

Meeting of the Council – 16th April, 2012

Report of the Cabinet

Dudley Business Loan Fund

Purpose of Report

1. To seek approval to invest £500,000, over a two-year period (2012/13 to 2013/14), with Black Country Reinvestment Society (BCRS), to create a local business loan fund to support small businesses in Dudley Borough. This investment will be matched by a further £500,000 of European Regional Development Fund (ERDF) monies to create a business loan fund of £1 million; and
2. To authorise the Director of the Urban Environment and the Director of Corporate Resources, or their nominated representative(s), to enter into negotiations and sign a formal contract with BCRS in consultation with the Cabinet Members for Regeneration and Finance.

Background

3. Access to finance continues to be a barrier to growth for businesses and remains a priority at both a national and local level. In July 2010, the Department for Business, Innovation and Skills (BIS) published 'A Strategy for Sustainable Growth' which stressed the importance of access to finance: "*There is a key role for government to play in facilitating credit availability for viable small businesses as well as developing non-bank lending channels to enable more businesses to obtain financing from a greater variety of sources*". At a local level, improving access to finance is an agreed priority of the Black Country Local Enterprise Partnership (LEP) and led by the LEP Access to Finance Group. Furthermore, the Dudley Borough Business Survey (2011) found that the economic climate, in particular the lack of available credit from banks, was cited as a principal factor why business performance had deteriorated over the previous 12 months.
4. BCRS was established in 2002 as an Industrial and Provident Society initially to provide Community Development Finance Institution (CDFI)-style finance to social enterprises and small and medium enterprises (SMEs) in the Black Country. It is formally constituted as a CDFI and currently provides small business loans ranging from £10,000 to £50,000. In 2009, BCRS lent £1.4 million and its total loan book exceeded £2 million; cumulatively, since 2002, BCRS has issued over £6 million worth of loans. Whilst BCRS has moved from a social enterprise emphasis towards a more SME focussed strategy it continues to offer a full range of CDFI products. In April 2011, BCRS was part of a national consortium, led by the Community Development Finance Association (CDFA), in securing £30 million of Regional Growth Fund (Round 1) funding.

More recently, in February 2012, BCRS was one of four lenders across the country to be accredited to offer loans to small business under the Enterprise Finance Guarantee (EFG) scheme.

5. It is proposed that the investment sum will be drawn down on a phased basis by BCRS and agreed in advance. Based on experience of similar schemes with neighbouring authorities it is realistic to expect 70% of any investment to be returned. BCRS would guarantee that the Council will receive back 70% of its investment, even if there is a higher bad debt rate. If BCRS achieves a lower bad debt rate, it will retain the difference for reinvestment as additional business loans within the Dudley Borough. However, in light of BCRS' recent EFG accreditation status (announced in February 2012) the Council, as part of negotiating the terms of a formal contract with BCRS, would seek to negotiate a lower bad debt percentage.
6. The combined £1 million fund, ring-fenced for local businesses located in Dudley Borough, will be lent at commercial rates to improve access to finance for working capital purposes. The fund would be administered by BCRS. Key performance indicators will be monitored by BCRS and the Council on a monthly basis and will include the total amount of loans to local businesses, jobs created/safeguarded, new businesses created, number of businesses supported, new businesses surviving at 12 months, number of black and minority ethnic (BME) businesses supported and number of women-led businesses supported. BCRS has confirmed additional project outputs can be included in the contract, if appropriate. Based on current loan allocations in other areas it is expected that the Dudley Business Loan Fund could potentially support up to 40 local businesses, create up to 30 jobs and safeguard 60.
7. BCRS will provide reports to the Council on the scale and nature of loan enquiries, rejections and approvals, as well as actual and projected outputs from the scheme. The Council will work closely with BCRS to ensure there is a mutually effective enquiry referral process. BCRS would take full responsibility for the appraisal of all eligible applications, including an assessment of the financial health of the business and the strengths of its future business proposals, to minimise the risk of lending to borrowers likely to default.
8. In terms of marketing the Fund, the Council would receive recognition through co-ordinated publicity for the launch of its funding (March 2012) and via the promotion of individual loans made to successful applicants.
9. Currently, no alternative CDFI loan providers offering finance up to £50,000 to existing SMEs are operating in Dudley Borough. The option of developing an in-house loan scheme has been discounted as the Council is not regulated by the Financial Services Authority (FSA) and lacks the specific expertise to operate a scheme directly.
10. On consideration of the above, the Cabinet, at its meeting held on 14th March, 2012, resolved to recommend the Council to approve the proposals set out in paragraph 15 below.

Finance

11. The Council's £500,000 investment into this scheme will be financed by funds available through the New Homes Bonus. This investment will be matched by a further £500,000 of ERDF monies, creating a business loan fund of £1million. Contract negotiations with BCRS will need to be undertaken in light of BCRS' recent EFG accreditation status and what appropriate proportion of the Council's investment should now be returned through loan fund repayments (refer to paragraph 5). Consideration will also need to be given to a reasonable frequency of loan repayments to the Council. An initial financial appraisal of BCRS has been undertaken.

Law

12. The Local Government Act 2000 empowers a local authority to take action to promote the economic, social and environmental well being of its area, including provision of financial support to individuals and organisations, on the condition that such support is not prohibited by other legislation. The agreement between the Council and BCRS would be via a formal contract document incorporating the Council's standard terms of business.
13. ERDF funding requires that the interest rate levied on loans be in excess of a specified threshold rate, which varies over time. BCRS would charge commercially appropriate interest rates set in each particular circumstance and this addresses potential State Aid issues. Specific sectors are prevented by the de-minimis rules from receiving support (fisheries and agriculture, coal and acquisition of road freight vehicles). Further ERDF restrictions include house building, retail, steel and synthetic fibres. BCRS would be responsible for clarifying eligibility and filtering non-eligible applications and liable for any ERDF clawback.

Equality Impact

14. The business loan fund would operate Borough-wide and would be open to all small businesses that have previously been refused finance from a bank. BCRS will appraise all applications on a case-by-case basis.

Recommendations

15. That the Council be recommended:-
 - That an investment of £500,000, over a two-year period (2012/13 to 2013/14), be made to BCRS, to create a local business loan fund to support small businesses in Dudley Borough and that this investment be matched by a further £500,000 of European Regional Development Fund (ERDF) monies to create a business loan fund of £1 million.
 - That the Director of the Urban Environment and Director of Corporate Resources, or their nominated representative(s), be authorised to enter into negotiations and sign a formal contract with BCRS in consultation with the Cabinet Members for Regeneration and Finance.

- That the capital element of the investment be included in the Capital Programme.

A handwritten signature in black ink, appearing to be 'L. Smith', written over a light blue rectangular background.

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Leader of the Council