APPENDIX 1

REPORT OF THE SERVICE DIRECTOR, FINANCE, PROCUREMENT & IMPROVEMENT

LOCAL AUTHORITY MORTGAGE SCHEME – PROGRESS REPORT

The LAMS Process and Associated Risks

1. Whilst the County Council is not a housing authority it clearly has a very significant role in terms of promoting economic prosperity within the County. Participation in LAMS, by way of lending to banks in a manner which allows them to make more affordable mortgages available to people who do not currently have the resources to put a significant deposit into a house, will make a significant difference on the property market within the County. There is a potential to aid about 500 first time buyers with approved proposed total investment of £15m in the Nottinghamshire scheme. In addition, there are expected to be knock-on economic benefits to the County of the scheme, although these are more difficult to quantify.

2. The scheme operates by way of the County Council lending an amount of money (the first tranche was set at £2m) to a financial institution that has agreed to be part of the scheme. This loan will be for a 5 year period and the interest payable will be a market rate for a 5 year loan plus an additional margin to protect against some of the risks associated with the default by mortgage holders. This is known as a cash-backed scheme.

3. The loan made to the financial institution is not used to provide the finance for individual mortgages and is merely used as an indemnity against any defaults on the mortgages that occur in the five year period. After this five year period the lender assumes full responsibility for the mortgage and any subsequent defaults, and the loan is returned to the County Council. If there are mortgages that are in arrears by more than a specified period at the end of the five year period, there will be an agreed ‘hold back’ to cover the possibility of these mortgages ultimately ending in default.

4. Two financial risks to the County Council were identified: firstly that the financial institution defaults on the loan and secondly that their lending criteria are insufficiently stringent and that a significant number of defaults occur. The former of these risks can be minimised, but not alleviated completely, by careful choice of the counterparty. The latter risk is more difficult for the County Council to control and it is important to be comfortable that the financial institution has a risk-aware methodology in respect of the granting of mortgages. It is reasonable to expect them not to

take risks with the County Council's money that they would not take with their own, and this has been confirmed.

5. For any mortgages granted the mortgagee will put down a deposit of at least 5% and the County Council's loan to the financial institution will indemnify the rest of the loan, down to a 75% level. In the event of a default an invoice would be issued to the County Council to cover the amount of the indemnity provided against the mortgage, less any monies recovered as part of the repossession and sale of the property.

   The Mansfield Building Society (MBS) schemes are non-cashed back schemes, whereby the Council offers guarantees to the financial institution on offering up to 20% mortgage guarantee for the payment of a premium, typically in the region of £500 per mortgage, which would in effect reflect the risk in offering the guarantee to each mortgage. In non-cash backed schemes it is only upon default of a mortgage whereupon the Council would have to pay over to the financial institution for the level of the indemnity provided on the mortgage (net of any recovery). Similar to the cash backed scheme the length of the indemnity is for a 5 year period. The same conditions would apply as to the maximum loan of £142,500 and the same strict lending criteria would be undertaken for a mortgage as for all mortgage applicants from the financial institution. Consequently, it is anticipated that with similar low default rates the premiums received would be in excess of any default risk. In addition, as no money is initially lent in a non-cashed backed scheme the initial counterparty default risk would not exist.