Will PWLB new lending criteria impact housing?

The Government have been consulting since March on changes to the Public Works Loan Board (**PWLB**) lending criteria for loans to councils. Though the proposals are not intended to stop the public funding of housing or certain regeneration activities they might have that effect, at least, for a number of local authorities. If you are interested, the consultation closes on 31 July.

The Treasury's objective is to stop Councils using PWLB loans to acquire property for profit/income generation; which the Treasury terms "debt-for-yield" acquisitions.

The backstory to the proposals is how a number of councils have sought to generate income through investment in order to (partly) offset the substantial reduction in local government funding since the 2008 economic crisis. The National Audit Officer (NAO) raised concerns in 2018 about some councils' use of PWLB loans to increase the acquisition of for profit commercial property portfolios in order to generate income. The NAO's main concern is the potential impact on a council's finances if its property investments turn sour. The Treasury's bête noire was a district council which is reputed to have borrowed £1 billion from the PWLB to fund debt-for-yield property acquisitions.

The Ministry for Housing Communities and Local Government (**MHCLG**) issued statutory guidance to councils in 2018 with the aim of deterring councils from borrowing (whether from PWLB or the markets) purely in order to make investments. In 2019 the Chartered Institute of Public Finance and Accountancy (**CIPFA**) also issued additional guidance with the same objective.

HMT's proposals on PWLB loans are consistent with previous guidance, though it does raise the question of why PWLB loans were not previously restricted. Surprisingly, this was because HMT did not prior to February 2020 control PWLB lending. Instead, PWLB Commissioners approved loans to local authorities with lending criteria primarily based on receipt of a loan request. Though this approach, at least, had the benefit of ensuring political neutrality in government lending to councils it failed, in the NAO's and the Treasury's opinion, to properly police what public funds/debt was being spent on.

The Treasury's consultation, together with responses made by departmental officials to the House of Commons Public Accounts Committee, does provide some insight into how future PWLB lending will operate. The government is clear that it does not want to restrict PWLB loans for council housing or other council funded housing, included those owned by council companies. However, it is possible that this might be the affect of the proposed changes for some local authorities.

The reason for this contradiction is due to how councils borrow. They borrow against their capital programmes which will include a range of projects and initiatives some of which might be housing. They do not borrow from the PWLB on a project specific basis. The proposed PWLB lending criteria would therefore apply to a local authority's entire capital programme rather than a specific PWLB loan request. This could result in a council being denied a PWLB loan (which it intend to use for housing) because if it proposed to include a "debt-for-yield" property within its capital programme.

HMT and MHCLG have also stated that they want to protect PWLB borrowing by local authorities which is primarily targeted at regeneration within a Council area. The principles set out in the consultation are not as comprehensive as they could be and are likely to be followed by more detailed guidance. HMT considers regeneration (which is eligible for PWLB loans) should address market failure and/or to prevent a negative outcome, (i.e. maintaining assets of community value) and/or that the Council is making an investment which is more than an acquisition price and/or the council's funding generates significant additional activity that would otherwise not happen.

The aim is to restrict councils using regeneration as an excuse to use PWLB debt to invest in "for yield" assets, rather than the government being over prescriptive about what regeneration should entail. Further guidance and cases studies on regeneration would be useful if only to stop some councils self denying themselves PWLB funded regeneration for fear of being subsequently found to be ineligible for PWLB loans.

The proposed PWLB reforms may provide opportunities for market lenders/investors to provide finance to local authorities particularly if councils are found to be ineligible for PWLB loans. However, MHCLG's existing statutory guidance is aimed at restricting Council's from borrowing (from any source) to acquire investment properties. MHCLG's concern is that local authority property investments are at risk of turning sour with potential catastrophic consequences for local authority finance.

Paul McDermott

Partner – Public Sector Group