Response: Public Works Loan Board -Future lending terms consultation

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DISTRICT COUNCILS' NETWORK
BETTER LIVES – STRONGER ECONOMIES

About the District Councils' Network

The District Councils' Network (DCN) is a cross-party member led network of 187 district councils. We are a Special Interest Group of the Local Government Association (LGA), and provides a single voice for district councils within the Local Government Association.

District councils in England deliver 86 out of 137 essential local government services to over 22 million people - 40% of the population - and cover 68% of the country by area.

District councils have a proven track record of building better lives and stronger economies in the areas that they serve. Districts protect and enhance quality of life by safeguarding our environment, promoting public health and leisure, whilst creating attractive places to live, raise families and build a stronger economy.

Response

Impact of Covid-19

While not part of the scope of the consultation, we cannot ignore that the pandemic has had a particularly severe financial impact for district councils. Districts are facing increased costs, additional service pressures, and have seen income from fees and charges decimated overnight. In this context, there is an opportunity for government to give urgent consideration to the role of the PWLB and how it could better support district councils – particularly as we look towards economic recovery where it is district councils that hold the legal levers, the local connections and the place power to drive forward the national economy.

We therefore urge the government to:

- Leave unchanged the current legislation, prudential framework and policy so that councils can borrow from the PWLB for commercial investments. The PWLB could offer a lower rate similar to that permitted for housing schemes, but for regeneration schemes. The Government should implement this automatically and not await the outcome of this review.
- Reform the PWLB to offer short-term, low rate borrowing to support cashflow in times of financial stress.
- Introduce a zero- or low-rate borrowing facility from the PWLB, for revenue or cash flow if required. This would need to be accompanied by a temporary change to capital finance system to allow borrowing for revenue purposes.
- Permit a two-year holiday on Minimum Revenue Provision (MRP), which would provide short-term revenue relief and enable councils to take a longer-term view on debt repayments.
- Government could provide incentives to councils such as a discount on the cost of early repayments on existing debt.

General comments on the consultation proposals

We welcome the intention to lower the rate on all borrowing from the PWLB, but this should not be dependent on introducing restrictions on borrowing.

At a national level, the scale of investments made by districts pale against record UK government levels of borrowing, but these investments make a real difference to our local economies.

Use of the PWLB has enabled districts to invest in the economic and social fabric of their local area – generating or protecting employment, regenerating the public realm, and providing housing. In some instances, investments have been taken out in order to generate yield that can be reinvested to protect local services in the face of central government cuts to funding. Many investments serve multiple purposes, and councils have owned commercial property for many years. It is vital that as we emerge from the Covid-19 crisis, districts maintain the freedom and flexibilities to take these decisions locally – particularly where the private sector may no longer be able to step in.

Before restricting councils' ability to invest, government should ensure the forthcoming Spending Review sets district council finances on a sustainable footing for the future. Government has encouraged districts to become financially self-sufficient, and it should not seek to restrict districts' ability to invest in their local economies and protect services, without first putting in place other measures for them to raise vital income.

Key areas of objection

HMT define the consultation as a specific targeted intervention to address debt for yield for the small number of councils borrowing from the PWLB for this sole purpose. However the impact will be felt across the whole sector, and is disproportionate the issue it seeks to address.

In consultation with district councils, HMT stated there is no intention from central government to stifle councils' ability to invest for yield, provided the PWLB is not used to finance it. However, the proposed restriction on taking out new loans from the PWLB in the year they have bought the asset may have a much wider impact on an individual district's capital investment strategy. This represents an unacceptable restriction imposed by central government on decisions that are matters for councils and their elected leadership.

This restriction could also have the unintended consequence of impeding districts' ability to respond to extreme situations. There are times when councils do need access to loans to support cashflow – removing this could impact councils' ability to act quickly.

The definitions of what will and will no longer be eligible need further clarification: for instance, HMT should clarify that investing in industrial space for the purpose of maintaining/protecting employment space would be permitted.

HMT should clarify that cross-subsidy within larger projects will be permitted – one aspect of a large regeneration programme may be commercial, such as a hotel for instance, and if this supports other aspects of the project, such as new leisure facilities, this is acceptable.

While we disagree with the proposed restrictions, should HM Treasury decide to proceed, the DCN is keen to work with government to develop more detailed guidance. Consultation and engagement with districts have been limited so far, and we urge government to engage more widely before introducing changes.

Specific Consultation question responses:

Some questions are aimed at individual authorities, and we therefore refer you to responses from individual districts for those questions.

Q1: Do you use the PWLB to support treasury management, for example by refinancing existing debt, or to externalise internal borrowing?

Not applicable.

Q2: How far do the lending terms of the PWLB affect the terms offered by private lenders?

There is no evidence that PWLB terms affect the terms of other lenders.

Q3: Are there any other effects or uses of the PWLB beyond those described here?

PWLB has been used in the past in respect of local government funding changes – e.g. the use of PWLB borrowing for Local Authorities who were required to make a one-off payment in 2012 and come out of the former HRA subsidy system and effectively buy their council housing stock.

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?

Restricting PWLB borrowing for non-commercial activity in a year when that Council may also use other funding mechanisms to undertake commercial acquisitions is prohibitive on the whole and represents an unacceptable restriction on local decision making. Any restriction should not mean that LAs cannot access PWLB loans for service delivery perusal, housing or regeneration purposes.

The majority of Local Authorities engaging in debt-for-yield activity, do so to maintain service delivery in the face of diminishing funding and increased expenditure pressures. The effect of restricting PWLB borrowing for non-commercial activity will create tensions in financial strategies.

We agree that the S151 officer is the right role in councils to assess the main objective of the investment and consider which of the four categories is the best fit. However, the proposed assessment by Section 151 Officers will be subjective - what is deemed acceptable by one S151 Officer may not be deemed so by another.

There is no indication in the consultation paper how HM Treasury would determine that a S151 Officer has not made a proper declaration. Would there need to be an audit process to determine this? Auditors may reach different conclusions on similar schemes at different authorities.

To achieve the aim, the proposals should be amended so that LAs can still borrow for service delivery, housing or regeneration purposes through more work to shape the link to financing to specific projects.

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?

Treasury Management decisions are not typically linked to specific capital schemes, though there are examples when borrowing is specifically linked to schemes. For example, see HRA self-financing and PWLB loans taken out to buy councils out of the former HRA subsidy system as an example. Assuming districts design their Treasury Management Strategies in line with their Capital Strategies, districts should reasonably be able to identify future schemes which require borrowing in order to be funded.

Q6: If you answered 'no' to question 5, do you have an alternative suggestion?

Districts should be able to align their balance sheet forecasts to identify future borrowing needs and align to specific projects. However, we appreciate that using other funding means for commercial acquisitions impacts the funding for non-commercial activity.

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?

Immediate repayment of a loan – which may have been deployed very successfully for local benefit for a wide range of issues – could remove the local benefits and cause considerable financial hardship. We would suggest a traffic light system whereby initially the authority would receive a warning and be advised to restructure its plans accordingly.

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

Capital spending on existing commercial property could be viewed as being pursued to increase yield on that property given the subjective interpretation/judgment approach.

Q9: Do you have a view on when in the calendar or financial year this new system should be introduced?

We believe further work is required to scope the proposals before implemented and would welcome the opportunity for further engagement. If restrictions are brought in, authorities should be given as much advance notice as possible, and restrictions should be aligned to financial years to match council planning cycles.

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?

Yes, subject to further work to shape the proposals.

Q11: Do you agree with the assessment in paragraph 1.30 that it is not necessary to change the arrangement for smaller authorities?

Smaller authorities already benefit from unrestricted council tax increases and therefore perversely are less likely to undertake commercial investments yet are more able to afford higher interest charges. If the aim is to prevent commercial investment, this should be applied across all tiers.

Q12: The government proposes that you submit your plans for the year or years ahead. Over what period could you provide meaningful plans?

Please refer to responses from member councils.

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

Please refer to responses from member councils.

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?

The S151 Officer is best placed to make this assessment if the Government goes ahead with its proposal. However, S151 Officers would need to understand in advance the process by which HM Treasury would reach the conclusion covered by paragraph 1.27:

'If 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, HM Treasury would reserve the right to require loans in that year to be repaid'

Who would undertake this assessment, during what time period, subject to what appeal process?

Q15: Would you as an s151 officer feel confident categorising spending into the categories proposed here? If not, what would you propose instead?

Not applicable.

Q16: Would these proposals affect the ability of LAs to pursue innovative financing schemes in service delivery, housing, or regeneration?

Potentially - any local scheme could be open to interpretation by a third party that it was primarily for the purposes of income generation and that regeneration/service delivery was a secondary objective. The overarching purpose of local investment is to help secure and develop the local economy. Local decision-making would therefore be hampered and distorted by the concern that the local decision of the S151 Officer could be overturned by subsequent review, potentially leading to crippling financial penalties. The proposals stifle creative approaches to financial management designed to further the authority's core aims and ambitions.

Q17: Are there specific examples of out-of-area capital spending for service delivery, housing, or regeneration that support policy aims?

Such purchases are explicitly authorised by several Acts of Parliament and therefore we don't support limiting a council's ability to borrow for an acquisition outside its area. The impact of wider economic areas' needs to also be considered.

Q18: Would these proposals affect your ability to refinance existing debt?

Yes, where it was deemed that the PWLB loan was supporting a debt-for-yield scheme or access to PWLB loans was restricted due to there being such a scheme in the forward capital plan, even where it was intended to finance that scheme in part at least from non-PWLB sources, such as internal borrowing.

The proposals could make it more difficult for authorities to refinance existing historical debt.

Q19: Would these proposals affect your ability to undertake normal treasury management strategies? If so, how, and how might this be avoided?

The impact on Treasury Management is unavoidable if every decision whether to access PWLB loans is dependent upon a statement that the Authority has no intention of seeking that loan for the purposes of 'debt-for-yield', which could be subsequently deemed to have been a misleading statement. We do not want to see any retrospective requirements to repay PWLB loans, which would have a completely disruptive impact on councils.

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?

Districts borrow to invest in their local area – whether for economic regeneration, housing, or to support wider service delivery in the face of a decade of reduced funding. Any restriction on borrowing could directly impact on this provision for residents. Given districts provide support especially for the more vulnerable, the main risk that is most likely to occur, and have the most detrimental impact is that described in the consultation document in para 1.53 a. The main positive impact of the proposals is that described in para 1.53 c.

Q21: Is there anything that could be done to mitigate any impact identified?

We ask government to revise the proposals, particularly considering the pandemic, so that PWLB lending is not restricted for service delivery where LAs want to pursue other borrowing for commercial activity.

Q22: Is there anything else you would like to add on this issue?

No.

Q23: Why did MRP fall as debt rose? Was the 2018-19 increase a one-off, or do you expect MRP to continue growing?

Please refer to responses from individual councils.

Q24: Why do you think the average loan length is increasing?

Probably because such competitive rates were available for longer term loans over the last 12 months and fixing a rate for a longer term provides certainty and removes refinancing risk.

Q25: What impact would changes to the maximum available length of loan, and/or the existing offer of repayment methods, have on your finances?

Restricting the maximum available length of a loan would reduce flexibility and restrict an authority's ability to obtain long-term secure financing. This would result in shorter loans and increase exposure to interest rate risk unless there were future guarantees of interest rates obtainable via PWLB on re-financing.

Q26: What are the benefits of the existing two-day turnaround time for PWLB loans?

Effective short-term treasury management decision-making. The ability to put policy decisions into immediate effect. Certainty for sellers that payments will be due very shortly after completion but without having to hold debt for lengthy periods while the transaction is completed.

Q27: What would the impact be of increasing the time between loan application and advance – for example, to three or five working days?

The current two-day turnaround is a key strength of the PWLB, and one that authorities do not want to lose. This would have a detrimental impact on districts' responsiveness and agility.

Q28: How long could the turnaround time be for a PWLB loan before the PWLB becomes less attractive?

Any extension to the current arrangement would be less attractive for LAs.

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?

Not applicable

Q30: How much PWLB debt would you transfer to other LAs if you could?

Not applicable

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?

Not applicable

Q32: Are there any other barriers to discharging unwanted PWLB debt?

Current levels of early repayment penalties are seen as an issue by several councils. If early repayment penalties cannot be withdrawn, then a reasonable low or nil cost solution would be the ability to transfer PWLB debt between local authorities by novation. This would be likely to have the advantage for the PWLB of reducing the amount of new borrowing.

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? Q34: Under what circumstances should this process be applied?

If there are particular concerns regarding a local authority's use of PWLB, it is unreasonable to penalise all local authorities. Local circumstances will dictate levels of borrowing for individual LAs and we do not want to see districts having different levels of access to borrowing. We do not support greater central interference in local decision-making.

The recent intervention whereby HM Treasury increased the PWLB interest rates to slow borrowing penalised those authorities that had intended to borrow for the purposes of regeneration or housing development. The warning system suggested above might be one means of achieving a more targeted intervention, but we do not support the proposal.

Q35: Do you use DMADF currently, and if so, why?

N/A

Q36: What would make you increase your use of DMADF?

N/A

Q37: Does your LA actively consider borrowing from alternative lenders to finance capital investment?

N/A

Q38: If you answered 'yes' to question 37, what are the reasons that would inform your choice to borrow from other providers?

N/A

Q39: What are the main reasons that you borrow from other LAs and how do these reasons differ to borrowing from the PWLB?

N/A

Q40: Following this, is there a case for changing the name of the PWLB?

The current name is well known and well understood by those in the sector, so we cannot see a pressing need for change.