

WIRRAL COUNCIL

CABINET

4 NOVEMBER 2010

REPORT OF THE DIRECTOR OF FINANCE

EXTENSION OF COUNCIL MORTGAGE SCHEME

1. EXECUTIVE SUMMARY

- 1.1 On 26 November 2009 Cabinet considered a report on options for the possible extension of the mortgage scheme. A further update was requested when the Financial Services Authority (FSA) had formulated proposals for a more sustainable mortgage market. This report provides an overview of the current situation regarding mortgage liquidity, a pilot Local Authority Mortgage Guarantee Scheme and Government plans to refocus the Mortgage Rescue Scheme.

2. BACKGROUND

- 2.1 The 2009/10 budget resolution requested the Director of Finance to investigate the extension of Council mortgage provision. This was to be targeted particularly to where the commercial supply of mortgages had dried up and where it would be beneficial for the Authority to encourage the ownership of housing.
- 2.2 Whilst the situation has improved since the economic downturn began, banks continue to restrict the supply of mortgages to the market. There has been a significant reduction in the availability of mortgages and increasingly stringent conditions and arrangement fees imposed by lenders. The latest figures from the FSA show that, in the first quarter of 2010, new lending with more than a 90% loan to value (LTV) ratio accounted for less than 2% of all new mortgages. Where 90% LTV mortgage deals are available, interest rates tend to be in excess of 6% as compared to rates of 4% for those requiring only a 75% mortgage.
- 2.3 The Authority currently has a mortgage portfolio which, in the main, relates to former Council tenants who applied for Council mortgages as part of the Right-to-Buy scheme. Cabinet, on 3 September 2009, agreed to the introduction of a Home Purchase Assistance Loan Scheme targeted initially at Housing Market Renewal areas and restricted to up to 30% of property value and funded from Growth Point resources. On 27 May 2010, Cabinet was advised that this product was subject to further legal advice which concluded that the Local Authority lacks sufficiently reliable powers to introduce the scheme as outlined. Therefore attention has moved to the possibility of introducing other initiatives to support home ownership.

- 2.4 A particularly relevant issue for new-build housing in regeneration areas of Wirral (as well as Liverpool and Sefton) is the undervaluation of property by lenders which is preventing interested buyers from concluding purchases at values they have agreed with developers. Discussions are underway with the Homes and Communities Agency (HCA) about possible options in areas where lenders are taking an extremely cautious position which is stalling the regeneration of neighbourhoods. Very recently, smaller high street lenders have been prepared to value new housing at the price which the developer and purchaser have agreed but this approach is inconsistent and is affecting the take-up of owner occupation. The result of undervaluation is that prospective buyers are forced to provide a larger deposit, the appeal of new-build housing suffers as new homes are being valued at the same levels as existing stock, the confidence of private developers and housebuyers is at risk and market downturn may occur.
- 2.5 The Authority also currently participates in the Government funded Mortgage Rescue Scheme designed to assist vulnerable households.

3. FINANCIAL SERVICES AUTHORITY (FSA) PROGRESS

- 3.1 In October 2009, the FSA set out proposals for reform of the UK mortgage market aimed at making improvements and ensuring greater sustainability for consumers. This was reported to Cabinet on 26 November 2009 when it was agreed that a further report would be presented when the FSA had made recommendations on the way forward.
- 3.2 Based upon the feedback from their initial consultation paper, in June 2010 the FSA put measures in place to ensure proper protection for vulnerable customers either in arrears on their mortgage or entering sale and rent-back agreements. This protection included preventing firms from charging for arrears when an agreement is already in place to repay the arrears and clarifying that repossession is always the last resort.
- 3.3 In July 2010 the FSA produced a consultation paper entitled 'Responsible Lending' which set out a package of proposals aimed at ensuring homeowners are treated fairly. The proposals included imposing affordability tests for all mortgages, making lenders ultimately responsible for assessing a consumer's ability to pay and ensuring that firms only lend to people who can afford to pay the money back. Feedback from this next consultation paper is due in November 2010.
- 3.4 As can be seen from the progress since October 2009 the reforms will be gradual rather than a wholesale change in approach. The FSA has made it clear that there is no set timeframe for its work, it will continue to monitor movements in the mortgage market and it does not intend to rush into any further implementation of rule changes. The preferred approach is to carry out a thorough consultation and impact assessment before any changes are made.

4. MORTGAGE SCHEME OPTIONS

4.1 The report to Cabinet on 26 November 2009 considered the various options available to the Council to assist Wirral residents in the mortgage market. These included:

- Internally run provision.
- Arrangements for third party provision of administration including mortgage application administration, vetting and collection.
- Partnership with lending institutions such as banks or building societies, perhaps either offering joint funding or guarantees

4.2 Local Authority Mortgage Guarantee Scheme (LAMGS)

4.2.1 A number of local authorities, in conjunction with the consultancy firm Sector, have investigated other options for supporting their local housing market. The issues of limited financial resources, staffing and expertise available, combined with the considerable operational risk in entering the residential mortgage market, led to the view that a Partnership Arrangement was the most appropriate solution.

4.2.2 This led to Sector developing the Local Authority Mortgage Guarantee Scheme (LAMGS) which is expected to be operational later in 2010. The scheme would be available to potential buyers who meet the criteria decided by the Local Authority and partner (the lender). The Local Authority would then provide a 'top-up guarantee' to the value of the difference between the typical 75% and a 95% LTV mortgage. The buyer would, thereby, obtain a 95% LTV mortgage but without the need to provide the substantial deposit usually required.

4.2.3 The guarantee could either be unfunded or cash-backed depending on the requirements of the lender. For both types of guarantee, the liability would terminate at the earliest of, either the end of the agreed guarantee period (i.e. five years, which may be extended for a further two years if the mortgage is in arrears at the end of the guarantee period) or an early repayment of the mortgage. In the case of a cash-backed guarantee, the fixed-term deposit would be repaid to the Local Authority at the date of maturity.

4.2.4 However this scheme is not without risk. The way the scheme is set up implies that the local authority is the first to be exposed to any fall in property prices and the lender takes little or no risk. If a property value falls 20% and the mortgagee defaults then the lender gets all their money back with the Local Authority having to make good the guarantee or, if cash-backed, would lose their element of the loan. Consequently the risks are heavily geared against the Authority.

4.2.5 Before progressing with any scheme Cabinet would need to consider the criteria for the scheme:

- Should mortgage guarantee arrangements be restricted to first time buyers and/ or particular areas of the Wirral e.g. the HMRI area?
Given the issues raised in paragraph 2.4 Members may wish to consider targeting the scheme at new build in the HMRI areas.
- What level of guarantee should be offered on a Loan to Value ratio basis?
The guarantee could be offered at the lower of 15% of the purchase price or £20,000 with a LTV of no greater than 95%.
- Should there be a minimum and maximum guarantee?
The maximum guarantee could be £20,000.
- How much should the Authority commit to guarantees?
With a maximum guarantee of £20,000, an allocation of £1 million could see 50 people benefiting from the scheme.
- How long should any scheme operate for and should there be a review date?
After offering £1 million of guarantees there could be an annual review.
- Who within the Council would run the scheme?
Given the potential links with HMRI and the knowledge and experience of the housing market within the Housing & Regeneration Division, the Scheme could be run by the Director of Corporate Services.

4.2.6. The Sector scheme, in partnership with Lloyds Banking Group, was expected to be operational in the summer of 2010. However, issues within the European Commission have delayed its implementation. Sector is confident that the issues can be resolved and, with Blackpool Council acting as lead authority, is hoping for a positive outcome in the near future which would enable the scheme to begin in November 2010.

5. MORTGAGE RESCUE SCHEME

5.1 In February 2009 Cabinet received a report outlining an additional tool available to the Council, through a Government scheme, aimed at providing Mortgage Rescue to vulnerable households.

5.2 The Mortgage Rescue Scheme initiative was set up with the objectives of:

- Assisting first time buyers who are frozen out of current mortgage markets;
- Supporting vulnerable homeowners facing repossession, particularly those who the Local Authority would owe a duty under homeless legislation;
- Ensuring the Government and Local Authorities are as well placed as possible to meet housing needs, especially affordable housing in the short and long term.

5.3 The scheme has, to date, helped 34 people nationwide but has had a positive impact upon helping increase the leniency of mortgage lenders on householders in difficulties and in mortgage arrears management. The scheme is scheduled to close at the end of this financial year and the Government is presently reviewing the scheme with a view to delivering better value for money and targeting homeowners who are most likely to benefit from it.

6. FINANCIAL IMPLICATIONS

- 6.1 The Authority would have to fund any Council-run scheme by borrowing, and charging interest to mortgage holders at a rate which is reviewed periodically by the Government but which is above normal bank rates. The administration of the mortgage portfolio is presently undertaken by an external organisation and any costs would be dependent upon the take up of any scheme.
- 6.2 In terms of the Local Authority Mortgage Guarantee Scheme there would be an element of financial risk for the Authority. This could arise via default on payments and particularly if negative equity occurred or property fell into disrepair. These could be mitigated, but not removed, by such as setting a maximum loan percentage and requiring owners to fund a deposit against the property and the use of rigorous financial assessment procedures.
- 6.3 Dependent upon the requirement of the mortgage lender involved in the Local Authority Mortgage Guarantee Scheme, money may have to be set aside up to the level of mortgage guarantees offered. For £1 million of guarantees the Council may set-aside £1 million, from balances, to cover against potential defaults. Alternatively, if the scheme is unfunded, the Council could decide to fund defaults as and when they occur without setting money aside.
- 6.4 The Mortgage Rescue Scheme is fully funded by the Government and the administration of the scheme can be managed within existing resources.

7. STAFFING IMPLICATIONS

- 7.1 These would vary depending upon whether any scheme was progressed and to what degree, with no staffing resources presently identified.

8. EQUAL OPPORTUNITIES IMPLICATIONS

- 8.1 Any scheme would assist those who are currently having difficulty obtaining mortgage finance. This is likely to benefit, in particular, young people and those in the less affluent areas of the Borough.

9. COMMUNITY SAFETY IMPLICATIONS

- 9.1 There are none arising from this report.

10. LOCAL AGENDA 21 IMPLICATIONS

- 10.1 There are none arising from this report.

11. HUMAN RIGHTS IMPLICATIONS

- 11.1 There are none arising from this report.

12. PLANNING IMPLICATIONS

- 12.1 There are none arising from this report.

13. LOCAL MEMBER SUPPORT IMPLICATIONS

13.1 There are none arising from this report.

14. BACKGROUND PAPERS

14.1 Mortgage Market Review Discussion Paper: Financial Services Authority October 2009.

14.2 Financial Services Authority Statistics on Mortgage Lending: June 2010 edition.

14.3 LAMGS - Local Authority Mortgage Guarantee Scheme: Sector.

15. RECOMMENDATIONS

15.1 That the work of the Financial Services Authority and the Government towards assisting vulnerable households be noted.

15.2 That Cabinet either:-

- a) Notes the availability of the Local Authority Mortgage Guarantee Scheme and that no further action be taken at this time, or
- b) Engage in discussions with Sector, and mortgage lenders, about Wirral joining the Local Authority Mortgage Guarantee Scheme and agrees that either £1 million be set-aside from balances to cover potential mortgage guarantees or that it be recognised that the Council would have to meet the cost of any defaults as and when they arise, from balances.

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