

Report to Cabinet
8 July 2015
Report of Executive head of regeneration and development
Subject Establishment of a local housing development company

Item

11

KEY DECISION

Purpose

To seek approval to establish a local housing development company to build residential properties for sale and rent

Recommendations

1. To approve the establishment of a local housing development company to build, sell and manage houses for sale and rent.
2. To delegate the detailed arrangements to allow the establishment of the company to the executive head of regeneration and development in consultation with the portfolio holders for resources and income generation and environment and sustainable development.

Corporate and service priorities

The report helps to meet the corporate priority of a prosperous city.

Financial implications

Under the proposed development model the council will fund the proposed development company through loans and equity investment and the council will receive an income stream for the general fund through dividends and interest on loans.

Ward/s: All

Cabinet member:

Cllr Stonard -resources and income generation portfolio holder

Cllr Bremner -environment and sustainable development portfolio holder..

Contact officers

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Background documents

None

Report

Background

1. The council acquired land in Bowthorpe in the 1970s to develop 3 villages- Clover Hill, Chapelbreak and Three Score. Originally the council developed the sites for 50/50 council and private housing, mostly in the 1970s. Three Score is the last village to be developed and a small part of the area was built in the 1990s by a private developer with a housing association providing the affordable housing. In the early 2000s the council intended to sell the remaining area of land at Three Score to a housing developer to generate a capital receipt. Due to the housing market crash, the deal was not concluded.
2. In September 2009, the council entered into an innovative partnership with the Homes and Communities Agency (HCA). A fundamental part of the partnership was to bring forward development of the Three Score site. HCA provided £2.5M investment to construct the road/ infrastructure to serve the whole site. The partnership aim was that the site should form an exemplar development with housing built to high design and environmental standards. The original intention was to sell a first phase to a developer who would build the first phase and also construct the infrastructure to serve the whole development. Whilst a preferred developer was selected following a procurement process, the contract was never entered into.
3. In January 2013, the council agreed to dispose of a first phase of land at nil value to allow Norsecare to develop a 172 unit housing with care and dementia care facility. This is now under construction and is due to be completed in March 2016.
4. In June 2013, the council obtained planning permission for the whole development, of 1000 dwellings a care home, open space and other community facilities.
5. In February 2014, cabinet agreed that the council should develop the second phase of the Three Score site itself rather than sell the site to a private developer. This forms part of the council's ambitious programme of housing development. Whilst the key driver is to generate income for the council's general fund, development will ensure housing is delivered to high environmental standards (maximising passivhaus) and comply with planning policy on affordable housing (33% of which 85% will be social rent and 15% intermediate tenure).
6. In January 2015, cabinet agreed to submit a planning application for this phase (phase 2) - 172 homes (private homes for sale and rent plus 33% affordable). The application was approved in May 2015.
7. In January 2015 the council entered into a contract with La Farge Tarmac to construct the road / infrastructure to serve the whole development. This is now under construction and is due to be completed later this year.
8. The council has also agreed to take forward development on a number of other sites in its ownership including Goldsmith Street.
9. The council has started a OJEU procurement process to establish a 'fabric first' framework of contractors from which a constructor can be selected for Threescore

Phase 2 and Goldsmith Street in the short term and then for other sites in the longer term. In order to achieve a start on site at Three Score as soon as possible, a decision will need to be made on the appointment of a constructor in September.

Requirement for a housing development company

10. Officers have been researching the legal and tax implications of developing private homes for sale and rent and had concluded that it will be necessary to establish a housing development company as a vehicle to do this. . This would be a limited liability company, limited by shares all of which will be owned by the council, so the council would have full control over its activities.

11. The key objectives of the company would be:

- The provision and management of private homes for sale and rent
- The generation of a new alternative source of income to support the council's wider activities

12. This would help the council to achieve its priorities :

- To make Norwich a prosperous and vibrant city
- To make Norwich a healthy city with good housing.

Consultancy advice on establishing a housing development company

13. Specialist legal and tax advice (via Savills and Trowers and Hamlin) was procured to:

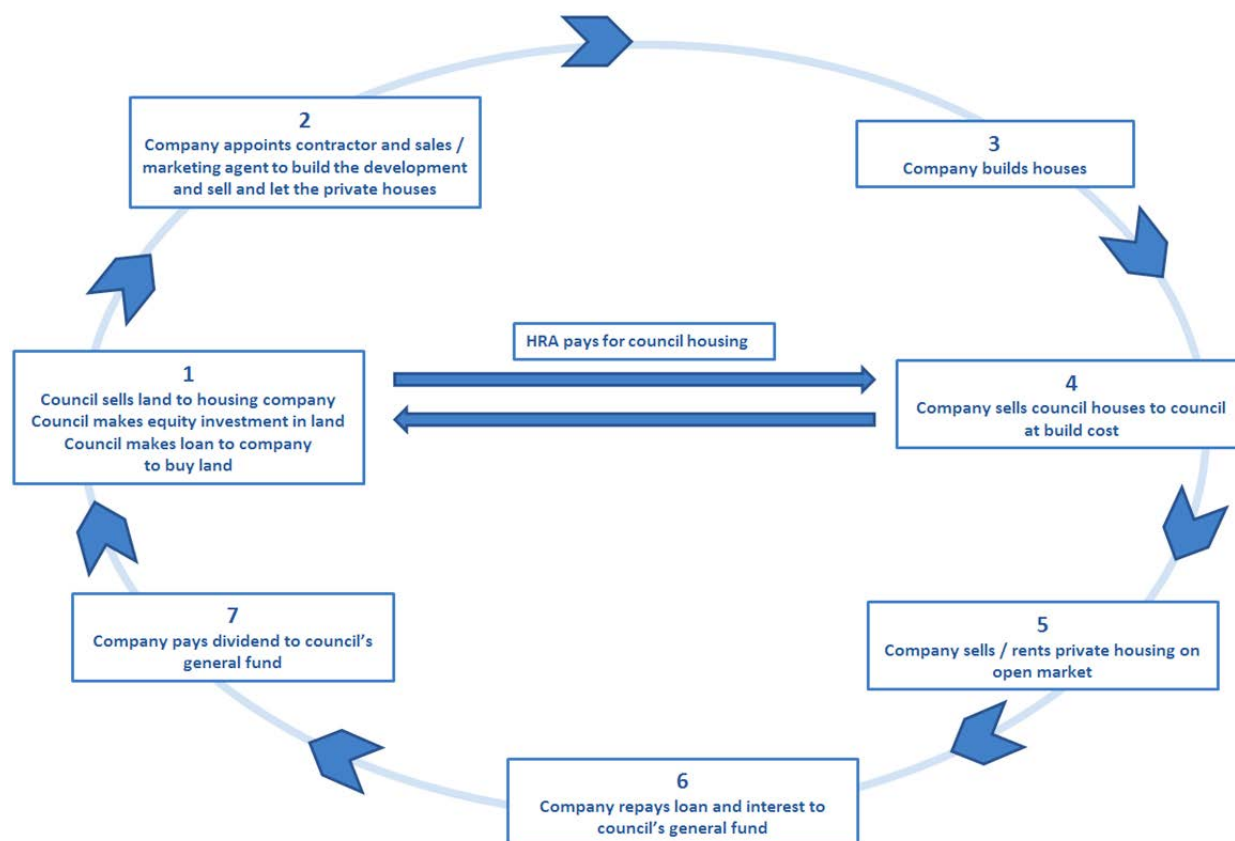
- Provide specific advice on Stamp Duty Land Tax (SDLT), VAT, Corporation Tax, state aid and 'commercial activity', (see Glossary).
- Review the proposed development model, in particular to provide greater clarity on whether the council or the proposed company need to act as client for construction contracts;
- Develop a detailed business case for Three Score phase 2 and Goldsmith Street. explaining how the company will be financed (through loans from the council); and
- Provide an audit of other issues and risks to be considered.

14. Their report has now been received and this is attached as part of confidential Appendix 1 to this report as it contains sensitive financial information.

15. The report confirms that a company is needed to develop the houses – as the council intends the project to have a "commercial purpose" in accordance with Section 4 of the Localism Act 2011 – and recommends that the company should build all the houses, regardless of tenure.

16. The Savills report has considered the option of the council developing housing itself. Section 1 of the Localism Act 2011 gives the council a wide and largely freestanding 'general power of competence' to do anything that an individual may do. This is subject (inter alia) to the requirement that, if what it is doing is for a commercial purpose then, in accordance with Section 4, it must do so through a company.
17. The programme of new build is to be seen as a whole. Advice suggests that separating out the construction of the affordable housing element and 'dividing' the programme, for tax or other reasons, between (say) a preparatory and an implementation stage would not be safe. Consultants advise that the programme has to be seen as a whole so that all parts of the activity should be carried out through a company.
18. The general power of competence, like any other power, must be used reasonably. The availability of another, more obvious, power could mean that the section 1 power was being used improperly. In this case, however, the fact that the affordable housing is being carried out through a company and might in other circumstances be based on the obvious power of Section 9 of the Housing Act 1985 is not material.
19. The report confirms that for commercial flexibility, the company should be a company limited by shares (CLS). In this case then group relief for SDLT purposes should be available. The development model proposed is as follows:
- Land is sold from the council to the company at market value – the funding to be provided by the council as debt or equity.
 - The company enters into construction and related contracts with a third party.
 - The council provides further loan funding to the company during the construction period, under a funding agreement which is state aid compliant.
 - Private sale properties are sold by the company, generating a profit in the company which would be liable to pay corporation tax on that profit.
 - Affordable housing is sold by the company to a registered provider (council or third party).
 - The company retains the private rented properties and renting them to the market – also taking on full responsibility for management, maintenance and life cycle repairs. Though there are options to contract out this responsibility to the council or others.

Diagram 1- Proposed development model



20. The company would be liable to corporation tax. VAT on construction is likely to be zero rated and VAT is not likely to arise from the sale of dwellings. The private rental business will give rise to some irrecoverable VAT on operating costs, such as management and maintenance. Loans from the council will need to be at market rates to avoid breaching state aid regulations.

21. Savills have produced a business case for phase 2 at Three Score which demonstrates that the proposed model is viable and will deliver income to the council's general fund. Details are included in the confidential Appendix 2.

22. The report also demonstrates the business case for the company through the inflationary increase in property values over time and how the static level of debt leads to a gradual build up in property equity in the company. It demonstrates that income gradually increases, compared to a static interest cost, so that over time there are significant profits being generated. Whilst surpluses are relatively small in the early years, these financial forecasts form the basis of a sound and viable financial business plan, which would satisfy the directors, shareholders and funders of the company.

23. Savills also advise that for the purposes of contract procurement, it will be important for the company to be in place before any contract is ready to be let. Provision for this has already been made in the OJEU process for the 'Fabric First' framework which allows for the council or a wholly owned subsidiary to be the client. Following the procurement process, the company will be in a position to appoint a contractor for Three Score phase 2 in September. This means that the company would need to be established in name (and registered at

Companies House) by this time. The timescale for the design and build contract is such that once appointed, the contractor will spend approx. 3 months on design with construction likely to start in January 2016.

Options for governance of the proposed housing development company

24. As part of the research into the establishment of a housing development company, officers have reviewed best practice and case studies from other local authorities. A number of other councils have established housing companies already. The type of company is influenced by the objectives that the council wishes to achieve.
25. There are a number of councils that have set up wholly owned companies limited by shares, including Daventry, South Cambridgeshire, Ealing and Thurrock. The governance and board membership of these companies varies from council to council. Many authorities have kept this very simple (especially when the company is first established) and restricted the decision making to 2 directors. Ealing, Thurrock and South Cambridgeshire have appointed senior officers as their directors (2 to 4 directors, including senior managers and the chief finance officer). The housing company set up by Daventry has a board of 5 directors, including 3 members and 2 officers.
26. It would be up to the council/ company to determine whether to include any external representation on the board. This could be helpful to provide commercial expertise. The majority of companies established by local authorities do not employ staff but buy services from the local authority. It is important to note that the directors will need to act commercially in the best interests of the company. There may be occasions where there could be conflicts of interest for the individual and their role within the council. However as the company would be wholly owned by the council, this is not likely to be a frequent issue. In order to register a company, a minimum of 1 director is needed.
27. Having researched the governance approach adopted by other local authorities who have set up housing companies, it is proposed that there should be a board of 5 directors. This would be made up of 2 members (portfolio holders, who would be appointed through the council's normal process of appointments to outside bodies and who would need to be named individuals for the purposes of the registration of the company) plus 3 officers (senior management team representatives including the s151 officer, again who would need to be named individuals). It is suggested that a quorum of 2 would be required for any decisions (one officer and one member). This is the preferred approach to provide a balance between democratic accountability and operational efficiency. It would be beneficial to allow for external representation on the board if needed in future to provide commercial expertise. Memorandum and articles of association will need to be drawn up.
28. The council would have full control over the proposed company. The company will be wholly owned by the city council so at both general meetings of the company and at board meetings of the directors the city council will have 100% decision making power within the law and within the company's constitution. It will also be possible to establish a shareholders' agreement between the council and the company to add an extra contractual layer of control over the company

to include requirements, for example, that the company's annual business plan needs to be approved by the council.

Next Steps

29. A further report to cabinet will be needed on the sale of land to the company and the funding arrangements between the council and the company. At this stage cabinet is only asked to agree to the establishment of the local housing company.

Glossary:

State aid: State aid is defined as an advantage in any form whatsoever conferred on a selective basis to undertakings by national public authorities. A company which receives government support gains an advantage over its competitors. Therefore, the EU Treaty prohibits State aid unless it is justified by reasons of general economic development. To ensure that this prohibition is respected and exemptions are applied equally across the European Union, the European Commission is in charge of ensuring that State aid complies with EU rules.(source ec.Europa.eu)

Stamp Duty Land Tax (SDLT): You must pay Stamp Duty Land Tax (SDLT) if you buy a property or land over a certain price in England, Wales and Northern Ireland.

The current SDLT threshold is £125,000 for residential properties and £150,000 for non-residential land and properties.

You pay the tax when you:

- buy a freehold property
- buy a new or existing leasehold
- buy a property through a shared ownership scheme
- are transferred land or property in exchange for payment, eg you take on a mortgage or buy a share in a house

(source: gov. uk)

Corporation Tax: Your limited company must pay corporation tax on its taxable profits.

Corporation tax also applies to:

- most unincorporated associations, eg clubs and co-operatives
- foreign companies with a UK branch or office

Your company must keep records for corporation tax.

The current rate is 20%.

(source: gov.uk)

Integrated impact assessment



NORWICH
City Council

The IIA should assess **the impact of the recommendation** being made by the report

Detailed guidance to help with completing the assessment can be found [here](#). Delete this row after completion

Report author to complete

Committee:	Cabinet
Committee date:	8 July 2015
Head of service:	Andy Watt
Report subject:	Establishing a local housing company
Date assessed:	09/06/15
Description:	

	Impact			
Economic (please add an 'x' as appropriate)	Neutral	Positive	Negative	Comments
Finance (value for money)	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Will generate an income stream for the council's general fund
Other departments and services e.g. office facilities, customer contact	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	The company could purchase services from the council
ICT services	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
Economic development	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Will deliver construction jobs
Financial inclusion	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Will deliver affordable housing
Social (please add an 'x' as appropriate)	Neutral	Positive	Negative	Comments
Safeguarding children and adults	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
<u>S17 crime and disorder act 1998</u>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
Human Rights Act 1998	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
Health and well being	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Will create high quality new housing development which encourages a healthy lifestyle (emphasis on walking and cycling)and provides homes which provide a healthy environment (passivhaus)

	Impact			
Equality and diversity (please add an 'x' as appropriate)	Neutral	Positive	Negative	Comments
Relations between groups (cohesion)	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
Eliminating discrimination & harassment	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
Advancing equality of opportunity	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Delivers new affordable housing
Environmental (please add an 'x' as appropriate)	Neutral	Positive	Negative	Comments
Transportation	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	Whilst the report results in new development , it will be taken forward in a way that reduces the impact on the environment
Natural and built environment	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	As above
Waste minimisation & resource use	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	As above
Pollution	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>	As above
Sustainable procurement	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	As above
Energy and climate change	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	As above
(Please add an 'x' as appropriate)	Neutral	Positive	Negative	Comments

	Impact			
Risk management	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	

Recommendations from impact assessment

Positive

The report will result in positive economic benefits for the council and the city

Negative

Whilst there are some negative impacts from development, the quality of development will minimise environmental impacts

Neutral

Issues