

ANGUS COUNCIL

DEVELOPMENT AND ENTERPRISE COMMITTEE – 20 JANUARY 2015

NATIONAL LOAN FUND FOR BUSINESSES

REPORT BY CHIEF EXECUTIVE

ABSTRACT

This report informs the Committee of the proposed winding up of the East of Scotland Investment Fund (ESIF) and the creation of a National Loan Fund (NLF) which will offer finance to business, and seeks approval to contribute funds to the new loan fund, and seeks approval for the proposed administration of the fund.

1. RECOMMENDATIONS

1.1 It is recommended that the Committee:

- (i) Approve in principle to Angus Council participating in the NLF and new company and becoming a Member of the NLF;
- (ii) Authorise the Service Manager – Economic Development, in consultation with the Head of Legal and Democratic Services and the Head of Corporate Improvement and Finance, to agree with other Scottish local authorities the creation and operation of a NLF to support businesses;
- (iii) Agree that the Service Manager – Economic Development in consultation with the Convener of Development and Enterprise, or the Depute Convener in her absence, be delegated to approve all loans offered to Angus businesses through the NLF;
- (iv) Agree the maximum loan from the NLF to Angus companies be set at £50,000;
- (v) Agree the proposal to wind up the ESIF and approve the transfer of remaining ESIF funds to the NLF;
- (vi) Approve the allocation of an additional £50,000 into the NLF for Angus; and
- (vii) Note that the Service Manager – Economic Development will inform the Committee of progress in establishing and operating the NLF via future information reports.

2. ALIGNMENT TO THE ANGUS COMMUNITY PLAN/SINGLE OUTCOME AGREEMENT

2.1 This report contributes to the following local outcome contained within the Angus Community Plan and Single Outcome Agreement 2013-2016:

- We have a sustainable economy with good employment opportunities

3. BACKGROUND

3.1 The background to the creation of the ESIF and how it operates in Angus was covered in Report 303/12 submitted to the Infrastructure Services Committee 14 June 2012.

4. CURRENT POSITION

4.1 East of Scotland Investment Fund

Angus Council is currently one of ten local authorities that are members of the ESIF. The fund, which was established via member contributions and funding from the European Regional Development Fund (ERDF), has been operational since 2011 and its primary purpose is to offer loans of up to £50,000 to new and growing, small and medium sized businesses (although by exception it can offer loans of up to £100,000). The fund can offer up to 50% of any funding package that a company is looking to secure and it is intended to be a lender of the last resort. Many businesses are eligible for support but those operating in certain activities (eg retail, professional services, property and primarily local services) are ineligible. The maximum repayment period is normally 5 years.

To date the ten local authorities have contributed £2.620 million to the ESIF. It has enabled this business support programme to secure ERDF match funding of £1.400 million offering a total fund £4.020 million.

Although it is a single East of Scotland fund with common operating procedures and a common fund manager, it can be considered to operate locally. Local authorities have sole discretion to approve loans in their respective areas and can only authorise loans to the total value of their contributions (and European match funding). In effect members' contributions are ring fenced to benefit businesses in their area.

Up to the end of November 2014, the ESIF has issued 89 loans totalling £3,543,500 (average loan value £39,815). 63 of the 89 loans issued (71%) have gone to companies in the four local authority areas of Edinburgh, Fife, Midlothian and West Lothian. Based on information provided in application forms, the loans issued to date have been predicted to support the creation of a total of 678 new jobs and increase business turnover by an average of £483,000 per project.

Up to the end of September 2014, loan repayments totalling £1.58 million had been received. However, as with any loan fund there is a risk of bad debts. While it is considered that there is strong governance in place with assessment criteria that borrowers must meet, it is almost inevitable that ESIF, as a lender of last resort, will incur bad debts or have some loans that are in danger of default. Currently there are 3 loans recommended for write off as bad debts, 8 loans where there is a strong possibility of loss or only partial recovery of funds and a further 11 loans where there have been either missed payments or a temporary payment moratorium agreed.

The ESIF charges interest on loans at a fixed rate of 6% per annum. This is considered a competitive, commercial rate and set at this level to avoid any state aid issues and to ensure the programme is eligible for ERDF support.

4.2 ESIF Activity in Angus

Angus Council's contribution of £50,000 to the ESIF was a transfer of funds from the Angus Loan Fund, a local fund for Angus businesses that was subsequently discontinued. It should be noted that the Council is by far the lowest member contributor to the fund. The next lowest contributor is Dundee City Council (£130,000) and the highest contributor is Fife Council (£623,000). The average local authority contribution is £262,000.

Officers have been active in promoting the scheme to Angus companies where there have been appropriate opportunities. Information is also available on the ESIF website www.eastscotinvest.co.uk and the business support website www.businessangus.com. Officers have engaged with a total of 32 companies where it was considered that a loan from the ESIF may have been appropriate for their needs. This resulted in the processing of three applications and the draw down of two loans – one of £25,000 to Pizza Plus and one of £30,000 to the Crazy Castle Play Centre. The third potential borrower eventually secured private finance from an alternative source. Unfortunately Pizza Plus ceased trading approximately 6 months after the business opened, having failed to generate the level of turnover forecast in the business plan. Pizza Plus made regular monthly payments while trading and the balance owing on the loan at the time the business closed had reduced to £21,667. This loan is one of the three recommended by the ESIF for write off as a bad debt.

Despite this setback, it should be noted that the loan was partly used to fund improvements to a leased property. A new business, with no connections to Pizza Plus, is now operating and benefitting from those refurbished premises. While there is little prospect of the loan being repaid, it can be argued the investment by the Council has indirectly led to the original job creation targets being met and indeed exceeded by the creation of the second business. The Crazy Castle continues to operate and pay the loan as scheduled.

The actual uptake of ESIF loans in Angus, and a number of other local authority areas, has been less than anticipated. Most enquiries in Angus have not proceeded either because it was not possible to secure the 50% match funding or it has been decided not to proceed with the investment project. There is also anecdotal evidence to suggest a number of businesses are still wary of taking on borrowing and they remain nervous of market conditions. Also, at times there are perhaps more attractive finance alternatives available.

4.3 Some Other Non-bank Finance Options Available to Angus Companies

Businesses within approximately an 18 mile radius of the Michelin factory in Dundee (taking in Arbroath, Carnoustie and Forfar) can apply for a loan through the [Michelin Development Fund](#). The eligibility criteria and value of the loans on offer are somewhat similar to the ESIF. However, loans are normally offered at the Bank of England base rate (currently 0.5%). Over the last 3 years, 4 Angus companies have drawn down loans from the Michelin Development Fund.

More recently there has been the launch of the [Start Up Loan Company](#) in Scotland. This is a UK Government initiative offering personal loans of up to £25,000 to individuals who are about to or have recently started a new business. The interest rate is 6% and the average loan in England, where the scheme has been operating for longer, is £6,000.

There are also grant schemes either currently available, or previously available, to Angus companies. These include [Regional Selective Assistance](#), the [Marketing Development Scheme](#) (for food processing related projects) and the [Scottish Rural Development Programme](#). Clearly a non-repayable grant, where it is available, is much more favourable than any business loan. However, it is not uncommon for officers to introduce a cocktail of grant funding and loan finance to businesses.

5. OPTIONS

5.1 There is a proposal, supported by the Scottish Government, for Scottish local authorities to create a NLF offering loans to businesses. This would see the closure of the ESIF (10 local authority partners) and its sister organisation the West of Scotland Loan Fund (WSLF - 12 local authority partners). It has been agreed by the Scottish Government that the NLF can bid for financial support from the 2014 - 2020 ERDF programme. From officer discussions, the indications are that the majority, if not all, Scottish local authorities will agree to become a Member of the proposed NLF.

5.2 Given the proposed creation of the NLF, the options open to Angus Council are:

- (i) Agree to the closure of the ESIF, become a member of the NLF and transfer remaining ESIF assets into the new fund. This is the recommended option that is proposed in paragraph 6.
- (ii) Agree to the closure of the ESIF and transfer Angus Council funds to a new Angus Loan Fund that would need to be created. While this would give more local autonomy it would not be possible to attract ERDF match funding support, thus reducing the amount of any potential loan finance available to local companies.
- (iii) Agree Angus Council withdraw from ESIF and any monies remaining be returned to the Council for alternate uses. However, given the European funding involved, a relatively long loan outstanding (The Crazy Castle Play Centre), the members' Agreement and the Articles of Association it could prove very difficult and therefore is not recommended.

- (iv) Seek support from other members to continue the operation of the ESIF. There does not appear to be any support for this option and as with option (ii) there would be no capacity to attract ERDF support going forward.

6. PROPOSALS

- 6.1 To take forward a Scottish wide NLF, it will be necessary for the vast majority of Scottish local authorities to agree to and support this initiative. Discussions are well advanced and draft documents comprising a 'Members' Agreement', 'Articles of Association', a prospectus, operating procedures and a business plan have recently been distributed for comment. Officers are currently reviewing these papers and subject to agreement of these, it is recommended that Angus Council become a member of the NLF. It is proposed that the NLF will operate similarly to the ESIF and the WSLF. Angus Council along with all other participating local authorities will become members of the new loan fund company. It will not be practical for every local authority to be represented on the Board, however each authority will be represented on one of the three proposed regional sub-groups covering the East, the West and Highlands and Islands. Representatives on these groups will nominate Board members from their respective areas. As with the ESIF, Angus Council will retain the right to approve or reject loans and funds will be ring fenced for local authority area.
- 6.2 Currently the maximum loan from the ESIF available to Angus companies is £30,000. To provide more flexibility, officers are recommending that the maximum loan on offer from the NLF available to Angus companies be set at £50,000, although it is anticipated most loans offered will be for a lesser amount.
- 6.3 It is proposed that the Service Manager – Economic Development in consultation with the Convener of Development and Enterprise, or the Depute Convener in her absence, be delegated to approve all loans offered to Angus businesses through the NLF.
- 6.4 Given the proposed NLF, consideration needs to be given to the future of the ESIF. It was first thought that the existing funds within the ESIF and the portfolio of loans outstanding would transfer to the NLF with ESIF then being closed. However, after due consideration it is proposed that:
- the ESIF offers no further loans once the NLF is operational.
 - the funds held within the ESIF at that time transfer to the NLF (with individual authorities retaining ring fenced contributions).
 - the portfolio of loans held by the ESIF remain with the ESIF and on an annual basis, or more regularly if appropriate, the income from loan repayments are transferred to the NLF.
 - after all of the ESIF loans are repaid and the final loan repayments are transferred into the NLF, the ESIF will close.
- 6.5 The key arguments for proceeding on this basis are (i) it avoids the 'mixing' of ERDF programmes, thus leaving a clear audit trail and avoiding putting any European funding in jeopardy and (ii) those local authorities that are not currently Members of the ESIF will not have any concerns over any contingent liabilities the ESIF may have being transferred to the NLF (not that any are foreseen).
- 6.6 As mentioned previously in this report, the NLF has the opportunity to draw down additional monies from ERDF. However, the match funding from local authorities must be 'new' monies e.g. new contributions or recycled monies (income from loan repayments). To maximise the potential to access ERDF and offer more Angus businesses the opportunity to benefit from the NLF, it is recommended that the Committee approve the allocation of an additional £50,000 into the NLF.
- 6.7 With the implementation of the NLF and an increased amount of funding available to Angus businesses, more pro-active promotion of the fund will be undertaken with increased marketing.

7. FINANCIAL IMPLICATIONS

7.1 The direct financial implication associated with this report is the recommendation to allocate £50,000 of new money to the NLF. This amount can be met from the 2014/15 Economic Development revenue budget and it is anticipated the transfer of funds will take place before 31 March 2015 (but after the NLF is established). To cover the possibility of a delay in the formation of the NLF and the transfer of money beyond 31 March 2015 a carry forward request will be made to carry forward the £50,000 into the 2015/16 revenue budget. The exact level of ERDF funding this contribution will attract is not currently known but it could potentially attract up to £40,000. This would mean the total amount in the NLF for Angus companies could be up to £90,000 of 'new' money plus the current balance in the ESIF of £42,832 (total £132,832).

7.2 For information, the following is a summary of ESIF financial transactions relating to Angus:

up to 30 September 2014	£
Contribution (from the Angus Loan Fund)	50,000
Funding from ERDF	40,486
Total funds available to Angus businesses	90,486
<u>Less</u> 2 loans issued (1 @ £25,000 and 1 @ £30,000)	55,000
<u>Plus</u> loan repayments	7,346
Current Balance (available for transfer to the NLF)	£42,832

7.3 There is also an annual fund management charge associated with the NLF and Angus Council's estimated share of this is 3%, approx. £3,250. This amount can be met from the Economic Development revenue budget for the three year period.

RICHARD STIFF
CHIEF EXECUTIVE

NOTE: The background papers, as defined by Section 50D of the Local Government (Scotland) Act 1973 (other than any containing confidential or exempt information) which were relied on to any material extent in preparing the above report are:

- Article 15 of the minute of the meeting of the Infrastructure Services Committee of 13 October 2009.
- Article 15 of the minute of the meeting of the Infrastructure Services Committee of 14 June 2012.
- Article 6 of the minute of the meeting of the Infrastructure Services Committee of 9 October 2012.

REPORT AUTHOR Alison Smith, Service Manager – Economic Development
Email:smithaj@angus.gov.uk