

AGENDA ITEM

REPORT TO CABINET

4 OCTOBER 2012

**REPORT OF CORPORATE
MANAGEMENT TEAM**

CABINET DECISION

**Corporate Management and Finance – Lead Cabinet Member – Councillor Harrington
Housing & Community Safety – Lead Cabinet Member - Councillor Nelson**

LOCAL AUTHORITY MORTGAGE SCHEME

1. Summary

To consider the introduction of a mortgage assistance scheme for First Time buyers.

2. Recommendations

1. Adopt the Local Authority Mortgage Scheme in accordance with the outline provided within this report.
2. Approve the following local criteria that officers should seek to have incorporated in the final agreement:
 - a) All post codes in Stockton-on-Tees Borough Council's area of coverage should be included.
 - b) The initial deposit and indemnity limit should be £1million.
 - c) That the maximum loan guarantee be set initially at £20,000, being 20% of a maximum purchase price of £100,000.
3. Delegate the finalisation of the documentation and any ancillary matters to Corporate Director of Resources and Head of Legal Services, in consultation with the Cabinet Members for Corporate Management and Finance and Housing and Community Safety.

3. Reasons for recommendations/decisions

Due to the present economic climate building societies and banks have become very risk averse and as a consequence have reduced the amount of lending they do to each other and to home buyers. As a result of this many mortgage applicants who previously would have been seen as being a 'good' credit risk can no longer enter the housing market.

Under the proposed scheme if a potential buyer meets the strict credit criteria applied by the lender and meets the criteria set out by the Council to qualify for a mortgage, the Council will provide a top-up guarantee to the value of the difference between the typical loan to value (i.e. 75%) and a 95% loan to value mortgage. The potential buyer will thereby obtain a 95% mortgage on the same terms as a 75% mortgage, but without the need to provide the substantial deposit usually required.

The lack of mortgage availability is a national issue and one which is adversely affecting the

delivery of the Council's priority of delivering substantial and sustainable growth at a local level.

4. Members Interests

Members (including co-opted Members) should consider whether they have a personal interest in any item, as defined in **paragraphs 9 and 11** of the Council's code of conduct and, if so, declare the existence and nature of that interest in accordance with and/or taking account of **paragraphs 12 - 17** of the code.

Where a Member regards him/herself as having a personal interest, as described in **paragraph 16** of the code, in any business of the Council he/she must then, **in accordance with paragraph 18** of the code, consider whether that interest is one which a member of the public, with knowledge of the relevant facts, would reasonably regard as so significant that it is likely to prejudice the Member's judgement of the public interest and the business:-

- affects the members financial position or the financial position of a person or body described in **paragraph 17** of the code, or
- relates to the determining of any approval, consent, licence, permission or registration in relation to the member or any person or body described in **paragraph 17** of the code.

A Member with a personal interest, as described in **paragraph 18** of the code, may attend the meeting but must not take part in the consideration and voting upon the relevant item of business. However, a member with such an interest may make representations, answer questions or give evidence relating to that business before the business is considered or voted on, provided the public are also allowed to attend the meeting for the same purpose whether under a statutory right or otherwise (**paragraph 19** of the code)

Members may participate in any discussion and vote on a matter in which they have an interest, as described in **paragraph 18** of the code, where that interest relates to functions of the Council detailed in **paragraph 20** of the code.

Disclosable Pecuniary Interests

It is a criminal offence for a member to participate in any discussion or vote on a matter in which he/she has a disclosable pecuniary interest (and where an appropriate dispensation has not been granted) **paragraph 21** of the code.

Members are required to comply with any procedural rule adopted by the Council which requires a member to leave the meeting room whilst the meeting is discussing a matter in which that member has a disclosable pecuniary interest (**paragraph 22** of the code).

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SUMMARY

To consider the introduction of a mortgage assistance scheme for First Time buyers.

RECOMMENDATIONS

1. Adopt the Local Authority Mortgage Scheme (LAMS) in accordance with the outline provided within this report.
2. Approve the following local criteria that officers should seek to have incorporated in the final agreement:
 - a. All post codes in Stockton-on-Tees Borough Council's area of coverage should be included.
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 - c. That the maximum loan guarantee be set initially at £20,000, being 20% of a maximum purchase price of £100,000.
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DETAIL

The Current Situation

1. Most mortgage lenders are typically prepared to lend a maximum of 75% - 80% loan to value (LTV), even if the applicant can afford a 95% mortgage. This means the applicant requires a substantial deposit, e.g. a first time buyer purchasing a property valued at £100,000 would have to provide a deposit in the region of £25,000. Indications are that many first time home-buyers do not have the funds needed for the deposit and are therefore unable to enter the housing market.
2. As a result of the current economic environment, uncertainty in the housing market and the difficulties in obtaining an affordable mortgage, many potential home-buyers may remain in social/affordable housing units, continue to live with parents or have limited option but to rent in the private sector.
3. In order to address these issues and help stimulate the local housing market a number of Local Authorities have considered issuing mortgages.

4. Rather than entering into the residential mortgage market themselves, Local Authorities have explored the possibility of entering into a partnership with residential mortgage lenders, with the remit of minimising the financial impact on the Local Authority, and at the same time taking advantage of the expertise already available from existing mortgage providers.

The initial Local Authority Mortgage Scheme Pilot

5. In September 2009, Sector Treasury Services (the Council's Treasury Advisors) set up a pilot scheme to assess the viability of a new Local Authority Mortgage Scheme (LAMS), including the legal and accounting issues surrounding a financial indemnity of this nature. 11 Local Authorities initially sponsored the pilot scheme.
6. The remit of the pilot scheme included initial discussions with a range of residential mortgage lenders, with a view to securing options for funding the scheme. Initial discussions with potential funders / partners revealed that due to the high level of set up costs, funders would only be interested in a large national scheme rather than separate arrangements with individual Local Authorities. It was also considered appropriate to discuss the proposed scheme with the Council of Mortgage Lenders (CML). Early discussion with the CML has secured support for a standard national scheme but with some local criteria.
7. Following the successful completion of the pilot scheme, this report outlines the proposed scheme where the Council can provide targeted help to potential home-buyers to enable them to obtain a mortgage. The scheme is a private sector initiative, i.e. not linked to the Right to Buy Mortgage scheme previously provided by Local Authorities. As at 1st September 2012, 27 local authorities have implemented the scheme and over 600 mortgages have been secured totalling over £66m. Another 30 local authorities are expected to launch the scheme in this financial year.

The Local Authority Mortgage Scheme (LAMS)

8. LAMS 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. Under the scheme, each Local Authority will be able to specify the qualifying characteristics for those who should qualify for a mortgage under the LAM scheme. The criteria are driven by local housing needs surveys and housing strategies although the scheme itself is standardised as much as possible.
9. 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) (i.e. 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.
10. It should be stressed that the scheme **does not** promote reckless lending, it is essential that the applicants meet the standard lending criteria as set out by the lender, and that the higher LTV mortgage is affordable. The Council has no role in selecting mortgage applicants; it would merely advertise the scheme.
11. The indemnity will be in place for a fixed 5 year period for each mortgage granted under the scheme, which may be extended for a further 2 years if a mortgage were to be in arrears in the last 6 months of the initial 5 year period.

12. The indemnity would only be called upon if a loss is crystallised by the lender. By way of example, a property valued at £100,000, with a 95% mortgage would have a Local Authority indemnity of £20,000. If the property was subsequently sold for £70,000, £25,000 less than the mortgage, then the full value of the £20,000 indemnity would be requested by the lender. If the property was sold at £90,000, £5,000 less than the mortgage, then only £5,000 would be requested from the Local Authority. If arrears were outstanding on the mortgage account the lender would also request this sum from the Local Authority but the overall sum payable would be limited to the total indemnity.
13. It is anticipated that the Council will set a maximum annual limit for indemnities offered, either in total or for the forthcoming year. The indemnity could be either unfunded or in the form of a cash deposit, depending on the requirements of the lender.
14. Whilst some schemes could be unfunded the majority will require a cash deposit from the Council. With a cash deposit the Local Authority is required to place a 5-year deposit at the start of the scheme 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. It should be noted that the first, and major, lender to participate as a partner in this scheme requires a cash deposit based indemnity.
15. The guarantee would only be called upon if a loss is crystallised by the lender. 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.
16. For both types of indemnity, and assuming no default by the buyer, the indemnity liability would terminate on the earliest of the end of the agreed indemnity period (i.e. 5 years) or an early repayment of the mortgage. In the case of a cash-backed indemnity, the fixed-term deposit would be repaid to the Local Authority at the date of maturity, plus interest due. In the Lloyds draft agreement, there is a provision for an extended indemnity period of 7 years where the borrower has been in arrears by more than 3 monthly payments at any time during the last 6 months of the 5 year initial indemnity period.

Local Criteria

17. The scheme would be run in partnership with either one or more national lenders. At present there are two major national lenders, Lloyds TSB Bank plc and Leeds Building Society, and a small number of regional lenders. The general nature of the assistance provided has already been agreed:
 - a. Each borrower in relation to the mortgage is a first time buyer (or in the case of joint borrowers at least one of them is a first time buyer) in accordance with the bank's standard criteria for determining eligibility for first time buyers.
 - b. The loan is for an amount up to a standard financial limit specified by the Council.
 - c. It will be available to purchase a property in the post code area that the Council determines, which means applications can come from anywhere in the UK.
18. Lloyds TSB Bank will not provide mortgages under this scheme for new build or shared ownership/shared equity properties. Other lenders may be able to provide this option, so this could potentially be an option in the future once more lenders join the scheme. Members are

asked to note that there are other schemes available which provide support for first buyers wanting to access new build properties, these include the Government backed “NewBuy” and “FirstBuy” schemes. However there are no similar schemes for first time buyers wanted to access a ‘resale’ property.

19. It is not available for buy to let mortgages.
20. All applicants will be subject to the bank’s normal affordability limits and credit checks.
21. The Council determine the value of the overall indemnity facility that the bank can access for Stockton, the bigger the value, the more mortgages they will be able to provide. The Council can top up that facility but cannot withdraw funds for at least 5 years. The facility would be used up on a first come first served basis. When the facility is used up, the bank would stop allocating mortgages under the scheme in Stockton.
22. It is recommended that the initial deposit and indemnity limit should be £1million, which should be sufficient to support between 50 and 75 mortgages, with a cap on the maximum loan value of £100,000.
23. It is possible to restrict the scheme to a single postcode, however there does not appear to be justification for this Stockton and as such it is recommended that all post codes in the borough should be included, therefore supporting an active housing market across the Borough.

Scheme Monitoring

24. Once the parameters have been agreed, the mortgage lender should manage the operational side of the scheme without any direct input from the council. Sector Treasury Services will undertake an annual audit of the scheme to ensure both parties are fully compliant with the agreement. It should be noted that they do receive a commission on each loan from the lender.
25. Due to the changing environment, further legal and / or accounting advice may be required during the life of the LAMS. To ensure consistency, it is anticipated that Sector Treasury Services Ltd will obtain updated advice on behalf of participating authorities. Any additional fees incurred in this respect will be agreed with all parties in advance.

Lenders

26. There are only a limited number of lenders in the market at present. The major lender is the Lloyds TSB group. So far eight Building Societies have signed up to the scheme; of these six are only offering services to they own area of operation. It is hoped that a North East based lender will join the scheme in the next few months. The two Building Societies that are offering the scheme nationally are:
 - a. Leeds Building Society – will lend nationally through branches and call centres. Will require a cash deposit indemnity of a minimum of £0.5 million and support new and existing properties.
 - b. Teachers Building Society - will lend nationally with the unfunded indemnity scheme.

Timescales & Delegations

27. An agreement will need to be made with one or more lenders and finance arranged. To minimise delays delegated authority is sought to negotiate and finalise the agreements to the Corporate Director of Resources and the Head of Legal Services.

Conclusions

28. LAMS is designed to help increase the number of first time buyers entering the 'lower' (affordable) end of the housing. It will help our wider local housing market through 'knock on' sales and thereby the local economy.
29. At the present time the Council actively supports first time buyers to access the housing market via Time2Buy (the consortium delivering FirstBuy across the Tees Valley and Durham area) and through our Homeownership Register (matching potential applicants with affordable housing delivered through S106 agreements on private housing developments). The introduction of LAMS would provide another 'tool' to actively support potential homeowners.
30. The scheme will utilise a £1m of Council resources and will enable 50+ first time buyers to enter the housing market and generate a return on this investment of approximately 4% per annum.

FINANCIAL IMPLICATIONS

31. With the major lending institution currently involved (Lloyds) the Council would provide a lump sum, invested for 5 years, at a rate of interest of approximately 4% per annum. It is possible that there will be further investment period of up to 2 years where a borrower is behind with repayments. If there is a default on a loan the lender will call in the Council's guarantee for that loan.
32. The £1m required would be financed from within the Council's existing funds.

LEGAL IMPLICATIONS

33. There are a number of contractual issues to conclude before the scheme can go live. Lenders require legal documents to be signed by the authority: the indemnity deed, a deposit agreement and any other relevant documents, the monitoring officer's opinion, and Council indemnity for the monitoring officer's opinion.
34. Sector Treasury Services have set out the legislative framework that would give a Local Authority in England, Wales and Scotland the power to implement the Scheme. The Council would use powers in the Housing Act 1985. Section 435 allows a local authority to "advance money to a person for the purpose of acquiring a house". 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; sub section 442(1) states that "a local authority may enter into an agreement with a person or body making an advance on the security of a house, whereby, in the event of default by the mortgagor, the authority binds itself to indemnify the mortgagee in respect of the whole or part of the mortgagor's outstanding indebtedness". Subsection 442(1A) requires that the advance has to be for a specified purpose. These purposes include: acquiring a house, constructing a house, and converting another building into a house. Sector has also taken advice on the State Aid all of which has been shared with the Council.

RISK ASSESSMENT

35. There is a risk attached to the provision of guarantees and indemnities:

- a. Applicant eligibility and affordability - lenders will ensure the mortgage is affordable and potential buyers meet the criteria.
- b. Costs incurred in the event of the guarantee being called. Given the checks in place the risks should be low but this would result in a call on the Council's deposit which would effectively reduce the level of return on investment.

SUSTAINABLE COMMUNITY STRATEGY IMPLICATIONS

36. The provision of the guarantee should increase the accessibility of mortgages to those who would not otherwise be able to afford them, and support the Council's aim of rejuvenating our local housing market. As such the introduction of LAMS will support the Sustainable Community Plan Key themes of Economic Regeneration and Transport and Environment and Housing.

EQUALITIES IMPACT ASSESSMENT

37. An Equality Impact Assessment has been drafted in consultation with the Diversity Team. An action plan has been developed and will be implemented prior to the implementation of this project.

CONSULTATION INCLUDING WARD/COUNCILLORS

37. The options outlined in the report will be subject to full consultation with Ward Councillors and Community Groups.

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Background Papers

None

Education Related

No

Ward(s) and Ward Councillors:

All

Property

None