

Business Loans Scotland Ltd (previously named Scottish Local Authority Business Loan Fund)

1.0 EXECUTIVE SUMMARY

- 1.1 The Policy & Resources Committee has agreed in principle to support the creation of a Scotland wide local authority loan fund, proposed as the Scottish Local Authority Business Loan Fund (SLABLF), now renamed Business Loans Scotland Ltd (BLS).
- 1.2 Via the Policy & Resources Committee 19th March 2015 members:
- a) endorsed the proposal to join SLABLF;
 - b) approved the proposed transfer all existing West of Scotland Loan Fund (WSLF) monies allocated to Argyll and Bute (at that date, £183,702), to SLABLF; and
 - c) endorsed the estimated demand for SLABLF loans over the initial three year period at £300,000 for Argyll and Bute.
- 1.3 The endorsed estimated loan demand of £300,000 will require a £100,000 contribution from the Council, including management charges estimated at £10,000. The Council contribution can be made via the transfer of funds from WSLF, therefore no additional Council funds were requested last year, nor are additional funds being requested now.
- 1.4 Whilst the core proposal for BLS remains the same, since the Policy & Resources Committee approval last year, there have been some proposed changes to operations, which require consideration and approval by committee members as they involve policy and resources. The changes relate to:
- Whether BLS will conduct regulated consumer credit lending activities or not. This has implications on whether BLS would be able to offer loans of under £25k to Sole Traders and Partnerships with fewer than four members; and/or
 - Whether the Council wishes to transfer all funds held by WSLF and allocated to Argyll and Bute into BLS, or wishes to seek to transfer any potential surplus to “like-minded” organisations for the purpose of ‘providing financial assistance to promote commerce’.
- 1.5 Specifically the Policy & Resources Committee is being asked to confirm:
- Does Argyll and Bute Council require BLS to be able to provide loans of less than £25k to Sole Traders and Partnerships with fewer than four members?;
 - If yes, is Argyll and Bute Council willing to nominate an individual to become an Approved Person (as defined by the Financial Conduct Authority) and Director of BLS?;
 - Is Argyll and Bute Council’s decision to join BLS dependent on the Fund being able to lend to Sole Traders and Partnerships?;
 - Does Argyll and Bute Council wish to transfer all of their WSLF “property” (currently cash of £184,016) to BLS?;

- If no, would the Council seek to transfer any “surplus” cash (after the Council membership contribution has been paid) to “like minded” organisation(s), for the purpose of providing financial assistance to promote commerce? If the Council wants to transfer any surplus to its Economic Development Service (if deemed a “like-minded” organisation), this may be possible but WSLF legal advice is that unanimous approval of the Member Authorities will be required; and
- Does Argyll and Bute Council wish to pay the estimated management fees of 3% per year up front from the WSLF contribution, taking the fees from the initial contribution, or be invoiced year-on-year?

1.6 It is recommended that the Policy & Resources Committee:

- Endorses the proposal to join BLS without BLS conducting consumer lending;
- Endorses the proposal to transfer the minimum Council contribution (£90k) from WSLF to BLS;
- Endorses the proposal to pay BLS management charges upfront for the first three years (estimated at £10k total) by transfer of funds from WSLF; and
- Endorses the proposal to seek to transfer any WSLF surplus to the Council’s Economic Development Service, or other appropriate body able to provide loans, for the purposes of promoting commerce by giving financial assistance by way of loans, donations or subscriptions, noting that this may require the unanimous approval of all WSLF Member Authorities.

Business Loans Scotland Ltd (previously named Scottish Local Authority Business Loan Fund)

2.0 INTRODUCTION

- 2.1 An opportunity exists to create a pan Scotland local authority loan fund modelled on the successful West of Scotland Loan Fund (WSLF) and East of Scotland Investment Fund (ESIF). A pan Scotland Loan Fund is eligible to secure ERDF funding from the next European Structural Funds Programme 2014-2020. A collective bid from Scottish Local Government is actively being encouraged by Scottish Government.
- 2.2 The BLS proposal is being led by the West of Scotland Loan Fund (WSLF), of which Argyll and Bute Council is already a member, in partnership with the East of Scotland Investment Fund (ESIF).
- 2.3 The proposal is to merge both WSLF and ESIF into the new national BLS.
- 2.4 As of 28th September 2015, 25 local authorities, including Argyll and Bute, have confirmed their commitment to participate in BLS.
- 2.5 Plans are now progressing to create BLS and plan the winding up/dissolution of WSLF.
- 2.6 As planning of this change progresses, issues regarding the detailed operations of BLS have emerged that were not identified last year when the Policy & Resources Committee agreed to join the new fund.
- 2.7 The proposed changes to operations require Policy & Resources Committee members' consideration and approval. The changes relate to:
- Whether BLS will conduct regulated consumer credit lending activities or not. This has implications on whether BLS would be able to offer loans of under £25k to Sole Traders and Partnerships with fewer than four members; and/or
 - Whether the Council wishes to transfer all funds held by WSLF and allocated to Argyll and Bute into BLS, or wishes to seek to transfer any surplus to "like-minded" organisations for the purpose of providing financial assistance to promote commerce.

- 2.8 Specifically the Policy & Resources Committee is being asked to confirm:
- Does Argyll and Bute Council require BLS to be able to provide loans of less than £25k to Sole Traders and Partnerships with fewer than four members?;
 - If yes, is Argyll and Bute Council willing to nominate an individual to become an Approved Person (as defined by the Financial Conduct Authority) and Director of BLS?;
 - Is Argyll and Bute Council's decision to join BLS dependent on the Fund being able to lend loans of <£25k to Sole Traders and Partnerships with fewer than four members?;
 - Does Argyll and Bute Council wish to transfer all of their WSLF "property" (currently cash of £184,016) to BLS?;
 - If no, would the Council seek to transfer any "surplus" cash (after the Council membership contribution has been paid) to "like minded" organisation(s), for the purpose of providing financial assistance to promote commerce? If the Council wants to transfer any surplus to its Economic Development Service (if deemed a "like-minded" organisation), this may be possible but WSLF legal advice is that unanimous approval of the Member Authorities will be required; and
 - Does Argyll and Bute Council wish to pay the estimated management fees of 3% per year up front from the WSLF contribution, or reduce its contribution and be invoiced year-on-year?

3.0 RECOMMENDATIONS

It is recommended that the Policy & Resources Committee:

- 3.1 Endorses the proposal to join BLS without BLS conducting consumer lending.
- 3.2 Endorses the proposal to transfer the minimum Council contribution (£90k) from WSLF to BLS.
- 3.3 Endorses the proposal to transfer £10k from WSLF to BLS to cover BLS management charges for the first three years (estimated at 3% per year).
- 3.4 Endorses the proposal to seek to transfer any WSLF surplus to the Council's Economic Development Service, or other appropriate body able to provide loans, for the purposes of promoting commerce by giving financial assistance by way of loans, donations or subscriptions, noting that this may require the unanimous approval of all WSLF Member Authorities.

4.0 DETAILS

The provision of regulated consumer credit lending

- 4.1 The provision of small loans (under £25k) to Sole Traders and Partnerships is now deemed consumer credit lending regulated by the Financial Conduct Authority (FCA). Conducting this type of regulated lending requires a Consumer Credit License, ongoing annual compliance costs and that key staff become Approved Persons under the FCA regime. Additional costs will be incurred to obtain a FCA licence namely; application fee, compliance fees and compliance manual estimated to be in the region of £10,000. There will be an annual recurring cost to maintain the FCA licence, the compliance manual and six-monthly monitoring visits, estimated to be in the region of £6,000.

4.2 Individuals required to become Approved Persons include Directors and staff with FCA compliance oversight, money laundering, systems and controls and significant management functions. Once a person has become an Approved Person, they are effectively individually regulated by the FCA and are therefore personally accountable to the Regulator. This has implications for the standards of conduct Approved Persons are expected to maintain and the disciplinary action that the Regulator can take against them.

Each person required to become an Approved Person will need to apply to the FCA, who in turn will determine if that person meet their rules on fitness and propriety which are set out in the Fit and Proper Test for Approved Persons. The most important considerations are; honesty, integrity and reputation, competence and capability and financial soundness.

4.3 If BLS were to conduct regulated lending, all Directors of BLS including the representative for Argyll and Bute Council will need to be approved by the FCA to become an Approved Person and be fully aware of the personal responsibility they are undertaking. Approved Persons would be accountable and responsible for the actions of all Member Authorities, not just their own, and are responsible for ensuring BLS meets its regulatory obligations.

4.4 At the October 2015 WSLF Board Meeting consideration was given to whether BLS should offer regulated lending given the added cost, administrative burden and requirement for all Directors of the new company to become Approved Persons.

After being briefed on the responsibilities of an Approved Person, WSLF Directors were not unanimously willing to become Approved Persons. The key concerns arising were;

- Elected Members/Directors rely on the competence and capability of Officers doing their job properly to be compliant with FCA regime
- Certain skills lie with Officers rather than Directors
- Directors are responsible and accountable for actions of the company
- Directors must represent the company first as opposed to their local authority Member
- Sanctions can be against the individual Approved Person for non-compliance with FCA regime

4.5 The decision taken by the Board was that WSLF and BLS will not offer this type of regulated consumer lending. Subsequently WSLF exited this type of lending and transferred the administration and collection of existing loans of this type to an authorised agency, DSL Business Finance.

4.6 As the Policy & Resources Committee approved the recommendation to join BLS before this exclusion was agreed, committee members' approval is now required to support membership of BLS on the new terms. Specifically the Policy & Resources Committee is being asked to confirm:

- Does Argyll and Bute Council require BLS to be able to provide loans of less than £25k to Sole Traders and Partnerships with fewer than four members in our area?
- If yes, is Argyll and Bute Council willing to nominate an individual to become an Approved Person and Director of BLS? and

- Is Argyll and Bute Council's decision to join BLS dependent on the Fund being able to lend to Sole Traders and small Partnerships?

4.7 Since 1st April 2009, WSLF and ESIF have invested £787,625 in 39 sole traders or partnerships with three or fewer partners to date. This equates to 8% by number of loans issued and 6% by value for WSLF and 12% by number of loans issued and 5% by value for ESIF. When taken into context of for all loans across all of the Members of both funds including unregulated loans, the overall percentage of loans to sole traders and partnerships with three or fewer partners accounts for less than 10% of the activity of both funds. No loans have been made in Argyll and Bute during this period.

4.8 In addition to banks there are other sources of finance available to sole traders and partnerships with three or fewer partners operating across Scotland, including;

- DSL Business Finance www.dsl-businessfinance.co.uk;
- The Prince's Trust www.princes-trust.org.uk; and
- UK Government's Start Up Loans programme www.startuploans.co.uk

The Scottish Government is also looking to set up a pan Scotland micro credit fund in the 2014- 2020 European Programme operating in the range of £1,000 - £25,000, although further details are not yet available.

4.9 DSL Business Finance offers fast and flexible business loans to businesses based in Scotland and is actively lending to businesses based in Argyll and Bute. It is a not-for-profit lender, which specialises in finance for start-up businesses, small to medium-sized businesses and third sector social enterprises. As an ethical lender, any profit made is recycled to allow DSL to lend to more businesses. The three loan areas DSL provide finance in are:

- SMEs - DSL offer Business Loans to enterprise located in Scotland, with loans up to the value of £50,000. There are no age or sectoral restrictions and the loans can be used for many purposes including working capital and vehicles.
- Start-Ups - DSL Business Finance is one of the first Scottish delivery partners for the Start Up Loan Company, a government funded initiative to provide start up support in the form of a repayable loan. DSL Business Finance has produced a dedicated website for start-up businesses New Start Up Scotland.
- Third Sector - Big Issue Invest Scotland (BIIS) is a joint venture between DSL Business Finance and Big Issue Invest. BIIS provides loans of between £5,000 and £1.5 million to socially minded ventures throughout Scotland.

4.10 Given the low uptake of WSLF when loans of <£25k were available to Sole Traders and small Partnerships in Argyll, and the current availability of loan funding to this type of business from DSL Business Finance, the pragmatic recommendation would be to agree to join BLS without conducting regulated consumer lending. This removes the need for Argyll and Bute Council's nominated Director of BLS to become an Approved Person.

The transfer of funds from WSLF to BLS

4.11 As at November 2015, the WSLF allocation for Argyll and Bute stands at:

Cash at bank	£278,345
Investments / Loans	£0
Unspent ERDF	(£94,329)
Net position	£184,016

4.12 Due to delays in the new European Structural Funds programme, WSLF is now expected to remain operational until summer 2016. If no WSLF loan applications are made and approved before BLS becomes operational, the £184,016 currently allocated to Argyll and Bute within WSLF could be transferred.

4.13 Based on an estimated BLS loan demand of £300,000 across the first three years from businesses in Argyll and Bute, the Council would need to make no additional financial contribution to BLS if all the current WSLF funds are transferred, as the £184,016 more than meets the £90,000 minimum contribution required plus £10,000 for management costs.

4.14 In March 2015 the Policy & Resources Committee approved the transfer of all WSLF funds to SLABLF (now BLS) when the new fund is launched.

4.15 Previously it was understood that no WSLF allocation for Argyll and Bute could be transferred to the Council. Whilst the WSLF Articles of Association are clear that on the winding-up or dissolution of WSLF, any “property” cannot be paid or distributed amongst the Member Authorities, recent advice from WSLF is that that Articles of Association of WSLF do permit funds to be transferred to ‘like minded’ organisations.

4.16 WSLF’s solicitors, Wright, Johnston & Mackenzie have been consulted regarding what type of organisations would constitute being “like minded”. Their advice is that such organisations would require to meet the test of being “*trusts, companies, organisations, associations or institutions having objects similar to the objects of the Company (WSLF) and subject to the same or similar restrictions to and which are at least as strict as those contained in Article 4.2 and Article 20*”.

The further provisions in Article 20 describe entities with “objects” similar to WSLF and “subject to the same or similar restrictions to and which are at least as strict as those contained in Article 4.2”. The provisions of Article 4.2 say that the “income and property of the Company are to be used in furtherance of the Company’s objects as set out in Article 4.1”.

The primary objects of the Company at Article 4.1 relate to holding and managing a “fund”, for the purposes of promoting “commerce by giving financial assistance by way of loans, donations or subscriptions” (4.1.1) and also relate to “raising funding for such purposes from the Company’s Members and other entities and sources (including ERDF)”.

4.17 Officers have requested advice from the Council’s legal Service on this matter. The working assumption in the interim, until such advice is received, is that funds may

be transferred into an alternative fund if used to provide financial assistance to promote commerce.

- 4.18 If there is any doubt over whether the Council's Economic Development Service would meet the test of being a "like minded" organisation, then WSLF solicitors advise that the best course of action would be to seek the unanimous approval of the WSLF Member Authorities that this is the case.
- 4.19 An investment target of £300,000 over the first three years of BLF, which requires £90,000 Council contribution, is optimistic based on the historical low demand for WSLF support in Argyll and Bute.
- 4.20 For this reason, rather than moving all monies allocated to Argyll and Bute within WSLF (currently £184,016), it would be prudent to explore whether any surplus can be utilised by the Council, either directly or via an other appropriate body able to provide loans, to provide financial assistance to promote commerce.
- 4.21 It should be noted that if any new WSLF applications are approved before BLS is operational, the funds will be withdrawn from the Argyll and Bute allocation. For example, if loans worth £50,000 were made, the transfer from WSLF would reduce to £134,016. This would reduce any potential surplus to £34,016.
- 4.22 If a large WSLF loan of £100,000 were to be approved before BLS launched, the transfer from WSLF would reduce to £84,016. This would mean no surplus and the Council would need to contribute £6,000 plus management costs to BLS to meet the target fund size, or reduce the size of the loan fund available to Argyll and Bute businesses for the first three years. Based on current demand and application lead times, it is not expected that the WSLF allocation will be significantly reduced before transfer to BLS.
- 4.23 As any new WSLF loans cannot now lever ERDF funding due to the closure of the previous programme, it is understood that some local authorities are considering offering no further WSLF loans prior to the BLS transfer.

Payment of management fees

- 4.24 In addition to the initial Council contribution required of £90,000, membership of BLS creates a requirement for ongoing management fees at an estimated 3% per year of the funds available for lending. For Argyll and Bute Council this would represent a management charge of circa £9,000 over the three years, based on the £300,000 investment target.
- 4.25 The management fees for the first three years can be paid:
- as upfront payment with the original match contribution;
 - yearly by payment of a separate invoice; or
 - by taking the payment upfront from the minimum match contribution and reducing the funds available for lending.
- 4.26 Upfront payment made by adding management costs to the initial match funding is the recommended option. The cost can be met by the transfer of funds from WSLF, so there is no additional budget requirement. This option also permits 40% ERDF funding to be leveraged on the management charge.

- 4.27 Payment by yearly invoice to the Council is not recommended. This would require additional budget of circa £3,000 per year to be found. Management charges cannot leverage ERDF via this route.
- 4.28 Taking the payment upfront from the minimum match contribution is also not recommended at this stage, as this would reduce the size of the lending fund available to businesses. However, this may be the preferred option for payment of management charges after the first three years if actual lending is lower than target.

5.0 CONCLUSION

- 5.1 The Policy & Resources Committee has already agreed in principle to support the creation of a Scotland wide local authority loan fund, proposed as the Scottish Local Authority Business Loan Fund (SLABLF), now renamed Business Loans Scotland Ltd (BLS).
- 5.2 As planning for this change progresses, issues regarding the detailed operation of BLS have emerged that were not identified last year when the Policy & Resources Committee agreed to join the new fund.
- 5.3 Therefore the proposed changes to operations require Policy & Resources Committee members' consideration and approval.
- 5.4 The Policy & Resources Committee is asked to endorse the recommendations of this paper.

6.0 IMPLICATIONS

6.1 Policy Making a local authority loan fund available to businesses across Argyll and Bute will support the Council's overarching Economic Development Action Plan 2013-2018 objective of assisting more businesses to start-up and grow. Furthermore this will align with the SOA Delivery Plans, in particular outcomes one and three.

6.2 Financial It is proposed that £100k of existing WSLF monies would transfer (currently £184,016). This would provide the required £90k Argyll and Bute contribution to SLABLF and cover the first three years management costs. No additional funds are required from the Council.

Seeking to transfer any WSLF surplus to the Council's Economic Development department, or other appropriate body able to provide loans, could, if approval is given by WSLF members, provide the Council with additional resources for the purposes of promoting commerce by giving financial assistance by way of loans, donations or subscriptions.

- 6.3 Legal
- Officers have requested advice from the Council's legal department on the potential to transfer any surplus funds to the Council's Economic Development department. The working assumption in the interim, until such advice is received, is that funds may be transferred into an alternative fund if used to provide financial assistance to promote commerce.
- If there is any doubt over whether the Council's Economic Development department would meet the test of being a "like minded" organisation, then WSLF solicitors advise that the best course of action would be to seek the unanimous approval of the WSLF Member Authorities.
- 6.4 HR
- No additional personnel within the Business Gateway Team are required to support the BLS delivery.
- As the Council is not currently resourced to run an in house loan scheme, options using some other appropriate body able to provide loans will also be considered if any WSLF surplus becomes available.
- 6.5 Equalities
- This will have no adverse impact on key equality groups. BLS will comply with all Equal Opportunities policies and obligations.
- 6.6 Risk
- Due to the operational overlap between the current method of Business Gateway delivery and the proposed BLS delivery, there is limited risk for the Council as it is well placed to support clients seeking funding.
- Legal advice will be considered before any proposed transfer of surplus is completed.
- As the Council is not currently resourced to run an in house loan scheme, options using some other appropriate body able to provide loans will also be considered if any WSLF surplus becomes available.
- 6.7 Customer Services
- Provision of affordable loan finance to businesses will have a positive impact and contribute to an improved customer experience. Clients unable to access BLS funding (Sole Traders and Partnerships with fewer than four members, for loans of <£25k) will be referred to other providers in the market such as DSL Ltd.

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