

Aug 10 2016

Dear XXXXXXXXXX

Objection to Wirral County Council's 2015/16 Annual Accounts on LOBO Loan borrowing

As an elector of Wirral Council, I wish to lodge an [objection to the accounts prepared for public inspection by the Council for the year 2015-2016](#). I request that you prepare a public interest report and apply to the courts for a declaration that items of the accounts, namely "Lender Option, Borrower Option" (LOBO) loan borrowing (reported in note 17), is unlawful.

The term 'unlawful' applies in this context, I believe, because the decision to sign up to so many (19 LOBO) loans was unreasonable and irrational.

In July 2015, LOBO loan borrowing was subject to a C4 Dispatches documentary: "How Councils blow your millions", is the subject of a Parliamentary Inquiry by the Communities and Local Government Committee and possibly of an investigation by the Treasury Select Committee.

The potential costs and derivatives risks of the LOBO loan contracts were not, and could not, be fully understood by council officers, and the type and volume of borrowing carries such a high risk as to be prejudicial to the interests of Wirral Council taxpayers.

Due to the complexity and "optionality" of the contracts, the overall interest rate of the loans would have been impossible to price over the long term, without sophisticated pricing tools that the majority of Local Authorities do not have direct access to.

As ex-Barclays Capital employee XXXXXXXXXX stated: "You just need a Bermudan swaption pricer to know the relevant volatility surface, some kind of interest rate model calibrated to the appropriate processes and the full forward and spot curve." - not the things the average council finance department has to hand.

LOBO loans contain [derivatives, which in some cases have similar properties to interest rate swaps declared ultra-vires or illegal for use by UK local government following the landmark 1989 Hammersmith and Fulham case](#). The legality of LOBO loans remains untested in a UK court of law.

Wirral City Council borrowed approximately £155 million in LOBO loans (refer to Note 17 of the accounts) Barclays, Bank of Scotland and other banks.

LOBO (Lender Option Borrower Option) loans are typically very long-term loans with a maturity of around 50-70 years duration, benchmarked to the LIBOR interest rate, systematically rigged by Barclays, RBS and a cartel of 16 global banks.

Making such a large borrowing commitment under the conditions which the banks imposed, without benchmarking and recording the decisions against comparable PWLB loans amounts to "irrational" conduct.

Wirral Council's LOBO loan borrowing accounts for approximately three quarters of the council's long term borrowing, contravening the explicit advice of Cipfa that Council's

should not hold more than 30% of their long term debt in LOBO loans. (see [Treasury Management Bulletin - April 2015](#))

The Council is now effectively locked into expensive LOBO loans with interest rates ranging from 4.4% to 8%.

The loan signed on 15 August with Hypothekenbank, is particularly problematic, as not only could the Council now refinance at much lower rates were it not locked into the LOBO loan by high “breakage fees”, but even at the time the loan was signed in August 2005 PWLB rates (4.6% interest) than the so-called “teaser rate” on the LOBO (6.25% interest), ensuring this loan was never taken out in the public interest.

The initial interest rate on LOBOs is usually a fixed “teaser” rate, but the lender has the “option” to propose or impose, on pre-determined future dates a new fixed rate. The borrower has the only “option” to either accept the new rate or repay the entire loan.

In the current low interest rate climate, it is highly unlikely that the lender will call it’s “option,” as it would be disadvantageous to the lenders.

That “lenders options” on LOBO loans are unlikely to be called by the banks was confirmed by [Barclays, which cancelled the lender’s option on vanilla LOBOs \(announced June 2016\)](#) converting outstanding LOBO loans to a fixed rate.

With the LOBO contracts, should the local authority choose to repay the loan (for example to access a cheaper rate loans elsewhere) without waiting for the lender to exercise their “option”, it would need to pay a “break penalty” to exit the loan. This is reflected in the “fair value” of LOBO loans in the accounts, which corresponds to nearly twice as much of the value of the loan principles.

The impact of falling base interest rates is that it increases the total repayment or “breakage cost” of the LOBO loan portfolio, effectively locking the council into paying higher interest rates until maturity, forgoing the opportunity to refinance at lower interest rates.

Effectively the total “breakage cost” to exit the loans is impossible to monitor by Council, and would only be determined through a negotiation process with the bank.

The decision to sign these contracts was therefore a gamble and an irrational and unlawful decision by the Council.

I would therefore be grateful for you, under the Local Audit and Accountability Act 2014, to apply to the courts for a declaration that Wirral Council’s LOBO loan borrowing as referenced in the 2015-2016 accounts is unlawful, and request that you prepare a public interest report on this matter,

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