**Link Group**

**Update to SDCT Meeting 5th June 2020**

**PWLB Consultation on future lending arrangements**

* PWLB consultation on future lending arrangements - deadline extended to 31st July (4th June). Link released a technical release to clients to assist them in responding to the consultation.
* Key points;
  + Immediately cutting HRA loans to Gilts + 80bps
  + Restricting future lending to non-commercial only (service delivery, regeneration, housing, refinancing existing debt) and prohibiting ‘debt for yield’ schemes
  + Will not lend, if LA has commercial scheme within their capital programme (irrespective of how that is financed)
  + Subject to this – intention is to reduce interest rate on new PWLB loans
* Borrowing options - use internal borrowing and/or temp but use forward Balance Sheet to manage future financing risks including use of forward starting loans, available through market lenders.

**Commercial activity within Local Government**

* PAC inquiry into LA commercial activity was held of the 11th and 15th of May (aware that SDCT submitted a response to the PAC call for evidence) -  Link issued a newsflash to clients, key points;
  + Rob Whiteman (CX - CIPFA) made it clear that his view was that recent changes to the CIPFA Treasury Management Code of Practice, Prudential Code and MHCLG Guidance meant local authority Investments purely for yield, and outside of their operational boundary, was prohibited.  His view is that they shouldn't be doing it and that after the on-going PWLB Consultation is concluded, no PWLB loans should be made available to support commercial activity.
  + Rob Whiteman was pushed to comment on why changes to Codes/Guidance had not seen local authority commercial activity end. The response was there is always a lag between implementation and impact.  He reiterated his comments about borrowing in advance of need changes meant the activity to borrow to finance an activity purely for yield was prohibited.
  + Richard Watts, the LGA representative, kept pushing the view that Central Government had encouraged local authorities to be more commercial as grant funding and other income was reduced.
  + Rob Whiteman suggested that External Audit needed more of a joined-up role.  Perhaps a return of something like the Audit Commission? Whatever happens, they all seemed to agree external auditors needed a more prominent role in the scrutiny and whistleblowing process.
  + An MP asked the panel about the proportionality of Spelthorne taking loans which were 44 times their annual turnover. He also questioned whether local authority councillors were equipped to approve complex, high value property deals. Rob Whiteman suggested separate meetings should be arranged to allow members time to ask for expert advice to scrutinise officer reports. This also brought into question the independence of S.151 officers and Rob Whiteman said he was concerned that some have been demoted below SLT/Director level, impacting their ability to carry out their statutory role.
  + The discussions also include reference to the current funding package to deal with initial pressures local authorities face from Covid and some reference to concerns about some local authorities potentially issuing S.114 notices.
  + On the commercial investment front, several local authorities are named specifically. MRP is also mentioned, and there is potential for changes to the Code and Guidance to ensure sufficient MRP is set aside. +
  + The various representatives also covered off income strips and there is a quote from MHCLG to say these will not be allowed if they are entered into purely for a yield.
  + S.4 power was also raised, which would allow the Secretary of State to prevent a local authority from raising debt if it cannot afford to pay it back. But MHCLG said that these powers have not been used as it relies on the prudential system to control borrowing. They also infer they want to continue simple PWLB lending arrangements but again make it clear that the intent is to end their loans for any commercial/yield only activity. It was also confirmed that the PWLB lending consultation deadline has been extended to 31st July 2020.
  + In summary, based on the evidence given, it looks like more transparency will be required, including a requirement to publish more information on all economic regeneration/commercial activity deals entered into by local authorities. We may also see more changes to Codes and Guidance, the removal of PWLB lending on commercial activity and an extended role for External Audit.

**COVID 19**

* Credit risk/liquidity issues/considerations under Covid-19
* Risk of negative UK interest rates, Link view, possible but unlikely, BoE more likely to extend QE. But if it does happen, will be a matter of longer dated will be less affected, it is still a priority to protect principal so beware of chasing rates with lower quality counter parties and if it does happen it shouldn’t be around for long.
* Potential loss of capital/unrealised capital and income losses on some longer term investments and commercial investments - impact on balance sheet and income account - use of pooled fund override and capital loss reversal where applicable
* Fair Value and Expected Credit Loss e.g. use of historical risk of default at 31st March 2020 and confirm no real change in ratings or CDS post Balance Sheet date.

**Rob Baxter, Associate Director – Link Group**