



# COTSWOLD DISTRICT COUNCIL

Council name	<b>COTSWOLD DISTRICT COUNCIL</b>
Name and date of Committee	<b>AUDIT COMMITTEE - 30 July 2020</b>
Report Number	<b>AGENDA ITEM (18)</b>
Subject	<b>PUBLIC WORKS LOAN BOARD: FUTURE LENDING TERMS CONSULTATION RESPONSE</b>
Wards affected	<b>N/A</b>
Accountable member	Cllr. Mike Evely - Deputy Leader and Cabinet Member for Finance Email: <a href="mailto:mike.evely@cotswold.gov.uk">mike.evely@cotswold.gov.uk</a>
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Summary/Purpose	To present the Audit Committee with the details of a consultation from HM Treasury and a draft response from the Council. The Audit Committee have the opportunity to consider the draft response and to provide input to the Deputy Leader and Cabinet Member for Finance.
Annexes	Annex A - HM Treasury Public Works Loan Board: future lending terms consultation document
Recommendation/s	a) For Members to consider the draft response to the consultation document. b) To propose any amendments to the draft response arising from (a) for consideration by the Deputy Leader and Cabinet Member for Finance.
Corporate priorities	Priority - Ensure that all services delivered by the council are delivered to the highest standard Principle - Value for money - we will use the council's resources wisely, but will invest in the fabric and future of the district
Key Decision	NO
Exempt	NO
Consultees/ Consultation	Not applicable.

## 1. BACKGROUND

- 1.1. HM Treasury is currently seeking responses to a consultation on future lending terms for the Public Works Loan Board. This report sets out the key points from the consultation document and a draft Council response to the consultation questions. The consultation closes on 31<sup>st</sup> July 2020.

### Key points - extracted from the consultation document

- 1.2. The aim of the consultation is stated as *“to develop a proportionate and equitable way to prevent local authorities from using PWLB loans to buy commercial assets primarily for yield, without impeding their ability to pursue service delivery, housing, and regeneration under the prudential regime as they do now.”*
- 1.3. The government proposes:
- a. requiring local authorities that wish to access loans through the PWLB to confirm that they do not plan to buy investment assets primarily for yield.
  - b. publishing guidance defining the activity that the PWLB will no longer support, with clear protections for service delivery, regeneration, housing, and the refinancing of existing debt.
  - c. standardising the information currently gathered through the application process for the PWLB Certainty Rate and using this as the primary way to confirm with LAs that their plans conform with the guidance.
- 1.4. Local authorities that wish to buy investment assets primarily for yield would remain free to do so but would not be able to take out new loans from the PWLB in the year in which they have bought the asset.
- 1.5. The government is supportive of local authorities using commercial approaches to deliver public services efficiently or to protect cash balances from the effects of inflation. But local authorities should not enter into financial arrangements which serve no direct policy or treasury management purpose.

### Proposed changes to PWLB lending terms

- 1.6. The government proposes ending access to the PWLB for local authorities that wish to buy commercial assets primarily for yield. Local authorities that wish to buy commercial assets primarily for yield would remain free to do so but would not be able to take out new loans from the PWLB in that financial year.
- 1.7. In order to avoid inadvertently capturing service delivery, housing, regeneration, or the refinancing of existing debt in this prohibition, the government would ask each local authority that wishes to borrow from the PWLB to provide a high-level outline of their capital plan for the year or years ahead, including an assurance from the statutory finance director (s151 Officer) that the local authority is not borrowing in advance of need and does not intend to buy commercial assets primarily for yield.
- 1.8. From work with the sector to date, the government does not think it is possible to meaningfully link particular financing components to specific projects, on the basis that local authorities fund their capital plans as a whole rather than on a project-by-project basis. The government therefore thinks that the restriction of access to new PWLB loans would have to apply if a local authority was planning a debt-for-yield scheme anywhere in their capital plan, including through a local authority-owned

company or a joint venture, regardless of whether their planned PWLB borrowing is notionally tied to that project or to a different project.

- 1.9. If a local authority borrowed from the PWLB and was subsequently found to have pursued a debt-for-yield scheme despite the assurances given through the application process, HM Treasury would reserve the right to require loans in that year to be repaid on demand, subject to the existing early repayment penalties.
- 1.10. The government does not propose any changes to the PWLB lending arrangements for smaller local authorities (parishes, town and community councils, and drainage boards).
- 1.11. The government proposes asking each local authority that wishes to borrow from the PWLB to submit a high-level description of their capital expenditure and financing plans for the year or years ahead, including their expected use of the PWLB. Local authorities would be able to revise these plans in year as required. The government proposes asking how much the local authority would spend in a set of categories, which would be developed through the consultation. Four categories are proposed: **service delivery, housing, regeneration, and refinancing**. Local authorities would be asked to provide a short description of the main projects in each of these areas – for example, ‘installing LED street lighting - £3m’.
- 1.12. PWLB would continue to support spend in all four of the categories. However, investment assets bought primarily for yield would no longer be supported.
- 1.13. Housing would be activity normally captured in the Housing Revenue Account and General Fund housing services, or housing delivered through a local authority housing company. The government suggests that this should be separated out from the rest of ‘service spending’ because the relative concentration of cross-subsidy and other innovative financing arrangements in these areas means there could be more projects that have characteristics of the unsupported activity. However, access to the PWLB would in principle be allowed for land release, housing delivery, or subsidising affordable housing.
- 1.14. Regeneration projects would usually have one or more of the following characteristics:
  - a. the project is addressing an economic or social market failure by providing services, facilities, or other amenities that are of value to local people and would not otherwise be provided by the private sector.
  - b. the project prevents a negative outcome, including through buying and conserving assets of community value that would otherwise fall into disrepair.
  - c. the local authority is making a significant investment in the asset beyond the purchase price: developing the assets to improve them and/or change their use, or otherwise making a significant financial investment.
  - d. the project involves or generates significant additional activity that would not otherwise happen without the local authority’s intervention, creating jobs and/or social or economic value.
  - e. while some parts of the project may generate rental income, these rents are recycled within the project or applied to related projects with similar objectives, rather than being applied to wider services.

- 1.15.** Investment assets bought primarily for yield would usually have one or more of the following characteristics:
- a. buying land or existing buildings to let out at market rate.
  - b. buying land or buildings which were previously operated on a commercial basis which is then continued by the local authority without any additional investment or modification.
  - c. buying land or existing buildings other than housing which generate income and are intended to be held indefinitely, rather than until the achievement of some meaningful trigger such as the completion of land assembly.
- 1.16.** The proposals in the consultation would continue to allow local authorities to invest capital outside of their area for service delivery, housing, or regeneration, where there is an economic or social rationale. The prohibition on debt-for-yield would apply inside and outside the LA's area.
- 1.17.** The government would also ask for an assurance from the finance director that the local authority is not borrowing in advance of need and does not intend to buy commercial assets primarily for yield. When applying for a new loan, the local authority would confirm that the plans they have most recently submitted remain current and that these assurances remain valid.
- 1.18.** The government fully supports any local authority's use of commercial structures to advance core objectives of service delivery, housing and regeneration. The aim of this consultation is to address the relatively narrow subset of capital spending in which local authorities use PWLB loans to buy investment assets primarily for yield.
- 1.19.** The government is aiming to develop a definition of debt-for-yield activity that:
- a. does not inflexibly rule out service delivery, housing, or regeneration.
  - b. is simple to interpret, so that LAs can confidently determine if a proposed scheme is eligible for PWLB support.
  - c. does not generate a disproportionate administrative burden for local authorities or central government.
  - d. cannot be circumvented by restructuring or disguising activity.
- 1.20.** Local authorities could in theory borrow privately in one year to support investment in an asset that the PWLB would not support, but then refinance this debt in a future year from the PWLB. This is outside of the intended use of the PWLB and is not something local authorities should deliberately do.
- 1.21.** If an LA wishes to on-lend money to deliver objectives in an innovative way, the government would expect that spending to be reported in the most appropriate category (service spending, housing, regeneration, and refinancing) based on the eventual use of the money. The changes set out are not intended to affect normal treasury management practices.

Consultation questions and draft responses

- 1.22. **Q1: Do you use the PWLB to support treasury management, for example by refinancing existing debt, or to externalise internal borrowing?**
- 1.23. The Council is currently debt free and therefore is not using PWLB. In the past, the Council has fully funded its capital expenditure and is therefore not using internal or external borrowing. However, the Council's Capital Strategy identifies that external borrowing will be required over the medium term to finance the Capital Programme.
- 1.24. **Q2: How far do the lending terms of the PWLB affect the terms offered by private lenders?**
- 1.25. ARLINGCLOSE RESPONSE TO FEED IN HERE
- 1.26. **Q3: Are there any other effects or uses of the PWLB beyond those described here?**
- 1.27. The Council's Capital Programme includes provision for capital grants for investment in community projects, for example, investment in village halls. The Community Projects Fund scheme is conditional upon the community raising funds for the project and therefore bringing inward investment in to the district.
- 1.28. **Q4: Do you think the proposal described in paragraphs 1.24 to 1.28 would be effective in achieving the aim set out in paragraph 1.22?**
- 1.29. Annex A sets out some examples of recent projects and whether or not PWLB loans would be available for each project. However, the wording in "Proposed changes to PWLB lending terms" does not reflect the detail contained in the example projects.
- 1.30. Regeneration schemes will often be a mix of policy objectives such as: improvements to the public realm, housing, economic development, employment opportunities. One element of the regeneration scheme could be producing an income to the Council which is supporting funding for other community benefits, such as enabling the provision of social housing.
- 1.31. Local authorities usually step in to fill the gap where developers fail to deliver due to the degree of risk or insufficient yield. Restricting access to PWLB loans due to the fact that one element of the regeneration scheme could be considered to be a debt for yield scheme could make the whole scheme unviable for the local authority, assuming that lending at or below PWLB rates is not available from other bodies.
- 1.32. **Q5: Do you agree with the conclusion in paragraph 1.26 that LAs finance their capital requirement in the round, and that it is not therefore possible to meaningfully link PWLB borrowing to specific spending?**
- 1.33. For Cotswold District Council this is not an issue as the Council is debt free. The Capital Programme identifies each capital project and the associated funding source or borrowing requirement.
- 1.34. **Q6: If you answered 'no' to question 5, do you have an alternative suggestion?**
- 1.35. While it will not be possible for Councils to retrospectively identify funding sources for previous capital expenditure, it may be possible in the forward looking Capital Strategy for Councils to identify funding sources for elements of the Capital Programme.
- 1.36. **Q7: Do you agree that the approach set out in paragraph 1.27 is a reasonable approach to the situation in which an LA borrowed from the PWLB and was**

**subsequently found to have pursued a debt-for-yield scheme despite the assurances given through the application process? If not, how would you recommend that the government addresses this issue?**

- 1.37. This could cause a Council to have an immediate problem with cashflow. Alternatively, HMT could notify the Ministry of Housing, Communities and Local Government of the situation and request that the Secretary of State investigates the matter and takes appropriate action.
- 1.38. **Q8: Do you think that the proposal set out in paragraphs 1.24 to 1.28 would limit your ability to effectively manage your existing investment portfolio in a year in which you still wish to access PWLB borrowing for 'accepted' purposes?**
- 1.39. No, subject to the Council's response to Q4 being adequately addressed.
- 1.40. **Q9: Do you have a view on when in the calendar or financial year this new system should be introduced?**
- 1.41. 1<sup>st</sup> April.
- 1.42. **Q10: Do you agree with the proposal in paragraph 1.29 that these new lending terms should apply uniformly to larger LAs in England, Scotland, and Wales?**
- 1.43. Yes
- 1.44. **Q11: Do you agree with the assessment in paragraph 1.30 that it is not necessary to change the arrangement for smaller authorities?**
- 1.45. Yes as smaller authorities already have additional scrutiny requirements such as seeking approval from the Secretary of State.
- 1.46. **Q12: The government proposes that you submit your plans for the year or years ahead. Over what period could you provide meaningful plans?**
- 1.47. The Council is currently preparing a Medium Term Financial Strategy which will cover the current financial year and the following three financial years, in line with the new Spending Review period.
- 1.48. **Q13: This proposal would also require a short description of the projects in each spending area as set out in paragraph 1.34 to improve the government's understanding of how the PWLB is used, but without putting an unreasonable reporting requirement on LAs. What level of granularity would give this understanding? For example: projects covering 75% of spending? Anything over £5 million per year? Etc.**
- 1.49. Cotswold District Council would be able to provide a detailed breakdown for each category as the Capital Programme is built up from individual projects with the funding source for each project identified.
- 1.50. **Q14: Do you agree with the approach in paragraph 1.38 that the section 151 officer of the applicant authority should assess if the capital plan is eligible for PWLB access, or would it be more suitable for another body to do this?**
- 1.51. Agree that the section 151 officer is best placed to make this judgement.
- 1.52. **Q15: Would you as an s151 officer feel confident categorising spending into the categories proposed here? If not, what would you propose instead?**
- 1.53. Yes

- 1.54. Q16: Would these proposals affect the ability of LAs to pursue innovative financing schemes in service delivery, housing, or regeneration?**
- 1.55.** The Council proposes the removal of the text at 1.46.c. *“buying land or existing buildings other than housing which generate income and are intended to be held indefinitely, rather than until the achievement of some meaningful trigger such as the completion of land assembly”*.
- 1.56.** There may be elements of a regeneration scheme where these circumstances are unavoidable.
- 1.57. Q17: Are there specific examples of out-of-area capital spending for service delivery, housing, or regeneration that support policy aims?**
- 1.58.** Yes, development of strategic sites can benefit neighbouring authorities and a joint investment approach helps to spread risk whilst supporting priorities across the authorities. For example, investment in projects which contribute towards addressing the climate change emergency can support communities across multiple local authority areas.
- 1.59.** Spend in the wider geographical area, for example across Gloucestershire, where the LEP, district councils and county council collaborate together and the economic and service benefits are for the wider geographic area.
- 1.60. Q18: Would these proposals affect your ability to refinance existing debt?**
- 1.61.** No, as we are debt free.
- 1.62. Q19: Would these proposals affect your ability to undertake normal treasury management strategies? If so, how, and how might this be avoided?**
- 1.63.** No, the proposals state that treasury management transactions are not impacted.
- 1.64. Q20: Do you have any views about the implications of these proposed changes for people with protected characteristics as defined in section 149 of the Equality Act 2010? What evidence do you have on these matters?**
- 1.65.** No.
- 1.66. Q21: Is there anything that could be done to mitigate any impact identified?**
- 1.67.** Not applicable.
- 1.68. Q22: Is there anything else you would like to add on this issue?**
- 1.69.** No.
- 1.70. Q23: Why did MRP fall as debt rose? Was the 2018-19 increase a one-off, or do you expect MRP to continue growing?**
- 1.71.** Cotswold District Council is debt free, therefore no comment on this question.
- 1.72. Q24: Why do you think the average loan length is increasing?**
- 1.73.** No comment as Cotswold District Council is debt free.
- 1.74. Q25: What impact would changes to the maximum available length of loan, and/or the existing offer of repayment methods, have on your finances?**
- 1.75.** The Council’s Capital Strategy includes the provision for providing registered providers with loans to enable them to increase the provision of affordable or social housing. It is anticipated that any such loan would be based upon PWLB annuity

loans. This enables the Council's PWLB liabilities to be match with repayments from the registered provider and avoids any negative impact upon the Council's revenue account.

- 1.76. The Council would prefer the current flexibility to be maintained.
- 1.77. **Q26: What are the benefits of the existing two-day turnaround time for PWLB loans?**
- 1.78. It provides assurance that the Council has access to funding for capital purposes at short notice and avoids the requirement to liquidate pooled investments crystallising capital losses.
- 1.79. **Q27: What would the impact be of increasing the time between loan application and advance – for example, to three or five working days?**
- 1.80. Limited impact, the Council could access short term funding from the local authority market.
- 1.81. **Q28: How long could the turnaround time be for a PWLB loan before the PWLB becomes less attractive?**
- 1.82. The rate of interest payable is a far more important factor than the turnaround time. A longer turnaround time would be acceptable if the interest rate is lower as a result.
- 1.83. **Q29: Do you have any PWLB debt that would you like to repay early? If so, what is the total value of this debt and at what price/discount would this be viable?**
- 1.84. Not applicable as the Council is debt free.
- 1.85. **Q30: How much PWLB debt would you transfer to other LAs if you could?**
- 1.86. Not applicable as the Council is debt free.
- 1.87. **Q31: If novation were permitted, under what circumstances would you take on debt from another LA rather than taking on new borrowing from the PWLB or another source?**
- 1.88. Only if the debt was at an interest rate which is lower than that available for new loans and if the period of the loan matched the underlying assets being funded.
- 1.89. **Q32: Are there any other barriers to discharging unwanted PWLB debt?**
- 1.90. Not applicable as the Council is debt free.
- 1.91. **Q33: Should HM Treasury introduce a process by which borrowing by an individual authority might be slowed or stopped without affecting PWLB access or terms for other LAs?**
- 1.92. Yes, but only where PWLB requires further information to gain assurance that the borrowing is not for debt for yield purposes.
- 1.93. **Q34: Under what circumstances should this process be applied?**
- 1.94. Only where PWLB requires further information to gain assurance that the borrowing is not for debt for yield purposes.
- 1.95. **Q35: Do you use DMADF currently, and if so, why?**
- 1.96. No, the interest rates are too low and it does not offer good value for money.
- 1.97. **Q36: What would make you increase your use of DMADF?**



- 1.98. A rate of interest which is closer to that available on other instant access products.
- 1.99. **Q37: Does your LA actively consider borrowing from alternative lenders to finance capital investment?**
- 1.100. Yes.
- 1.101. **Q38: If you answered 'yes' to question 37, what are the reasons that would inform your choice to borrow from other providers?**
- 1.102. Lower interest rates.
- 1.103. **Q39: What are the main reasons that you borrow from other LAs and how do these reasons differ to borrowing from the PWLB?**
- 1.104. There is a market for local authority borrowing and this can be cheaper than tying in to PWLB fixed term borrowing.
- 1.105. **Q40: Following this, is there a case for changing the name of the PWLB?**
- 1.106. No comment.

## **2 FINANCIAL IMPLICATIONS**

- 2.1. None.

## **3 LEGAL IMPLICATIONS**

- 3.1. None.

## **4 RISK ASSESSMENT**

- 4.1. None.

## **5 BACKGROUND PAPERS**

- 5.1. The Council approved its Capital Strategy, Investment Strategy and Treasury Management Strategy for 2020/21 on 26 February 2020. These strategic documents set out the Council's Capital Programme and the financing of the Programme, which included a requirement for part of the programme to be financed through external borrowing. The documents are available on Committee Minutes page of the Council website.

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