

**Report to** Cabinet  
26 November 2013  
**Report of** Chief finance officer  
**Subject** Local Authority Mortgage Scheme

**Item**

**3**

## KEY DECISION

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### Purpose

To present an outline of the Local Authority Mortgage Scheme (LAMS) and show how it could be implemented in Norwich to help first time house buyers.

### Recommendations

That cabinet:

- 1) approves the implementation of a LAMS in accordance with the outline provided in this report, including the following criteria:
  - a) a total indemnity value of £1 million;
  - b) a maximum loan size of £152,000; and
  - c) the qualifying post codes to be provided to the lender in a schedule to the indemnity deed to include all post codes that fall entirely within the council area; and
- 2) recommends to council the addition of capital expenditure of £1m to the 2013-14 capital programme for the cash deposit to support the indemnity

### Corporate and service priorities

The report helps to meet the corporate priority “Decent housing for all” and the service plan priority to consider options for assisting first-time buyers into owner-occupation contained within the council's housing strategy.

**Financial implications:** These are set out in the body of the report.

**Ward/s:** All Wards

**Cabinet member:** Councillor Waters – Deputy leader and resources

### Contact officers

Caroline Ryba  
Philippa Dransfield

07920 500618  
01603 212562

### Background documents

None

## Report

### Introduction

1. Average local incomes are in the region of £22,000 per annum while an average priced property in Norwich is almost £170,000<sup>1</sup>. This places home ownership beyond the reach of households who do not have existing property equity, financial assistance from family, or a large income. However, there are potential first-time buyers with regular incomes who could afford a mortgage but are unable to save a large deposit. A 25% deposit is often necessary, equal to £40,000 on an average two or three bedroom property for sale at £160,000.
2. The city has a high proportion of young people aged 20 -29 (21.2 %) compared with just 11.9 % in Norfolk and 13.66 % in England<sup>2</sup>. Those aged 20 -29 are more likely to rent privately because they are unable to access mortgage finance to purchase on the open market<sup>3</sup> due to tougher lending criteria following the Mortgage Market Review.
3. Capita Asset Services Treasury Services (Capita Asset Services), the council's treasury management adviser, has set up the Local Authority Mortgage Scheme (LAMS) to assist councils to address this issue. In so doing, a number of other benefits are likely to be achieved, including the freeing up of social / affordable housing units, young couples and families moving out of overcrowded parental homes, and more purchasers for new build properties providing a kick start to house building programmes.

### The scheme

4. The 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. The borrower raises a 5% deposit, the council gives an indemnity for a further 20%, allowing the mortgage lender to advance a 95% mortgage on lower rates more typical of a 75% loan to value (LTV) mortgage. The main lender working with Capita Asset Services is Lloyds bank, although smaller, local lenders have been used by some existing schemes.
5. The Council's indemnity would be backed by a cash deposit with the lender for the duration of the indemnity, which would normally be 5 years. If a mortgage is in arrears during the last 6 months of the 5-year indemnity period, that period is extended to 7 years, by which time the homeowner should have acquired more equity in the property.
6. On the basis that the Council provides an indemnity of £1 million, 30-40 first-time buyers could be helped, assuming that a 20% indemnity equates to £25,000 on a £125,000 property or £32,000 on a £160,000 property.
7. Under the scheme, the council would specify three qualifying criteria; the maximum level of indemnity, the maximum loan size (based on 95% of maximum property valuation) and the qualifying post codes. The lender

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<sup>1</sup> Source BBC news channel – UK House prices January to March 2013

<sup>2</sup> Census 2011

<sup>3</sup> English Housing Survey (Households) 2010-11, DCLG, 2012






would apply their strict credit criteria. If a potential buyer meets all criteria the council would provide the top-up indemnity.


8. The indemnity would only be called upon if a loss is crystallised by the lender. For example, if a property purchased for £150,000 with a mortgage of £142,500 and indemnity of £30,000, is sold at £100,000, net of attributable costs, then the full value of the £30,000 indemnity would be requested by the lender. If the property is sold at £130,000 net of costs, i.e. an actual loss of £12,500 is incurred, £12,500 would be requested from the council. Any loss in excess of the value of the indemnity would be attributable to the lender.
9. Once these parameters have been set, the mortgage lender manages the operational side of the scheme without any direct input from the council. Capita Asset Services Treasury Services undertake an annual audit of the scheme to ensure both parties are fully compliant with the agreement.

## Review of options

### Do nothing

10. The housing market is showing signs of recovery, making the need for intervention less pressing. However, the shortage of housing supply is driving long-term increases in prices and different mortgage products are added and withdrawn on a daily basis. At the time of writing there are mortgages at a maximum Loan to Value (LTV) of 95% available.
11. The table below, taken from Moneyfacts.co.uk on 15 November, shows some of the high LTV mortgages for first-time buyers on the market. Mortgages for 95% LTV are available between 4.3% to 5.8%.

	Rate	APR Cost	Mortgage Type	Period	Max LTV	Redemption
	4.89% reverting to 5.19%	<b>5.3%</b>	Fixed	31/12/2015	95%	To 31/12/2015
Product Fee: Arrangement £100, Booking £250						
	4.99% reverting to 4.00%	<b>4.3%</b>	Fixed	31/03/2016	95%	To 31/03/2016
Product fee: Booking None						
	4.99% reverting to 5.69%	<b>5.8%</b>	Discounted Variable	2 years	95%	1st 2 yrs
Product Fee: Booking £199, Completion £800						
	4.99% reverting to 4.95%	<b>5.2%</b>	Fixed	31/01/2017	95%	1st 3 yrs
Product fee: none						
	5.19% reverting to 5.69%	<b>5.7%</b>	Fixed	31/12/2018	95%	To 31/12/2018
Product Fee: Booking £199, Completion £800						

	5.49% reverting to 4.00%	4.8%	Fixed	31/03/2019	95%	To 31/03/2019
Product fee: none						

12. There are a number of existing government schemes which support purchasers of new build houses. A new scheme was launched on 1 October 2013 (Help to Buy – Mortgage Guarantee) which also covers existing properties. See Appendix A for a summary of the schemes and a comparison with LAMS.

### Launch a Norwich LAMS

13. Launching a local scheme will provide an alternative source of support for local people looking to buy a home for the first time. The council will be able to promote the scheme locally and choose scheme criteria so that it supports the council's housing strategy. LAMS therefore represents an additional mechanism that complements the council's other activities in relation to housing.
14. The key features of the proposed scheme are:
- a) Lender – Lloyds bank, as recommended by Capita Asset Services. Lloyds bank currently run 79% of existing schemes.
  - b) Indemnity - £1m, taken from cash balances, treated as capital expenditure in accordance with accounting guidance supplied by Capita Asset Services.
  - c) Maximum loan value £152,000, reflecting a maximum purchase price of £160,000, to enable the purchase of a two or three bedroom property within the city.
  - d) Eligible postcodes to include all postcodes that fall fully within the city boundaries<sup>4</sup>
15. There are a number of risks that should be considered:
- a) The financial stability of Lloyds bank: Recent years has seen great turmoil for financial institutions and the economic outlook remains uncertain. Lloyds bank has a credit rating of A<sup>5</sup>. The council invests short-term with Lloyds bank in accordance with its investment strategy.
  - b) The council's financial position: Committing £1million from cash balances for five years reduces flexibility and fixes the interest rate that can be earned. Interest rates are predicted to increase during this time.
  - c) Targeting of support to Norwich residents: Eligibility is based on the location of the house being purchased. Therefore support will be provided to both existing Norwich residents, and those looking to move into the city. Conversely, existing residents purchasing outside the boundaries would not be eligible for support.

<sup>4</sup> Postcodes at street level must fall fully within Norwich's boundary, any that straddle district boundaries are ineligible under the terms of the scheme

<sup>5</sup> Rating by Fitch as at 15 November 2013

- d) Take up: As at 31 March 2013, there are 67 schemes in 52 local authority areas. Some local authorities have more than one scheme, i.e. they open another scheme when the first scheme is fully utilised or they have schemes with more than one lender. However, the success of LAMS in Norwich is difficult to predict. Exceptionally high demand may raise the public's expectations, putting pressure on Members to increase the Council's investment and financial risk. It is equally feasible that very few indemnities will be issued.
- e) Repossessions: As yet, no existing schemes have suffered any repossessions, reflecting well on the financial assessments done by the lenders on potential buyers. However, repossession would be in the hands of the lender, although the council could look to provide support to the purchaser, possibly through the provision of financial advice. There would be potential financial and reputational implications of purchaser default.
- f) Accounting treatment: Due to decisions taken by the Welsh Audit Office surrounding the accounting treatment of LAMS and possible audit qualifications, LAMS have closed in Wales. Capita Asset Services have obtained Counsel's opinion which confirms that a court is likely to find that the cash advance is used towards the acquisition of a house by the mortgagor, which will make it capital expenditure under Regulation 25. They have also obtained a separate Counsel opinion on the lawfulness of treating the cash advance as an investment rather than capital, and the second opinion states that Regulation 25 is mandatory, and an authority which accounted for the LAMS cash advance as an investment rather than capital expenditure would be acting unlawfully.

### **Resource implications**

- 16. The £1m indemnity falls to be treated as capital expenditure under regulation 25 of The Local Authorities (Capital Finance and Accounting) (England) Regulations 2003. Therefore this scheme will require full council approval for it to be added to the 2013-14 capital programme.
- 17. The offer from Lloyds requires a 5-year deposit of at least £1m. Annual interest on the deposit, including a 0.7% premium, is currently in the region of 2.4%, therefore a £1m indemnity over the 5 years with Lloyds bank could earn £120,000. This is £10,000 more than that from a typical five year investment (calculated at 2.2%pa<sup>6</sup>).
- 18. Interest received will be placed in an earmarked reserve in case of possible defaults.

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<sup>6</sup> Rate as quoted by Lloyds bank 22 August 2013

## **Legal implications**

19. Capita Asset Services have provided legal documents setting out the legal basis of the scheme and addressing the state aid rules. These have been reviewed for the council by NPLaw, who have confirmed their accuracy.


## APPENDIX A

## Overview of initiatives to assist home buyers

Product	New Buy	Help to Buy * Equity Loan (replaces FirstBuy)	Help to Buy * Mortgage Guarantee	Local Authority Mortgage Scheme *
<b>Characteristics</b>	Started in March 2012	Started in April 2013 and will run for three years	Due to launch in January 2014	Seeking Cabinet approval in October 2013 for launch in November
		Guarantees to support £130 billion worth of mortgages	Subject to final design but could facilitate up to 325,000 mortgages over the next three years	£1 million total indemnity could facilitate in excess of 30 mortgages across the district (£5 million worth of mortgages)
	95% LTV (full ownership)	Equity loan up to 20% of property value provided by government (loan can be repaid at anytime, or when buyer sells the property)	Government backed mortgage guarantee of 15% (LTV between 80-95%)	Cash backed mortgage guarantee of up to 20% provided by local authority (LTV between 75-95%)
		Interest-free loan for five years then a fee of 1.75% is payable which rises annually by Retail Price Index inflation plus 1%	Guarantee lasts for seven years after the mortgage is originated	Guarantee lasts for five years after the mortgage is originated
	First time buyers with family incomes below £60,000	All buyers on any income	All buyers on any income with 5% deposit	First time buyers with 5% deposit
	New build (restricted to specific sites and properties)	New build	Existing & new build	Existing
			Existing homeowners could use the Mortgage Guarantee	

Product	New Buy	Help to Buy * Equity Loan (replaces FirstBuy)	Help to Buy * Mortgage Guarantee	Local Authority Mortgage Scheme *
			to remortgage their current homes at lower rates (where there is a change of lender)	
		Applies to properties worth less than £600k	Applies to properties worth less than £600k	Property value threshold set by local authority (can be up to £350k) recommend £160k
	National scheme	National scheme	National scheme	Qualifying post codes set by Norwich City Council
	Participating lenders	Participating lenders	Participating lenders	Eight lenders involved
				Authority input required to set up, then scheme is administered by lender & management information supplied through CAPITA ASSET SERVICES



<b>Integrated impact assessment</b>		 <b>NORWICH</b> City Council
<p>The IIA should assess <b>the impact of the recommendation</b> being made by the report</p> <p>Detailed guidance to help with completing the assessment can be found <a href="#">here</a>. Delete this row after completion</p>		
<b>Report author to complete</b>		
<b>Committee:</b>		
<b>Committee date:</b>		
<b>Head of service:</b>		
<b>Report subject:</b>		
<b>Date assessed:</b>		
<b>Description:</b>		

	Impact			
<b>Economic</b> (please add an 'x' as appropriate)	<b>Neutral</b>	<b>Positive</b>	<b>Negative</b>	<b>Comments</b>
<b>Finance (value for money)</b>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	The indemnity deposit will be at risk, but no defaults have been experienced by current schemes. A marginally enhanced interest rate will be earned.
<b>Other departments and services</b> e.g. office facilities, customer contact	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
<b>ICT services</b>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
<b>Economic development</b>	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	The scheme will support employment in house building and associated businesses, by supporting house purchase. It may also attract new residents into the city.
<b>Financial inclusion</b>	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	The scheme will support first time buyers to purchase a property, and take their first steps on to the housing ladder.
<b>Social</b> (please add an 'x' as appropriate)	<b>Neutral</b>	<b>Positive</b>	<b>Negative</b>	<b>Comments</b>
<b>Safeguarding children and adults</b>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
<b>S17 crime and disorder act 1998</b>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
<b>Human Rights Act 1998</b>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
<b>Health and well being</b>	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	The scheme will assist those living in overcrowded and unsuitable accommodation to purchase a more suitable homes (subject to lender's financial checks)

	Impact			
Equality and diversity (please add an 'x' as appropriate)	Neutral	Positive	Negative	Comments
Relations between groups (cohesion)	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
Eliminating discrimination & harassment	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
Advancing equality of opportunity	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	The scheme will provide opportunities for those with limited deposits to purchase their first home (subject to lender's financial checks)
Environmental (please add an 'x' as appropriate)	Neutral	Positive	Negative	Comments
Transportation	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
Natural and built environment	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
Waste minimisation & resource use	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
Pollution	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
Sustainable procurement	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
Energy and climate change	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
(Please add an 'x' as appropriate)	Neutral	Positive	Negative	Comments
Risk management	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	

Recommendations from impact assessment	
Positive	
Negative	
Neutral	
Issues	