NORWICH
City Council

Committee Name: **Cabinet**

Committee Date: **12/01/2022**

Report Title: Norwich Regeneration Ltd Business Plan 2022/23

Portfolio: Councillor Kendrick, cabinet member for resources Councillor Kendrick, cabinet member for resources

Report from: Executive director of development and city services

Wards: All Wards

OPEN PUBLIC ITEM

Purpose

To consider the Norwich Regeneration Limited (NRL) Business Plan for 2022/23, which the company is required to produce under its articles of association and to make a recommendation to Council that appropriate provision is made within the Council's budget to deliver the plan.

Recommendation:

a) To endorse the NRL business for 2022/23 on behalf of Norwich City Council as the shareholder;

b) To agree that provision for the necessary additional loan finance of £6m to deliver the business plan, is incorporated with the capital programme being proposed to Council as part of the budget for 2022/23;

c) Invite NRL to undertake work on the design, feasibility and phasing of a possible fourth phase of development for NRL on the Threescore site, the provision for which is identified in the approved budget for the company within section 6.6 of the business plan.

d) That further work be undertaken to identify possible further sites for residential development that may form part of the company's pipeline in future years.

Policy Framework

The Council has three corporate priorities, which are:

- People living well
- Great neighbourhoods, housing, and environment
- Inclusive economy

This report assists with delivering the great neighbourhoods, housing and environment priority and supports a healthy organisation.

Report Details

Background

1. Prior to making any investments in housing sites, Norwich Regeneration Limited (NRL) is required to bring a business plan to the Council, as its shareholder, for approval. This report provides the context to the NRL business plan, through setting out the current financial and operation of the company, and the details of the business plan itself which is recommended for approval.

2. NRL throughout FY 2021/22 has continued to work to improve the operation of the company and stabilise the financial position, alongside a continued focus to work alongside the Council to improve the company's governance. The Council has sought to build the expertise, competency, and experience at board level to support the company, so it continues to build on operational improvements delivered over the past three years.

3. Steps undertaken to date include:

   - Taking forward expert advice from the appointed non-executive directors to the board. Both non-executive directors hold a wealth of experience and expertise to assist the company to grow as a housing developer. The role of the non-executive directors has been to support and challenge both the company board and Managing Director.

   - Further recommendations are now in place to continue to strengthen the company board, with further restructuring of board to occur at the start of the annual plan for FY 2022/2023. The Articles of Association for the company will be amended in various ways, including the appointment of a further non-executive director with the agreement of the Council at the end of quarter 1 of the current financial year to reflect this.

   - Close engagement between the Council and company continues with the executive director of the corporate and commercial services and executive director of development and city services attending board meetings as participating observers. The participating observers are not part of the final decision making of the company board to avoid any potential conflict of interest.

   - The company also communicates its progress in delivering its business plan to a Shareholder Panel every quarter.

   - Greater resilience for the company from a resource point of view is also in place. Resource from the council's housing delivery team will now be recharged into NRL – including its managing director – to increase capacity and pace with regard to the delivery of commercial developments. This not only builds the Council's capacity to deliver social housing but controls the operating costs of the company whilst building resilience for the company.

4. The above measures have contributed to significant improvements in performance of the company over the past year. These are considered further below.

Activity in 2021/22

5. Activities in 2021/22 have enabled the company to positively complete the operational transformation and turn round of the company. This activity has sought to reshape how the company both strategically and operationally performs.

6. The key aim for last year's Business Plan was the completion of building, sales, and occupancy of Trinity Gardens at Rayne Park. In addition to this, the company has been engaged in several other high priority workstreams.
   - Continuing to improve the overall operation of the business and becoming more business-like
   - Continuing to progress new housing developments through approved budgets

7. The company is pleased to report that performance has exceeded forecasts, with regards the sale forecasts and financial forecasts. The sales result of Trinity Gardens at Rayne Park was impressive based on the many challenges this development has faced. The company grows in confidence in terms of understanding its Price – Product – Place specifically to Threescore but is confident the learning can be taken forward into new development opportunities.

8. The company still recognises the financial challenges it faces but, there is growing confidence by the company Board – with support from Council – that it can erode the company's historic losses and grow in the medium term, built on the foundations of the significant changes it has made.

9. The company, via improved operational process and the use of robust residential viability appraisals, is focused on ensuring that future developments make a return. Work continues to position our development opportunities in the best possible way to ensure we deliver financial stability and growth.

10. In its 2021/2022 Business Plan, NRL was able to complete the construction of all new homes at Trinity Gardens at Rayne Park and complete the sale and occupancy of 73 new homes – this represents 100% of homes built (apart from one property which is held as the marketing suite for the next build phases). As a result, the company has repaid £6.5m of loan to the council through the sale of new homes in the financial year 2021/2022, leaving a current loan balance of £6.15m. Interest costs of the 2021/22 financial year are forecast to be £0.376m.

11. It should be noted that this improved financial performance has been achieved without compromising on the vision and goals of the company which is to deliver new homes into the market that are of high quality and to lead the way on high environmental performance which results in a sustainable neighbourhood.

Current Performance

12. An update on the financial performance of the company was given to the shareholder panel in November 2021. This covered actual performance on the

first 6 months of the financial year and forecast projections through to 31 March 2022. Detail on the updated projections of the company is provided as part of the exempt Business Plan appendix.

13. The company believe that the council should continue to invest in developments via NRL as there is now a proven track record at making loan repayments and interest or SLA payment which provides income for the council.

14. Sale of new homes were launched in September 2020 which led to strong reservations from Sept 2020 to March 2020. Exchanges of the first plots started in October 2020 and were delivered in line with Build Programmes. Final exchanges on the site were made in October 2021.

15. This gave the company a run rate on average of 6 properties per month to reserve and exchange – ahead of a forecasted average 4 plots per month. This achieved circa £18m sales value. 74% of purchasers were 1st time buyers and 71% used the help to buy scheme.

Proposed response to the Business Plan 2022/23

16. The business plan for the company for 2022/2023 is contained in the attached exempt appendix A. It sets out NRL's vision, mission, values, objectives, and business principles. It describes how financial performance and governance have been improved. It has been approved by the Company's board and submitted to the Council for consideration.

17. The NRL business plan for 2022/23 is presented as a continuous plan for the future of the company and to further its ambitions to build high-quality houses in Norwich. It does so with improved assurance that the company can shift the financial challenge it has historically faced.

18. At its heart is the proposition that the Council as shareholder and lender continues to provide additional resources to the company to deliver the business plan.

19. Staffing for the company will primarily be fulfilled by service level agreements between council and company. Key expertise and competency will now be agreed with the council's in-house Housing Delivery Team which will add greater resilience to the delivery of NRL's developments and future proposals.

20. It is the Council's role as shareholder to strike the right balance between risk and reward and, although it is acknowledged that the company is undoubtedly performing better in the last trading year, there are clear risks which need to constantly be reviewed. The Council will continue to work with the company to encourage ongoing development of the company's governance framework to help manage such risks.

21. There are considerable uncertainties in the private housing market arising from the impact of the Covid-19 and Brexit which result in volatile economic conditions. Whilst the housing market has proved to be resilient to date, and recent announcements of government support in the mortgage market may

assist, there is no guarantee that it will remain so going forward. The company's supply chain will need to be constantly reviewed and this business plan shows a good level of awareness of risks and how this can be mitigated.

22. Given the request for continued future council investment in NRL to develop new homes for the city, and the risks in relation to the UK housing market and construction sector, NRL has again engaged independent expert analysis of the assumptions and forecasts in next year's business plan to provide for a greater degree of confidence in the plan.

23. This can be reviewed as an appendix as part of the NRL business plan and gives confidence that the council has considered the risks and rewards of investment decisions and that there is an appropriate level of return for the risk involved in each development.

24. Independent commercial development advisors have worked alongside the company to scrutinise the commercial information, financial assumptions, forecasts, and risks identified in the business plan and have provided assurance that the information and assumptions support a sound and deliverable plan.

25. Such an examination cannot eliminate risk. However, it is considered that such independent commercial advice can provide the council with an additional layer of assurance to inform any further investment in NRL and demonstrate that it has sought to minimise any further loss of shareholder value.

26. As further investment in new NRL projects will need to be subject to the preparation of detailed business cases which will be subject to considerable scrutiny and will need Council approval, it is considered that having this level of independent assurance will aid the process of considering the detailed business cases.

27. The work to continue to improve the governance of the company to bring it into line with best practice and to minimise the potential for conflicts of interest, coupled with even further expertise to board level – will also help to reduce the risk of future investments.

28. The Shareholder Panel, comprising senior councillors and officers, will continue to oversee the performance of NRL and scrutinise and have oversight of the appropriate indicators.

Implications

Financial and Resources

Any decision to reduce or increase resources or alternatively increase income must be made within the context of the Council's stated priorities, as set out in its Corporate Plan 2019-22 and Budget.

29. The current position is that the council has an equity investment of £3.42m in Norwich Regeneration Limited and the company has an outstanding loan balance of £6.15m with the council. This means the current debt to equity ratio equates to 64:36.

30. The delivery of the Norwich Regeneration Ltd Business Plan will require financial investment from the council in the form of additional debt financing. The company's forecasts a maximum loan balance of £12.15m to deliver the business plan (current balance £6.15m). To ensure sufficient headroom in the loan facility it is proposed to request a maximum loan facility of £13m be incorporated into the 2022/23 capital programme.

31. No further equity investment is proposed above the existing investment of £3.42m. This will mean that at the peak of the loan there will be higher debt to equity ratio than 75:25 but this is only expected to be for a short period of time before the first loan repayment is made in 2023/24.

32. In July 2021, Council approved an increase to the General Fund capital programme of £2m in 2021/22 and £2m in 2022/23 to provide loan finance and share capital to Norwich Regeneration Ltd for Threescore Phase 3. This requirement will now be updated in the 2022/23 budget papers to reflect the revised business plan requirements – additional loan of £6.85m in 2022/23. The capital budget for 2022/23 will be presented to Full Council for approval in February 2022. Future developments will be subject to detailed business cases that need to be prepared for finance to be advanced on individual developments.

33. The loan will provide the up-front funding to the company to development the pipeline of sites. The financial modelling shows, that following the sale of private units, the company is able to repay the additional loan as well as a portion of the existing loan balance.

34. Following the budget approval of the loan facility, a new loan agreement will be developed setting out the interest and repayment terms.

35. Further lending to the company will have the effect of increasing the council's capital financing requirement (the underlying need to borrow). This would require the council to borrow externally. The council will need to continue to assess the affordability and proportionality of its overall indebtedness arising from lending to the company.

36. The council has an earmarked reserve relating to Norwich Regeneration Limited. The reserve level was increased in 2019/20 to mitigate against any potential future non-recovery of the loan balance and the associated Minimum Revenue Provision[1] charges. The current balance on the reserve is £3.35m and an MRP charge of £0.650m was made in 2020/21. This will be kept under review to reflect any changes (positive and negative) in the risk profile of the loan balance.

37. It must be noted that the government is currently consulting on changes to the capital framework, specifically around the application of Minimum Revenue Provision. Where authorities borrow to finance capital spend, they are required under regulations to set aside money each year from their revenue account, to

[1] Minimum Revenue Provision (MRP) is the minimum amount which a Council must charge to its revenue budget each year, to set aside a provision for repaying external borrowing (loans). This is an annual revenue expense in a Council's budget.

make sure they can afford to repay the principal of their debt. Local authorities have flexibility in how they calculate MRP, providing it is ‘prudent’.

38. The government is concerned that not all authorities are fully compliant with the need to make prudent revenue provision, in particular, around asset investments and capital loans. The council’s current policy is to ensure MRP is charged where there is any indication that an element of the loan is not recoverable. Under the revised proposals, there may be a requirement to charge MRP on the full loan balance over the period in which the benefits are provided. This would potentially increase the revenue costs to the council during the loan period. The implications of any changes will need to be considered following the conclusion of the government consultation.

39. The business plan assumes that the company purchases the land required from the council at market value.

Legal

40. The company’s Articles of Association require that any action it takes in respect of its activities must be undertaken within the parameters of the business plan agreed by the Council. The setting up and operation of the Council’s companies is an executive function, however in line with the recommendations, the Council’s funding for the business plan will need to be considered as part of the Council’s budget for 2022/23.

Statutory considerations

Consideration	**Details of any implications and proposed measures to address:**
Equality and Diversity	There are no direct equality impacts arising from this report.
Health, Social and Economic Impact	There are no direct impacts arising from this report
Crime and Disorder	There are no direct impacts arising from this report
Children and Adults Safeguarding	There are no direct impacts arising from this report
Environmental Impact	There are no direct impacts arising from this report

Risk Management

The business plan sets out the company’s principal risk and their mitigations in Section 8 of the exempt appendix.

Risk	**Consequence**	**Controls Required**
Financial risks	NRL not being able to repay or provide return on the investment.	See sensitivity testing in the business plan and the assurance report from Savills. Council continues to hold

		an earmarked reserve to help manage risk associated with the loan financing.
	Changes to the Minimum Revenue Provision guidance increases revenue costs associated with providing loan financing to NRL.	Continue to monitor the outcome of the government consultation.

Other Options Considered

41. To not adopt the business plan: if the Council does not adopt the business plan, then NRL will not be able to progress further development and the Council will need to consider the options for sites currently earmarked for development by NRL.

Reason for the decision/recommendation

It is recommended that Cabinet support the Business Plan for Norwich Regeneration Limited for 2022/23 and agree that:

a) NRL Business Plan FY 2022/23 is agreed on behalf of the shareholder
b) Council be recommended to make provision within the 2022/23 capital programme to provide financing to the company to deliver the business plan.

Background Papers: None

Appendices: Business Plan is attached as an exempt appendix

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