Centre for Ageing Better

Developing a local loan offer

Insights for local authorities considering adapting or introducing a local loan scheme

April 2024

Introduction

This briefing focusses specifically on the theme of loans. It provides reflections for local authorities considering adapting an existing home improvement loan scheme or introducing a new scheme for the first time based on research conducted of loan schemes that supported individuals over 50, as well as others, to make home improvements across four areas: Bradford Metropolitan District Council, Eastleigh Borough Council, Somerset Council and Wirral Council.

This briefing is an edited version of the full report: Financing Home Improvements: Local Authority Case Studies, researched and written by Foundations, the UK Government appointed National Body for Home Improvement Agencies in England, between February and September 2023, commissioned by The Centre for Ageing Better.

The councils profiled offered a range of different loan models including capital repayment loans, low-interest loans and equity share loans as well as a combination of grants and loans, administered in-house, as part of a consortium or by commissioning an external financial organisation. The detailed case studies on the finance schemes employed in these areas can be found in our full report.

Learning from these areas has highlighted a few fundamental decisions local authorities will need to make when developing a local loan scheme. Namely:

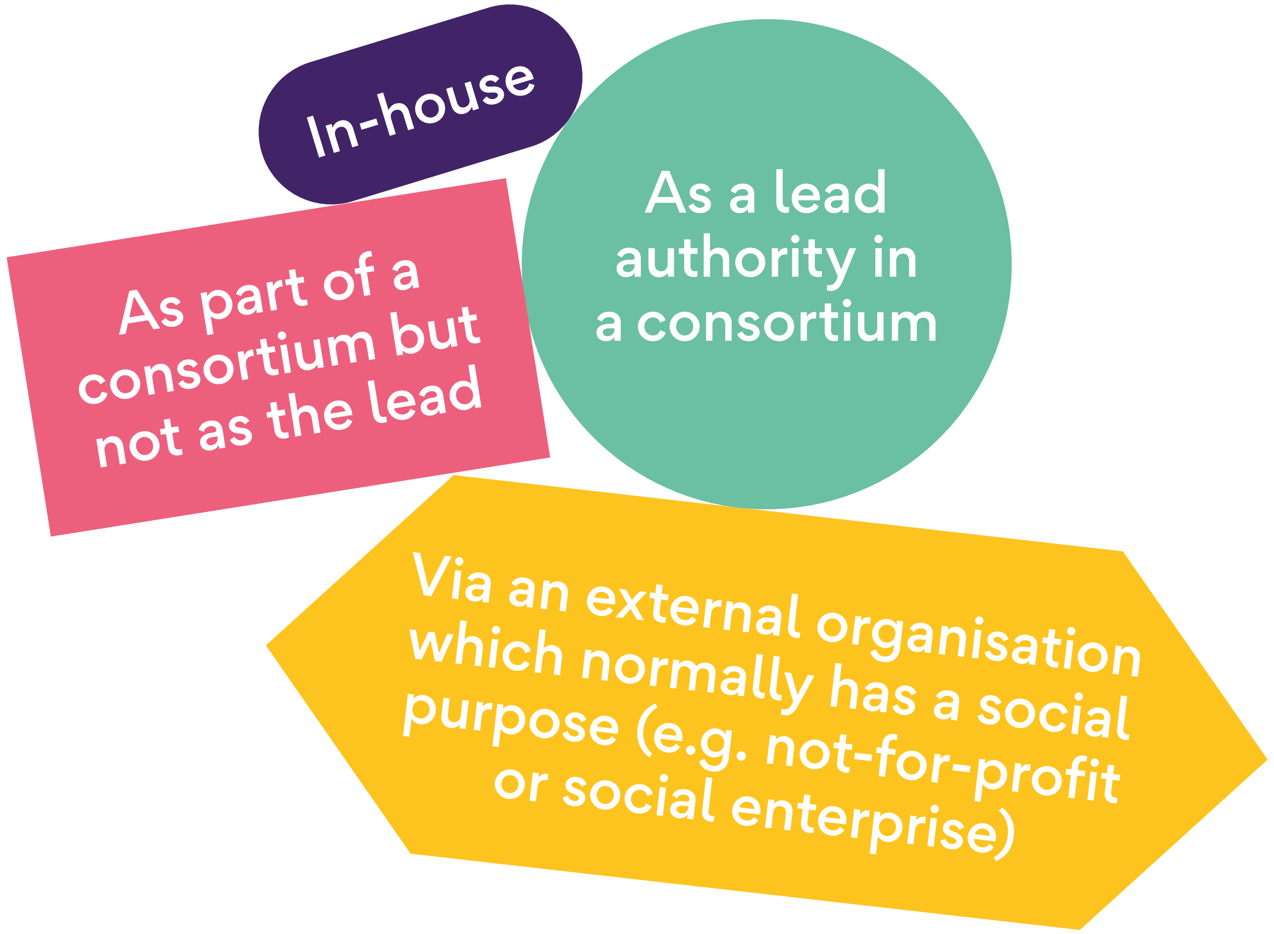
- Who might administer the loans?
- What types of loan could be offered?
- What could the eligibility criteria be?
- What governance arrangements should be considered?

This briefing explores each of these elements, sharing key learning local areas may want to consider.

It is important to note that this briefing should not be considered exhaustive or comprehensive. Official guidance should be sought out by local authorities introducing or adapting a loan offer. Further information on this can be found here. Our ambition is that this information, compiled through analysis of a few local loan schemes, will serve as a useful starting point to support local authorities on their journey to develop a tailored, local loan offer that enables more individuals to access the financial support they need to improve the quality of their home.

Who might administer the loans?

Introducing loans as a part of a local authority financial support offer is a major decision. Our case studies identified four typical options for loan administration:



In all four options local authorities had a role to play and their involvement could confer trust and credibility in the product, helping to overcome some of the perceived barriers to taking on a loan.

1. In-house administration

Local authorities who want to administer loans in-house are generally exempt from Financial Conduct Authority regulation for mortgage lending and administration but are expected to comply with the key principles of Mortgage Regulations, published in 2005. These can be accessed here and are one of the key elements that the Local Government Ombudsman will consider if a complaint is referred to them.

Examples of principles include ensuring information on loan procedures is open, transparent, and readily available to a loan applicant, as well as ensuring the loan administration process is reasonable and fair to the consumer akin to current credit regulation practice.

Regulation by the Financial Conduct Authority could apply however if the local authority financial product involves an interest rate, even a discounted one compared to mainstream lenders.

In addition to this, dependent on the volume of cases, there could be a recharge arrangement that would need to be met by the in-house home improvement agency.

An example of an in-house loan model was demonstrated in the Wirral case study in our full report and Sheffield Council also provided this service for a number of local authorities in the Yorkshire and Humberside region (including Bradford) as a lead authority in a consortium.

2. Partnering with an external organisation

If in-house administration is not viable, a local authority may want to partner with an external organisation to administer loans, which has the added value of outsourcing loan expertise. If this is the case, selecting an external organisation that is suitably registered and has a good track record of compliance with the Financial Conduct Authority is essential. Local authorities who provided loan finance to be administered by an external organisation anecdotally reported that older homeowners seemed more comfortable and confident if the partnership was with a not-for-profit loan administrator with a social purpose.

The external loan administrator will need their costs to be covered in the partnership agreement with the local authority. This could be met in a number of ways including:

- A fee which can be a fixed amount per loan or on a sliding scale dependent on the size of the loan
- An annual management fee
- A proportion of the monthly loan repayments received
- Interest earned on funding transferred from the local authority pending allocation to referred cases

Operational costs could be met from more than one of the four options listed above but the initial set up arrangements are likely to involve a cost in addition to the annual fees.

A single authority, especially a two-tier council with a small budget set aside for loans, may struggle to attract and meet the costs of a loan administration organisation who has not previously worked with a local authority for home improvement purposes. If this is the case, two alternative options could be to:

- Become an additional member to an existing partnership or
- Encourage other local authorities, preferably in the same region or sub-region, to jointly commission such a service.

One of the fundamental requirements of working with an external financial organisation is that they need to be fully aware of the detail within each local authority's Housing Assistance Policy to be able to provide informed advice to local residents seeking assistance. Regular contact with each council and the ability for both parties to respond quickly and flexibly in urgent cases was valued in partnerships.

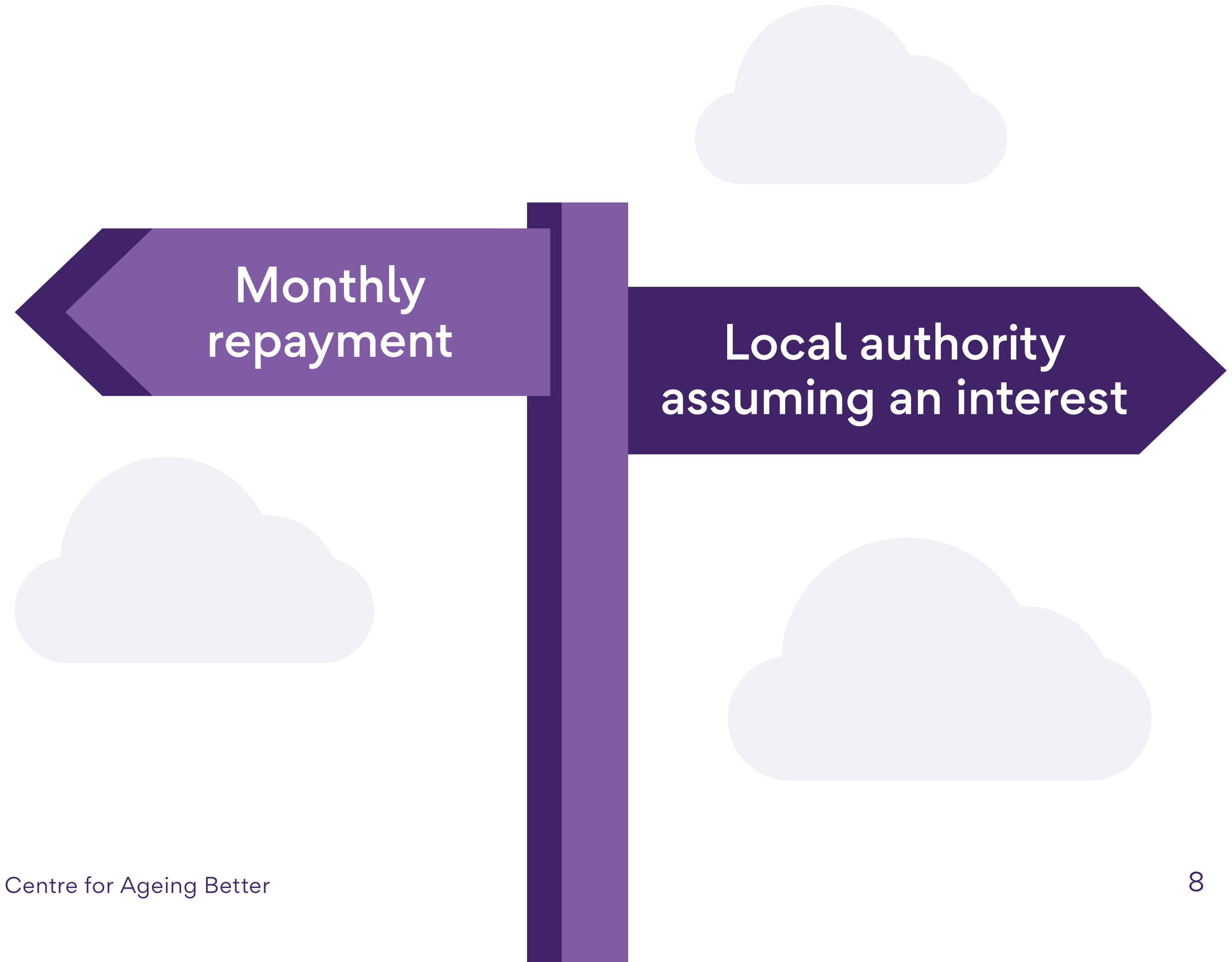
What types of loan could be offered?

Loans can involve:

A monthly repayment (which could include capital and/ or interest); or

The local authority assuming an interest in a proportion of the equity value of the property in exchange for the cost of work (and fees) that is repaid for reasons including when the owner dies, the property is sold, or the householder moves into residential care.

It is for each local authority to determine what type of loan they would like to offer. In some areas, both were offered, and the loan offered to a householder was dependent on their financial circumstances and ability to manage regular repayments. For low-income households where major works are being undertaken, a shared equity product is likely to be more affordable as there are not any monthly repayments. However, it is important to note that in areas with very low property value, the necessary loan to value criteria may not be achievable for a shared equity product.



What types of loan could be offered?

Loans involving a monthly repayment

There are a number of different forms this type of loan can take. Some examples from our case study areas are included below:

- Capital repayment loan: the monthly repayment covers both interest and capital. The loan is repaid in full over a fixed term.
- Interest only loan: the monthly repayment covers only the interest on the loan. The loan capital is repaid on the date on which a property is sold.
- Interest roll up/ deferred capital repayment loan: the initial loan period is Interest Roll up. There are no monthly repayments and the interest compounds annually for a fixed term and is added to the outstanding balance. The original capital borrowed, and the accumulated interest converts to a Capital Repayment Loan at which time monthly repayment commences. The monthly repayment then covers both interest and capital, and the loan is repaid in full over a fixed term.

Loans involving a monthly repayment provide certainty on the term of the loan. It also enables the repayments received during the loan period to be available for loans for other householders. However, there must be a robust mechanism to determine if the repayments are affordable to the householder to minimise the risk of default on payments.

Shared equity loans

This type of loan can involve either:

- Repayment of the equity-share on a non-appreciation basis (i.e. the same capital figure is repaid at a future date – as is demonstrated in the Wirral case study); or
- Repayment on a capital appreciation basis where the proportional percentage value of the home at the start of the loan and redemption of the loan remains the same (as in the Bradford case study). Unless there is a major downturn in the housing market the redemption value will be greater than at the inception of the loan which results in a larger sum being returned to the authority.

Shared equity loans mean that repayment is not made at a fixed point in the future but instead is repaid when a householder's circumstances alter and the applicant no longer resides at the property. As such, there is less certainty when the loan will be redeemed.

However, for two of the profiled councils operating a shared equity appreciation product, the average redemption period was modest, with time periods of 6 years 4 months across the total geographical area covered by the Sheffield Homes and Loans Service and between 7- 10 years for The Parity Trust across their total administrative area. Consequently, there should not necessarily be an assumption that redemption of a shared equity appreciation loan will be any longer than within a capital repayment loan.

Across the case study areas, it was also common for loans to be repaid early but, unlike some commercial loans, local authorities tended not to impose any additional charges for early repayment.

The mortgage guidance issued in 2005 specifies that with regard to equity loans, if the council's level of equity share is in excess of 30%, the applicant will be required to take financial advice before the loan is approved. The guidance also requires the local authority seeing evidence that the applicant has a valid and appropriate home insurance policy before approving the loan. The local authority details must also be included on the insurance policy so that they will be notified if the insurance is cancelled within the term of the loan, with a failure to rectify the situation potentially resulting in the local authority initiating a process to recover the loan.

Shari'a Compliant Financial Products

It is important to note that Islamic finance must not involve the payment of interest. As such, some of the loan types offered by our profiled case study areas would not be acceptable to Muslim households. A capital repayment loan without any interest (as demonstrated in Wirral) is considered acceptable as are shared equity appreciation loans based on a consistent ratio of loan to property value at the start of the loan and when it is redeemed.

Islamic finance accepts the principle of a shared equity product in that there is a shared risk of gains and losses to the lender and borrower in how property prices change over time.

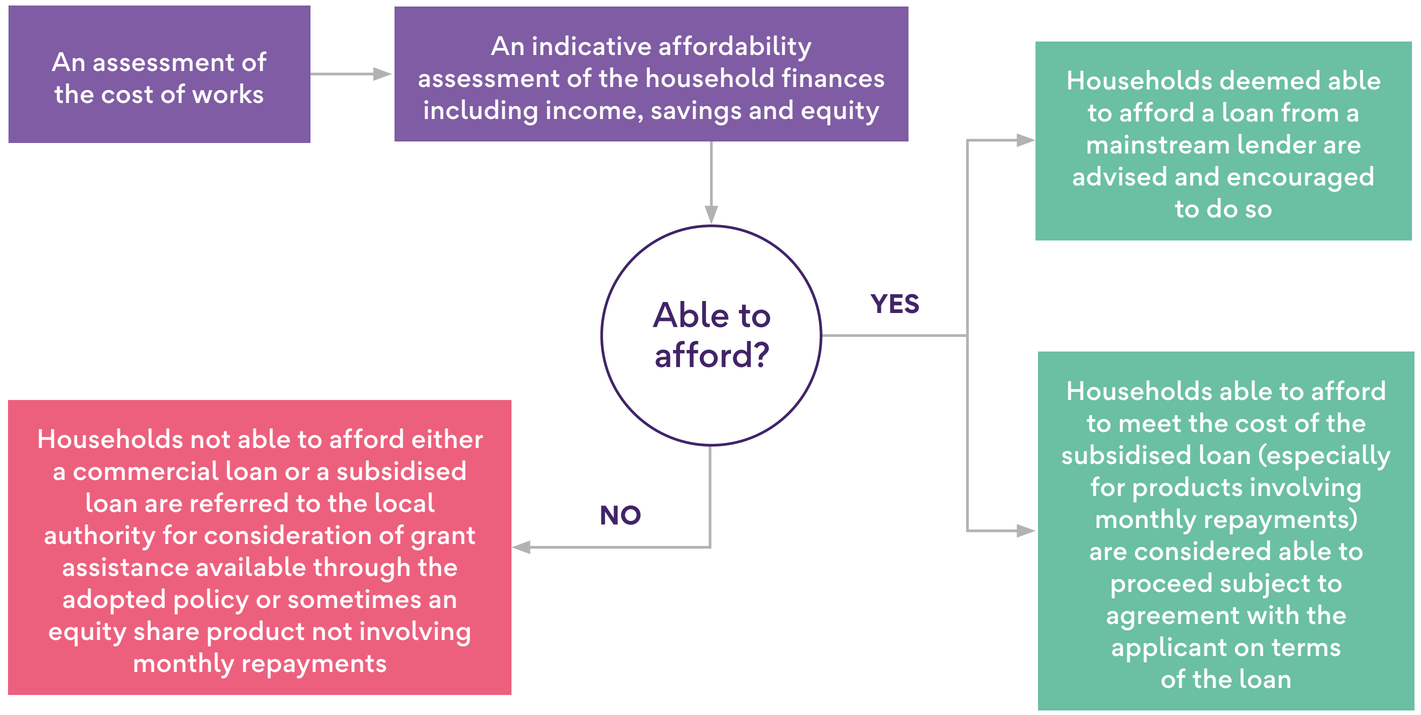
What could the eligibility criteria be?

The criteria by which loan eligibility is assessed is an important decision that local authorities need to make. The profiled case studies in our report operated a system of eligibility informed by a number of factors, including:

- Who administers loans
- Householder age
- Types of loan
- The types of work attracting loan assistance
- Household financial circumstances
- Property and equity value
- Sources of funding to support the loan product

More detailed information on eligibility criteria for local loan schemes can be found in the case study profiles. Regardless of the exact measures, the assessment process for case study areas all seemed to broadly align with the following procedure to ensure targeting of limited resources to those most in need (Figure 1).

Figure 1: Loan eligibility process across a number of case study areas



What governance arrangements should be considered?

For local authorities partnering with an external organisation for loan administration, contract conditions and a mutually agreed way of working with local residents must be established. In case study areas, the division of responsibilities broadly divided on the following lines:

Local Authority

- Initial assessment of whether household is eligible for any form of assistance by virtue of type of work and receipt of specified benefits.
- Capturing information from the applicant and obtaining their consent to share it with the loan administrator.
- Confirming costs of the work either from estimates obtained by the applicant or through offering a full agency service to the applicant to obtain estimates.
- Formal approval of loan (and any grant if jointly resourced in this way).
- Dealing with any contractor issues or unforeseen works.
- Authorising a first payment to start works, stage payments and final payment after inspection of works and obtaining confirmation of satisfaction with the works by the applicant.

Loan Administrator

- Knowledge of the local authority Housing Assistance Policy to provide reliable information to the loan applicant.
- Receive information from the local authority on household eligibility.
- Ensure by contacting the local authority, that external funding is not available for works being sought (e.g. energy efficiency).
- Arrange detailed discussion with the applicant and any accompanying trusted family or friend.
- Encourage applicant to seek independent financial advice.
- Send affordability assessment to local authority with recommendation on options i.e. self-funding, loan type or grant.
- Prepare a loan agreement for the applicant including full detail of the type of grant (including at minimum the monthly repayments, term of loan if applicable, interest payments if any, equity share information after independent valuation obtained).
- Send completed loan agreement to local authority for approval.
- Arrange charges on the property, if any, after loan approval received.
- Monitor payments and deal appropriately with any arrears.
- Settle accounts when the loan is redeemed. This is more complicated for shared equity appreciation products (as operated in the Bradford case study) as a final property valuation is required.

What governance arrangements should be considered?

Other Responsibilities

Complaints

Generally, any issue of complaint relating to the manner in which an enquiry was determined by the loan administrator was processed initially by them.

Local authorities retain an obligation to investigate a complaint involving their partner loan administrator if it cannot be resolved internally. They also have the obligation to investigate any dissatisfaction with the building contractor(s) especially if they are operating an agency service.

Monitoring Loan Activity

A local authority will usually specify that they require a quarterly or annual financial report on their budget administered by the loan administrator.

Customer Feedback and Evaluating Impact

The responsibility for seeking and receiving customer feedback (and in what form) varied between each locality but it is good practice to capture this information. Measuring impact of financial interventions in a rigorous way was recognised as a weakness generally in the Private Housing sector.

Further information

For further information about local loan models and processes, please refer to our full report: Financing Home Improvements: Local Authority Case Studies.

Centre for Ageing Better

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Let's make ageing better.

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The Centre for Ageing Better is pioneering ways to make ageing better a reality for everyone, including challenging ageism and building an Age-friendly Movement, creating Age-friendly Employment and Age-friendly Homes. It is a charitable foundation funded by The National Lottery Community Fund and part of the government's What Works Network.

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