

Creation of a Pan Scotland Local Authority Business Loan Fund – Progress Update

Report by Ian Johnson, Head of Communities and Economy

1 Purpose of Report

- 1.1** The purpose of this report is to provide an update on progress with the proposed creation of a Pan Scotland Local Authority Business Loan Fund and to outline the course of action that has been taken, to date, in terms of Midlothian Council's proposed participation in the new Loan Fund.

2 Background

- 2.1** At its meeting on 3 March 2015, Cabinet considered and approved the content of a report entitled 'Proposed Creation of a Scottish Local Authority Business Loan Fund'.
- 2.2** The report highlighted that since Autumn 2014, detailed discussions have been underway at national level to create a Pan Scotland Local Authority Business Loan Fund modelled on the successful East of Scotland Investment Fund (ESIF) and the West of Scotland Loan Fund (WSLF). These discussions have involved representatives from the Scottish Local Authorities Economic Development Group, the Scottish Government and the Fund Managers for ESIF and the WSLF. A collective bid from Scottish Local Authorities has been actively encouraged by the Scottish Government. The initial aim was to have the new Fund operational from April 2015, with lending commencing around July 2015. Unfortunately a time lag has been encountered during the setting up process due to delays regarding the availability of European Structural Funds support and the Scottish Government tendering process. It is now unlikely that the Loan Fund will be open for business until early July 2016, at the earliest.
- 2.3** The proposed new Scotland wide fund will build on the existing East of Scotland and West of Scotland Loan Funds. Midlothian Council has been involved in ESIF since its inception in 2010. ESIF comprises nine Councils which have worked together to provide loan finance to new and growing businesses within the East of Scotland. The Council's Economic Development Manager has served as a member of the ESIF Board and also it's Corporate Working Group.
- 2.4** The West of Scotland Loan Fund has operated since 1996 and together with ESIF, these Funds have made a substantial contribution to economic development and business support / growth in East and West Scotland in line with national, regional and local strategies.
- 2.5** The current state of play with the establishment of the new Fund is that on 5 January 2016, the tender for the "Fund Managers Service for the Scottish Government" was published in the Official Journal of the European Union (OJEU) and on the Scottish Government's Public Contracts Scotland website. The Scottish Government is seeking to competitively select up to six organisations to become Fund Managers, with at least one Fund Manager for microfinance, at least one for debt finance and at

least one for early stage equity. Business Loans Scotland is targeting the debt finance strand. The Scottish Government held an Open Day on the procurement process on 15 January 2016 and on 3 February 2016 a Pre Qualification Questionnaire (PQQ) was submitted to the Scottish Government by Business Loans Scotland. On 11 March 2016, the Scottish Government advised that Business Loans Scotland had been successful in qualifying from the PQQ stage of the Fund Managers Service. The tender was released on 21 April 2016 with a closing date of 26 May 2016. Subject to a successful tender, the Fund has a potential start date of 01 July 2016 running until 31 December 2018, a timescale of 30 months to deliver the full value of the Fund.

- 2.6 Once fully established and operational, the Scottish Local Authority Business Loans Fund Limited will be a consortium of Scotland's 32 Local Authorities, incorporated as a company limited by guarantee and providing loan finance of up to £100,000 to new and growing small and medium sized enterprises across Scotland.
- 2.7 Details of the proposed operation of the new Loan Fund, a draft Business Plan 2015-18 and a Members Agreement in respect of the operation of the new Fund have been placed in the Members' Library. It should be noted that the documentation is subject to ongoing review and refinement prior to the launch of the new Fund.
- 2.8 Key points to note from the new Fund documentation include:
 - a new company, limited by guarantee, has been incorporated in December 2014 with the name Scottish Local Authority Business Loan Fund, with the option to trade as Business Loans Scotland.
 - a Members Agreement and new Articles of Association have been drafted for adoption by the new company. These documents will regulate the running of the new company. Copies of the documentation have been scrutinised and approved by staff in the Council's Legal Section.
 - the existing business and assets of the West of Scotland Loan Fund and the East of Scotland Investment Fund will be transferred to the new company.
 - any cash contained within the West of Scotland Loan Fund and the East of Scotland Investment Fund, together with monies received from debtors in these companies will be transferred to the new company. **It is emphasised that monies allocated to a Local Authority will be held exclusively for that Local Authority. Additional funds are not being requested from the Council for Business Loans Scotland;**
 - the new Loan Fund is seeking to benefit from an award of circa £ 6 million from the European Regional Development Fund. Matched with funding from a Bank Term Loan (to be advised) of circa £ 4.5 million and financial contributions from Member Authorities totalling circa £4.5 million, a Loan Fund of circa £15 million will be created to be invested over a contract length period to 31 December 2018. Annually, the Fund will have the capacity to invest circa £5.5 million, support circa 150 businesses and help create over 600 new jobs;
 - the Fund and its Local Authority members will operate across three regional delivery areas covering the whole of Scotland. These are East, West, and Highlands and Islands areas; and

- the Fund's governance structure will consist of five elements:
 - i) The Board of Directors.
 - ii) Corporate Governance Working Group.
 - iii) Regional Management Group.
 - iv) Regional Investment Panels.
 - v) Regional Officers Groups.

The Council's Economic Development Manager represented the Council at a meeting of the Business Loans Scotland Regional Management Group on 21 April 2016. Four Director nominations were sought to cover the undernoted East of Scotland areas:

- Fife
- Edinburgh and the Lothians
- Forth Valley
- Aberdeen / Angus / Dundee / Perth and Kinross

It is likely that Edinburgh and Lothians will be represented by an Elected Member or Senior Officer from The City of Edinburgh Council. With regard to Midlothian Council involvement in the governance arrangements for Business Loans Scotland, it is recommended that the Council's Economic Development Manager represents the Council on the Regional Management Group, the appropriate Regional Investment Panel(s) and the appropriate Regional Officer Group(s).

- 2.9** As is the current practice with ESIF applications made to the Council, the initial Business Loans Scotland application appraisal will be undertaken by suitably trained / briefed Business Gateway staff members from this Council's Economic Development Section. An appropriate report will be prepared for Cabinet recommending approval or rejection of the loan application. In line with the Fund's (draft) Articles of Association and Members Agreement, final decisions for loans between £50,000 and £100,000 will be the responsibility of the (to be formed) Regional Investment Panels.
- 2.10** The new Fund will use a web based online loan application system, allowing loan applications, appraisals, compliance checking, approval, drawdown, customer care and monitoring to be undertaken online. Appropriate staff training will be required, in due course, to effectively utilise these systems.

3 Report Implications

3.1 Resource

In terms of human resource implications, participation in the new Fund will be undertaken by Economic Development Section staff, particularly those staff working on Business Gateway issues, in close liaison with Council officer colleagues and the managing body for the new Fund. Business Gateway staff will be involved in loan application appraisal and monitoring.

In addition, it is recommended that the Council be represented by the Economic Development Manager on the undernoted Business Loans Scotland governance groups:

- Regional Management Group
- Regional Investment Panel(s)
- Regional Officer Group(s)

With regard to financial resource implications, the (draft) Business Plan 2015-18 for the new Local Fund highlighted an ambition to put in place an overall Fund of circa £18 million. This figure has been revised downwards, due to delays in setting up the Fund which has reduced the effective operating period to around two and a half years, to circa £15 million and comprises:

- Circa £6 million European Regional Development Fund support;
- Circa £4.5 million Bank Term Loan (to be advised) funding support; and
- Circa £4.5 million Member Authorities funding support.

It is anticipated that each Council will transfer the balance from its current business loan accounts into the new Fund. For Midlothian this would comprise funds currently held in its East of Scotland Investment Fund. Figures highlighted in the Members Agreement, recently prepared by Wright, Johnston and Mackenzie (Solicitors) on behalf of Business Loans Scotland show that Midlothian's anticipated size of Fund is likely to be circa £485,000. This sum includes a Midlothian ESIF balance transfer of circa £145,500 to Business Loans Scotland. The Midlothian balance will be further topped up with a share of European Regional Development Fund support amounting to circa £194,000 and a share of Bank Term Loan funding. Once a contribution has been made towards the overheads incurred in running Business Loans Scotland, it is anticipated that the net amount available for lending in Midlothian will be circa £447,000. It should be noted that these figures are very much indicative at this stage and may well be subject to change. However, they provide a guide as to what sum is likely to be available for future Business Loan Scotland lending in Midlothian. Indicative loan targets have also been set out for Midlothian in the Members Agreement and these are as follows:

- 2016 - £ 89,361
- 2017 - £ 178,723
- 2018 - £ 178,723

It should be noted that these are very much indicative figures at this stage and may well change.

3.2 Risk

There is a risk that the Council's failure to participate in the new Loan Fund will reduce the potential access to loan funding to enable Midlothian based businesses to develop and grow. Midlothian Council's participation in ESIF has been active since December 2010.

In any loan scheme of this nature, there is an inherent risk that businesses will default on loan payments. This risk will be mitigated by rigorous credit checks, due diligence controls, the taking of appropriate security and regular after care monitoring visits. The (draft) Business Plan for the new Fund proposes the implementation of a debt management policy with the aim of acting swiftly to safeguard the interests of the Fund.

There is also a relatively low risk that Business Loans Scotland will not come into operation if the tender for the work is lost. If that eventuality did occur then the ESIF and WSLF Boards would have to reconvene to consider an alternative course of action. One option might be the continuation, in some shape or form, of both Loan Funds.

3.3 Single Midlothian Plan and Business Transformation

Themes addressed in this report:

- ☐ Community safety
- ☐ Adult health, care and housing
- ☐ Getting it right for every Midlothian child
- ☒ Improving opportunities in Midlothian
- ☒ Sustainable growth
- ☒ Business transformation and Best Value
- ☐ None of the above

3.4 Impact on Performance and Outcomes

A supportive business environment is a strategic priority highlighted in the Scottish Government's Economic Strategy. The Strategy includes the provision of advice and support to help small and medium sized enterprises grow. This supports Ambitious Midlothian (Midlothian Economic Recovery Plan) and the Single Midlothian Plan 2016/17 by contributing to economic growth and business support within Midlothian.

3.5 Adopting a Preventative Approach

In assisting businesses to grow, the new Loan Fund may save the business from ceasing to trade and may, as a consequence, safeguard jobs as well as create them.

3.6 Involving Communities and Other Stakeholders

Appropriate consultation has been undertaken with other Council staff during the preparation of this report. Once the new Loan Fund is operational, staff from the Fund management body will be fully consulted throughout the application process and be fully advised of caseload developments.

3.7 Ensuring Equalities

Appropriate checks will be undertaken to ensure that applicants comply with employment legislation.

3.8 Supporting Sustainable Development

All businesses participating in the new Loan Fund will be informed about services to enable their uptake of good environmental practice. This has been standard practice during the operation of ESIF. Relevant schemes include the Green Ticks scheme operated by the Business Partnership. The proposed funding model for the new Loan Fund consists of investment in the Fund by Member Authorities, a Bank Term Loan (to be advised) and the European Regional Development Fund. The proposed revolving nature of the new Fund, consisting of capital and interest loan repayments, will help to ensure its sustainability as successive generations of borrowers meet their debt obligations to the Fund.

3.9 IT Issues

There are no IT issues although it should be noted that it is planned that the new Fund will use a web based online loan application system. It is not anticipated that this will pose any problems from an IT perspective.

4 Recommendations

4.1 It is recommended that Cabinet:

- notes progress with the proposed establishment of a Pan Scotland Local Authority Business Loan Fund;
- agrees that the Council continues to fully participate in the proposed establishment of a Pan Scotland Local Authority Business Loan Fund;
- agrees that the Council's Economic Development Manager represents the Council's project governance interests on the Business Loan Fund Regional Management Group, appropriate Regional Investment Panel(s) and appropriate Regional Officer Group(s).
- approves, at the appropriate time, transfer of existing balances in the East of Scotland Investment Fund account, and the Midlothian Business Loan account, to the new Pan Scotland Local Authority Business Loan Fund; and
- requires that further progress reports be submitted to Cabinet to advise on the establishment, development and operation of the proposed new Pan Scotland Local Authority Business Loan Fund.

4 May 2016

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Background Papers:

Scottish Local Authorities Business Loan Fund