of lost interest.
21. To mitigate the risk of default, due diligence checks have been performed by Sector, an independent financial consultant, who have advised other councils such as Warrington on its loan to Warrington and Arena Housing Associations. Soha is strong financially and has obtained their Regulator's highest rating for viability for each of the last 8 years. When considered with the almost non-existent level of default in the housing association sector overall, the risk of Soha not meeting interest payments is very low. There is added protection for the council from cross-default provisions in all Soha's loan agreements, which mean we can rely, to a reasonable extent, on other funders' (banks) expertise in monitoring Soha's financial situation on an ongoing basis.
22. Sector's conclusion having completed its due diligence checks is that the financial standing of the borrower represents a relatively low lending risk. Sector had concerns about possible other uses of the loan finance which might be outside the 1988 Act. However the loan agreement specifically limits the purpose to the provision of social housing and Soha has confirmed it will provide regular reports to demonstrate how the council's money is used exclusively for that purpose.
23. To further mitigate the risks, the loan will be secured against properties with strong future rental streams. The total value of property assets, which will be valued based on net rental streams rather than the higher market values and over which the council will have a legal charge, will exceed 100% of the balance of the loan at any point in time, with regular monitoring checks.

## Other implications

24. This proposal uses a significant proportion of the council's balances to benefit local housing, whilst protecting council taxpayers' funds. There is a positive message for both the council and Soha to publicise by way of a joint communications plan. In addition, the council will be publicly recognised on individual specific social housing schemes which are facilitated by the loan.

## Conclusion

25. This loan arrangement makes a positive contribution to meeting the local housing need by enabling our largest local registered social landlord to access cheaper finance which will reduce its administrative overheads, freeing up more of its resources for housing schemes. The council will receive public recognition as funder of the resulting schemes. This is a loan rather than a grant and therefore the balances will be repaid in due course. Whilst the council could make a higher financial return from other unsecured investments which would represent higher risk, the negotiated interest rate on this loan provides a good return for lower risk, secured on housing assets.

## Background Papers

- None