APPENDIX 1 – Financial risk assessment of proposed payment options

	Equity Loans	Maturity Loans	Interest-Free Repayment in Instalments	25 Year Loans
How does the loan work?	The loan will be secured on the property to which the service charge relates and charged at the Land Registry. The charge on the property is expressed as a percentage of the value of the property. It will be paid either when the property is sold or by the leaseholder in situ in agreement with the council. The amount paid back is dependent upon the valuation at the time of sale of the property. The council will need to rely on expert advice from its Right to Buy valuer in order to determine the best consideration in the property. This percentage will depend on factors such as predicting the future value	This is where a loan is taken out to fund the value of the works and a charge is placed on the property. The loan will attract interest which will be rolled up with the principal and when the property is sold the value of the loan plus interest is repaid to the Council. There is no maturity date for the loan so it can carry on indefinitely. It will be paid either when the property is sold or by the leaseholder in situ in agreement with the council. Each case will be considered on an individual basis and consideration will be given to any other loans secured against the property.	This is where the Council makes a formal agreement with the leaseholder to repay in monthly instalments over a specified period without adding interest. The leaseholder would only be liable to repay the principal sum over the period outlined in paragraph 3.14.	These are interest bearing loans over 25 years offered by the council and work in the same way as any other commercial mortgage.

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	of the property and the potential length of the loan. This is to ensure when the property is sold there is sufficient equity to cover both the original loan and the accumulated interest. Each case will be considered on an individual basis and consideration will be given to any other loans secured against the property.			
What are the annual costs to the leaseholder, assuming a £10,000 debt?	The leaseholder will not need to pay anything until the property is sold. At this time the agreed percentage equity share of the value of the property will be paid to the council. As an example, if a property is valued at £100,000 and the loan is £10,000 it might be assumed that the council would offer the loan in turn for 10% of the property value. Instead the council may decide to offer a loan at a higher % of the value	The leaseholder will not need to pay anything until the property is sold. The charge on the property will mean that the council will get first call on the sale proceeds. If the £10,000 loan lasted for 10 years, say, the charge on the property would be £15,981 at current interest rates.	To repay £10,000 over 3 years, the leaseholder would need to make instalment payments of £277 per month. Therefore, it is unlikely that this option would be taken up for large sums.	A £10,000 loan over 25 years would cost £57.95 per month at current interest rates.

	Equity Loans	Maturity Loans	Interest-Free Repayment in Instalments	25 Year Loans
	to ensure that property market risks are covered and that the principal, interest and administration fee are repaid in full.			
What are the Administration fees or set up costs chargeable to the Leaseholder	Professional costs of conveyance including valuation, solicitors and Land Registry fees will be recharged to applicants by consolidation in the equity share. These fees could be substantial (in the region of £500) and would therefore need to be assessed prior to any decision to take up an equity loan.	An administration fee of approximately £200 would be added to the loan.	Not applicable.	An administration fee of approximately £200 would be added to the loan.
Transfer of property ownership (for non-repayment options)	It is proposed that a property with such a loan on it may only be transferred once on the death of a leaseholder. This transfer would be to either a spouse or long term partner living in the property. In all other cases the property would have to be sold or the debt otherwise cleared prior to the property being	A property with a maturity loan secured on it may only be transferred once on the death of a leaseholder. This transfer would be to either a spouse or long term partner living in the property. In all other cases the property would have to be sold or the debt otherwise	Repayment arrangement	Repayment loan

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	inherited. Any instance of repurchase of the loan share or further granting of a loan will be at the current market value with all associated interest, fees and costs.	cleared prior to the property being inherited.		
Risks to the council	There is a risk that due to the unpredictability of the social housing market over the longer term, the equity percentage applied will not fully recover the costs of principal, interest and administrative costs. **An example is given in the footnote to this appendix.**	There is a risk that, if the loan period is long, insufficient equity will exist in the property to pay back the loan sum and the interest accrued. This type of facility may be more suitable where the loan period is likely to be short.	This method is relatively low risk to the Council if the instalment arrangement is considered affordable to the leaseholder. Although interest is foregone, there is a benefit of the whole principal sum being repaid in the agreed period.	Given that these leaseholders are likely to be on low or fixed incomes as they are unable to fund the major works in any other way, there will be a high risk of default on these loans. Careful assessment of the individual's ability to pay will be necessary prior to the offer of such a loan.
Financial implications	The percentage charge put on the property would have to ensure that the loan, interest and administration fees were paid back. Any shortfalls resulting	If the loan sum plus interest is paid back when the property is sold, there are no cost implications for the HRA over the term of the loan.	The cost to the HRA is the interest foregone. For a £10,000 arrangement over 3 years, the interest foregone would be £771 at current	If the principal and interest is paid back monthly there are no cost implications for the HRA. If the leaseholder does

	Equity Loans	Maturity Loans	Interest-Free Repayment in Instalments	25 Year Loans
	from incorrect assessment of the equity share would have to be paid by the HRA and a provision for this risk would have to be made. However, it is also the case that the HRA could gain if the agreed equity share paid back more than the outstanding debt in a rising housing market. The delay in receiving this income may lead to increased temporary borrowing by the HRA. This may result in other projects being delayed due to the application of borrowing restrictions under the new self financing regime.	However, the delay in receiving this income may lead to increased temporary borrowing by the HRA. This may result in other projects being delayed due to the application of borrowing restrictions under the new self financing regime. As mentioned above there is a risk that insufficient equity will exist in the property to pay back the loan sum and the interest accrued, especially if the loan period is long. Future budget and business plan assumptions will need to take account of this risk and provisions made for any potential shortfalls.	interest rates. An average of £257 per annum for each £10,000 arrangement. A £5,000 repayment interest-free over 2 years would cost £249 in lost interest to the HRA. Current estimates for the take-up of this option during the next 2 years means the interest foregone is estimated to be approximately £14,500. This will be met from current HRA budgets.	default on the loan there are other options open to the council to pursue the debt, including legal action for recovery. However, given the risks mentioned above, provision for default will need to be made. The delay in receiving this income may lead to increased temporary borrowing by the HRA. This may result in other projects being delayed due to the application of borrowing restrictions under the new self financing regime.

Footnote: Examples of equity share on £10,000 for property currently worth £100,000 showing changing market values

Change in value	**Value after 10 yrs £**	**Admin Fee £**	**Total owed £**	**Equity share required**
No change	100,000	300	16,281	16.7%
+10%	110,000	300	16,281	15.2%
+20%	120,000	300	16,281	13.9%
+30%	130,000	300	16,281	12.8%
-10%	90,000	300	16,281	18.6%
-20%	80,000	300	16,281	20.9%