

APPENDIX F

WAVERLEY BOROUGH COUNCIL

EXECUTIVE - 3 NOVEMBER 2008

Title:

LOCAL DELIVERY COMPANY

[Portfolio Holder: Cllr Richard Gates

[Wards Affected: All]

Summary and purpose:

The purpose of this report is to set out the legal and financial principles for setting up a wholly owned Local Delivery Company within the control of Waverley Borough council, to have available to maximise opportunities when future conditions are suitable.

How this report relates to the Council's Corporate Priorities:

It is expected that, if formed, a Local Delivery Company could potentially contribute to all five corporate priorities, Environment, Improving Lives, Subsidised Affordable Housing, Leisure and Value for Money.

Equality and Diversity Implications:

There are no equality and diversity implications arising from this report at present.

Resource/Value for Money implications:

There are no equality and diversity implications arising from this report at present.

Legal Implications:

There will be a legal resource required and this is identified in the report.

Background

1. Members will be aware of the continuing Government policy of Negative Subsidy, which places continuing financial pressure on Waverley Housing Revenue Account (HRA), and consequently on the extent of the services it can continue to provide for its customers.
2. In July 2007 the Government published A Green Paper Homes for the Future, More Affordable, More Sustainable (CM7191) which positively promotes the idea that alongside Housing Associations, Local Authorities should develop an enhanced role in the provision of new affordable housing.

3. Furthermore it recommended that vehicles may be set up by Local Authorities which enable them to invest in affordable housing and to keep the income and capital returns in a way that currently the HRA cannot.
4. A report was submitted to the Executive in October 2007 which recommended that a Special Interest Group be created to receive reports into how a Special Purpose Vehicle (SPV) may deliver new affordable housing for Waverley Borough Council.

Introduction

5. Work to determine the shape of a Special Purpose Vehicle has concentrated on the identification of sites, and within certain criteria, developing a business model to determine their viability for development.
6. In June 2008 the SIG received a paper, outlining within existing resources, the business plan for the provision of 200 homes over a period of 5 years. It concluded that this could be achieved by providing a third of the units for market sale, another third for shared ownership and the final third for intermediate renting.
7. Whilst, the business plan showed that theoretically it was possible to deliver those homes. For the number of units expected, within the determined timescale and current resources it did not, in the short term, provide rented homes in sufficient number, to house those most in need.
8. Also, although the delivery of any new properties would not be for a minimum of two years, the current and foreseeable condition of the housing market means that the risk assessments carried out on the business plan produced unacceptable results at this time.
9. This arises from the lack of mortgage finance, which is having a profound negative effect on sales of shared ownership and for-sale properties at this time.
10. At its meeting in October 2008, the New Subsidised Affordable Housing Special Interest Group reached its conclusions and recommended that the Executive endorses the proposal to establish a Local Delivery Company (see report attached at Annexe 1).

Local Delivery Vehicle (LDV) or Company

11. However the principles established during this project has provided an opportunity to look again at how a Company or Local Delivery Vehicle (LDV) wholly owned by Waverley Borough Council might be set up to potentially benefit the Council in delivery of its services.
12. Investigations, with the help of legal consultants Trowers and Hamlin, have shown that currently for Waverley the most appropriate vehicle would need to be non-charitable, not for profit and with no equity partners.

13. The main advantage that an LDV would have over the regulated normal accounts administered by the Council is its relative freedom from Government controls.
14. If the company develops a portfolio of housing in the future, because of the negative subsidy regime, revenue income generated by the LDV would be 48.5% more than that generated by the HRA.
15. This principle would also apply to capital income, which would not be subjected to governmental capital receipts pooling.
16. Balancing these advantages is the fact that an LDV would be subject to company rules and would be liable for tax. However there are different company structures, which seek to mitigate these effects. A paper which sets out the most suitable models has been prepared by Trowers and Hamlin and is attached to this report – see Annexe 2.

Potential uses for an LDV

17. The following headings describe the possible uses an LDV may have
 - 1) Receiving vacant properties that require major works
 - 2) Receiving other voids through a trickle transfer programme
 - 3) New house building, either independently or in partnership with a Housing Association
 - 4) Involvement in estate remodelling including land acquisition
 - 5) Possible use as a vehicle to build other facilities normally financed through or by the general fund

Creation of an LDV

18. The initial setting up of a Local Delivery Vehicle is not a complicated or difficult process, involves only modest financial outlay, and can be carried out in house. It can then remain dormant until a business case and risk assessments are developed for its use at an appropriate time. Its creation now would deal with any potential administrative issues in advance, and would be carried out in parallel with the development of any business plans.

Type of preferred company

19. Trowers and Hamlin in their paper indicate some legal and financial limitations of a possible four models of LDV in two categories, and touches on the governance required.
20. The two categories are defined as
 - 1) A company, which is set up as a sole entity without equity partners

- a) Company Limited by Guarantee- (CLG)
 - b) Industrial and Provident Society (IPS)
- 2) A company, which forms the nucleus of a joint venture or project
- a) A Company Limited by Shares (CLS)
 - b) Limited Liability Partnership (LLP)
21. It is T & H opinion that a sole company can also become a partner of a joint venture company without losing its sole status, thereby maintaining flexibility for the future.
22. Significantly an IPS and an LLP are not easily set up as dormant companies as they both require specific reasons for their registration process, and the implied recommendation is to consider a CLG.

Costings

23. The registration of the Company Limited by Guarantee needs to be with Companies House and can be carried out by one subscriber—normally a member of the legal in house staff, and one shareholder with a registration fee of £20. Registration normally takes a week to ten days. Subsequently there is an annual fee payable of £30.
24. Beyond the actual registration fees there would be a consultant's fee for advice and guidance during registration of approximately £800. A suggested name for the new Company is Waverley Initiatives Ltd. Preliminary investigations through Companies House website shows that currently this form of name is available to be used.

Conclusion

25. The creation of an LDV as a Company Limited by Guarantee (CLG) wholly owned by the Local authority, and used to potentially benefit Council services, is possible, even if the business case to build new homes is not currently viable. Once legally established, the Company could remain dormant until business plans for its possible functions are prepared, and appropriate arrangements made for its governance.
26. The most advantageous use of an LDV is to enable a maximum possible return on investments made, and not be subject to governmental levies as in the negative housing subsidy on the HRA.

Recommendation

It is recommended that

1. approval be given to set up a Company Limited by Guarantee called Waverley Initiatives Ltd, as a wholly-owned Local Delivery Vehicle by Waverley Borough Council;

2. further work be carried out to determine the business models for the various areas of activity that the Company might undertake, and further reports be brought to the Executive with details of the possible future activities of the Company, potential timetables and details of governance.

Background Papers (DCEx)

There are no background papers (as defined by Section 100D(5) of the Local Government Act 1972) relating to this report.

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WAVERLEY BOROUGH COUNCIL

NEW SUBSIDISED AFFORDABLE HOUSING SPECIAL INTEREST GROUP
- 1 OCTOBER 2008

REPORT TO THE MEETING OF EXECUTIVE ON 3 NOVEMBER 2008

A. APOLOGIES FOR ABSENCE

Apologies for absence had been received from Cllrs Edwards and Reed.

B. DISCLOSURE OF INTERESTS

There were no disclosures of interests.

C. LOCAL HOUSING COMPANY

C.1 The New Affordable Housing SIG was established in January 2008 to consider the legal, financial and constitutional implications of setting up a Special Purpose Vehicle (SPV) to deliver affordable homes in mixed communities, outside the Housing Revenue Account or General Fund. The SIG was tasked with setting out a possible business model for an SPV, or Local Housing Company, and an assessment of its viability.

C.2 At their meeting in April 2008 the SIG considered the principles of how a company might be financed, its impact on Council finances and the sort of tenures that it might offer. The SIG agreed criteria on governance, structure and potential tax liabilities, which would underpin a business model. The SIG noted the emerging difficulties in the housing market and the financial problems that could be experienced by some organisations in the medium term.

C.3 In June 2008 the SIG considered a draft business model within which the Local Housing Company might operate. This concluded that for the Local Housing Company to be viable with no borrowing after five years it would be necessary to offer a tenure mix of 35% rented and 65% shared ownership and outright sale.

C.4 The SIG was concerned that the proposed level of outright sales was contrary to the Council's corporate priorities to provide more affordable rented housing. There was also concern that the market conditions for sale and shared ownership were deteriorating and improvements in the short- to medium-term did not appear likely. Consequently the risks involved with the proposed tenure mix were increasing. Officers were asked to re-visit the assumptions under-pinning the business model and to test their validity for the changing financial climate.

- C.5 At its meeting in October 2008 the SIG received a report from Officers outlining the fall in average values across all housing types in Waverley since the development of the original business plan. It concluded that within the specified criteria, the delivery of affordable homes of the appropriate tenure would not be possible. Furthermore, the mix of tenures that could be delivered in current market conditions had an unacceptable degree of risk attached.
- C.6 Therefore the SIG agreed to RECOMMEND to the Executive that this specific business model for the Local Housing Company for the provision of subsidised affordable housing should not be adopted.
- D.1 However, the SIG noted that the work undertaken in connection with the Local Housing Company had provided information and insight into what other opportunities might be available to Waverley by setting up a SPV, and endorsed the proposal to establish a Local Delivery Company, as detailed in the report to the Executive at Appendix F

Present at the Meeting

Cllr R J Gates (Chairman)
Cllr Mrs E Cable
Cllr V Duckett
Cllr Mrs P A Ellis
Cllr Mrs N Warner-O'Neill
Cllr K Webster

The following officers were present:

Fiona Cameron
David Simmons
John Swanton
Paul Wenham

**A report to Waverley Borough Council on the options for
setting up a local delivery vehicle**



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A report to Waverley Borough Council on the options for setting up a local delivery vehicle

1 Background

1.1 We understand that Waverley Borough Council (the Council) are looking at the possibility of setting up a local delivery vehicle (an LDV), which could be used to achieve one or more of the following purposes:

- new house building,
- receiving vacant properties through a trickle transfer,
- estate remodelling,

and could include generating receipts for the Council to use towards its Decent Homes programme.

1.2 We have set out below a description of the different corporate forms which the LDV could take and provided examples of the types of legal structures which involve these different corporate forms taking into account the above purposes for which the Council may wish to use the LDV. If required the LDV could be set up with wider objectives than just housing (for example, to provide community facilities such as leisure centres) and its objects could include land acquisition, although more detailed consideration of such wider objectives is beyond the scope of this paper.

1.3 There are various options for the form of the LDV. It could be set up as a company, either limited by shares or by guarantee, an industrial and provident society or possibly as a limited liability partnership. The key decision making factors on choice of legal vehicle are likely to be whether the LDV is trading for profit or not, whether it is to be charitable or not, and whether there is a need now or in the future to be able to offer a partner or partners equity in the company. It is understood that at present the Council wishes the LDV to initially be set up as a non-charitable, not for profit vehicle with no equity partners.

1.4 In the final section of this paper we have described the basic formation requirements for setting up an LDV.

2 Companies Limited by Guarantee and Industrial and Provident Societies

If there is a possibility that the LDV is not going to be used to trade for profit, as is currently anticipated, the most suitable options are to set it up either as a company limited by guarantee (a CLG) or an industrial and provident society (an IPS). Both CLGs and IPSs can be charitable or non-charitable. There may be little to choose between using a CLG or an IPS for the LDV – it may simply come down to which model a local authority is most familiar with.

We have set out below a description of the main features of a CLG and an IPS followed by an example of a legal structure involving a CLG or IPS which has been considered by some authorities to raise finances to refurbish dilapidated void properties whilst also raising funding to invest in its Decent Homes programme for its retained HRA stock.

2.1 Industrial and Provident Societies

Industrial and provident societies have evolved out of mutual societies and they are registered with the Financial Services Authority. An IPS can be charitable or non-charitable but must be not for profit and exist for community benefit.

An IPS has shareholders, although the shares carry no financial benefit. The Council could never be the sole shareholder as there have to be at least three shareholders, but subsidiary status can be achieved if wanted by giving the Council a share and the right to appoint the board.

If the LDV were to be set up as a charity, a current advantage of an IPS over a company limited by guarantee is that charitable IPSs are exempt from registration with, and regulation by, the Charity Commission. However, it should be noted that at some point in 2009 charitable IPSs which are not registered social landlords will need to register with the Charity Commission also. IPSs may also have an advantage in terms of presentation as they are not perceived as being linked with profit-making in the same way that companies can be, although it should be noted that companies limited by guarantee are increasingly perceived as distinct from profit-making vehicles since many are charitable.

The IPS model used to be more restrictive than the CLG model because until recently it was not possible to register an IPS with 'class' voting rights. Class voting allows each class of an organisation's members potentially to have parity of votes, rather than each individual member having one vote. However, the Financial Services Authority have now been persuaded to accept registrations with class voting rights and it would be hoped that applications of a similar nature would be accepted in the future.

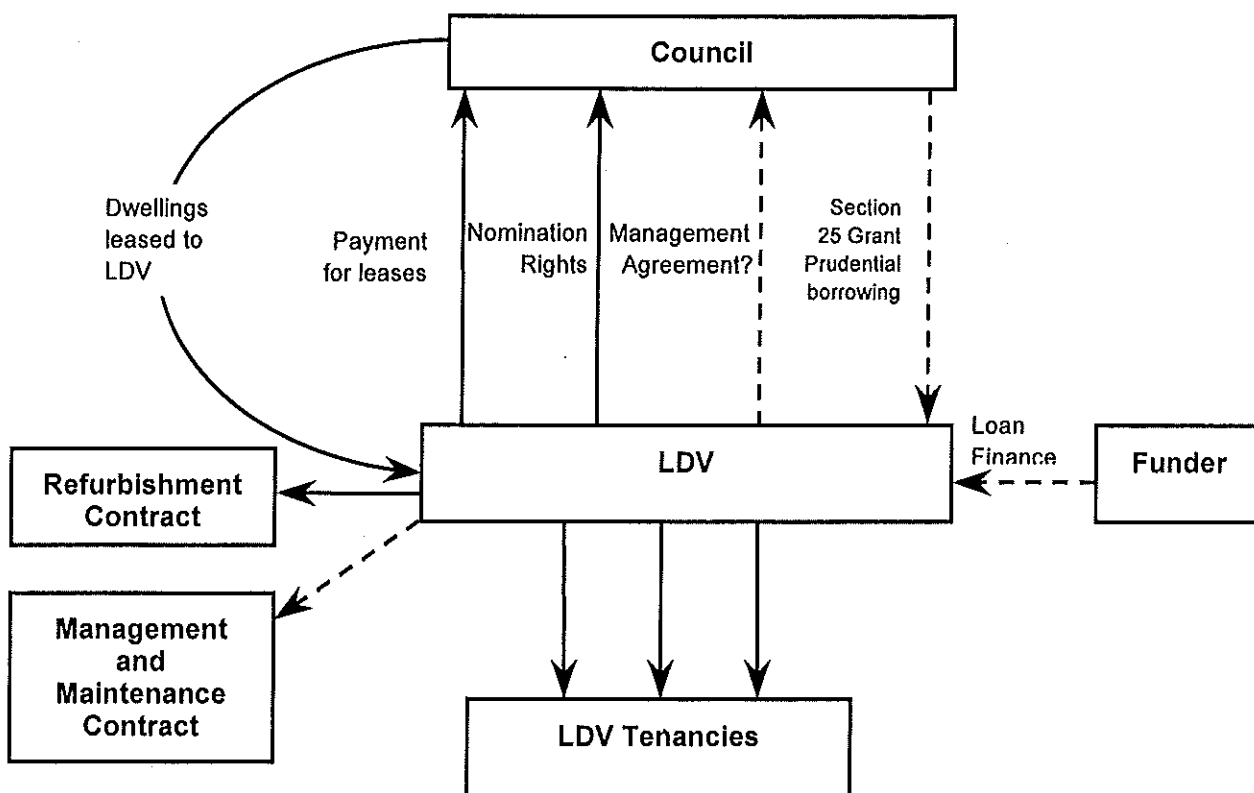
2.2 Companies limited by guarantee

A CLG is a company where the general members do not hold shares – but instead each member undertakes to pay a nominal figure (usually £1) in the event of any insolvency on the part of the company. It is possible to regulate the various interests of the members by creating different classes of members with different voting rights.

In addition CLGs are frequently used for social housing activities as they are not associated with profit-making in the same way companies limited by shares are.

If the LDV is to be a wholly-owned subsidiary, the Council could initially be the sole member. But a company limited by guarantee can have many members and different categories of members with different voting rights. Changing from a single member company to one with many is also simple.

2.3 A structured example of an LDV receiving vacant properties and raising HRA funding



As stated above, this model has been considered by some authorities to raise finance to refurbish some dilapidated void properties which are pepper-potted around its stock and also to raise funding to invest in its Decent Homes programme for its retained HRA stock. It would include the following features:

- The council creates an LDV as a company limited by guarantee or an industrial and provident society.
- The council grants a 125-year lease of up to 499 void properties to the subsidiary over a 4 or 5-year period at full value (taking into account any obligations contained in the transfer agreement). The cap of 499 properties prevents the lease of the properties being classified as a 'large scale disposal'. The lease could contain a break clause entitling the council to end the lease in certain circumstances or at certain times, although any outstanding loans would need to be repaid to the funder at the point that the break clause is exercised.
- The LDV would procure a contractor to refurbish the properties within the first 6 months of the lease.
- The funding to pay for the leases and the refurbishment works would come from either private finance and/or possibly from prudential borrowing by the council.

- The LDV then lets the properties on a mix of tenures, including social rented accommodation (possibly including some temporary accommodation to homeless households or to other clients for whom the council has a duty to provide housing) and potentially some intermediate rentals.
- The lease payments to the council by the LDV could be used by the council to carry out improvements to its housing stock under its Decent Homes programme.
- The LDV would contract back to the council for management services (subject to the applicability of the EU procurement rules).
- The council would have nomination rights to the LDV's social rented accommodation.

3 Companies limited by shares and limited liability partnerships

It may well be that the Council decides that it does not wish to involve equity partners in the LDV but it may still be useful to rehearse the potential for a joint venture LDV here. As an alternative to the CLG and IPS models, if the Council wished to enter into a joint venture then an LDV set up as a company limited by shares (a **CLS**) or a limited liability partnership (an **LLP**) would be most suitable. These types of vehicles are used where the LDV either now or in the future is likely to want to trade for profit.

Set out below is a description of the main features of a CLS and an LLP followed by an example of a legal structure involving a CLS or LLP which has been considered by some authorities to remodel estates.

3.1 Companies limited by shares

The company limited by shares is generally viewed as the most appropriate legal form for the majority of joint ventures where an on-going business is to be run, due to the fact that the corporate structure is tried and tested and is underpinned by an established body of law and practice. However, there are potential tax disadvantages in the partners conducting the project through the medium of a limited company, which can be avoided by opting to form an LLP.

A company limited by shares is the type of company with which most people tend to be familiar. If the LDV is to be a joint venture company, the Council and its partner would each agree to subscribe for shares in the LDV and the rights and obligations of the partners with regard to the venture would be set out in a shareholders agreement.

In terms of overall control and financial and tax planning, the structure of a limited company provides considerable flexibility through the creation of different types of share and loan capital. A company can also create a floating charge over its assets, which is often a requirement of external finance. Companies can only distribute profits as dividends if profits have been made because of rules relating to maintenance of capital.

3.2 Limited liability partnerships

The Limited Liability Partnerships Act 2000 allows the incorporation of LLPs. The LLP is a novel business entity and combines limited liability for members with the relaxed internal

regulation of a traditional partnership. It is also a body corporate which is a legal entity separate from its members.

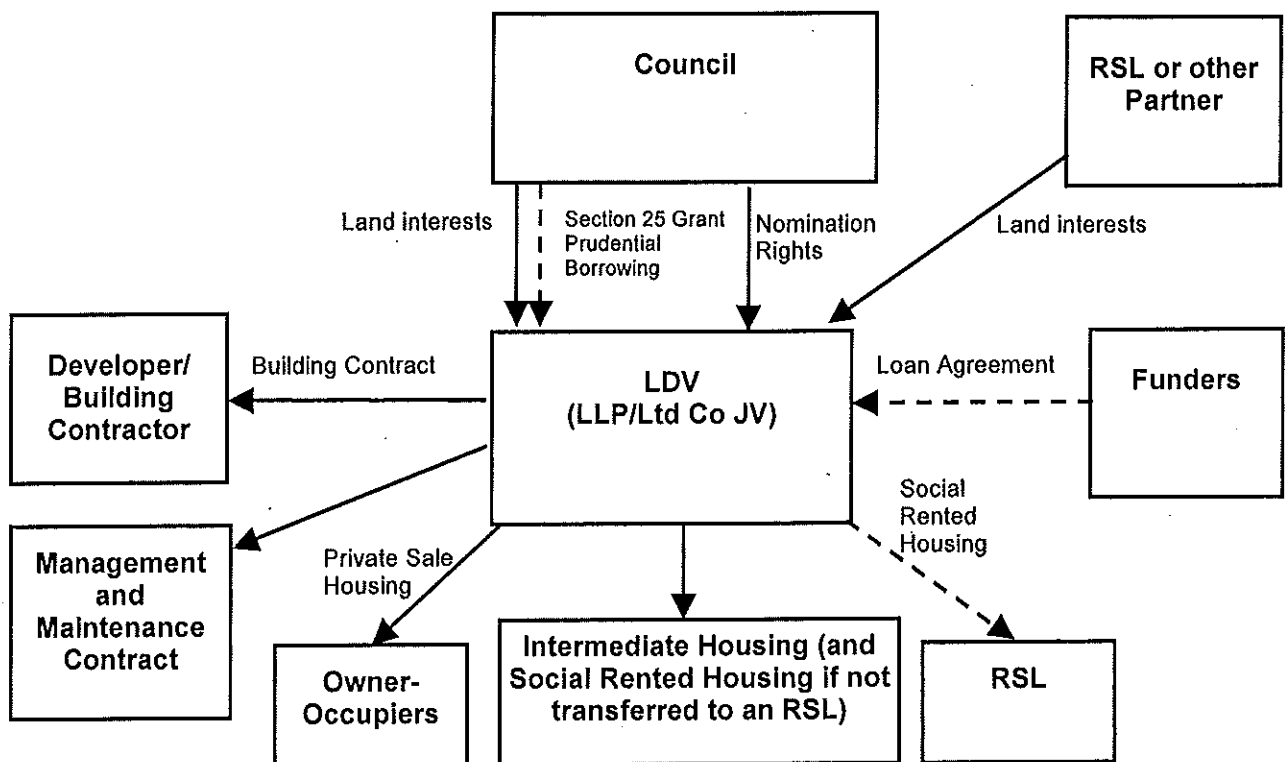
In a joint venture LDV set up as an LLP, the Council and its partner would be members of the LLP and the relationship between them would be governed by the terms of a members agreement. Any further parties wishing to join would need to execute a deed of accession to the members agreement, agreeing to be bound by its terms.

Members do not appoint a board to run the LLP on their behalf. There are at least two formally appointed designated members who are merely compliance officers. The running of the LLP rests with the members as they agree it. This internal freedom resembles a partnership. In practice, a body similar to a board is then established as the decision-making forum for most decisions.

The members are free to agree how to share profits and are also free to agree management roles and responsibilities. An LLP has no share capital so capital can therefore be reduced or increased at the will of the members. As the LLP is a body corporate with unlimited capacity it can create floating charges like a traditional limited company.

However, the principal advantage of using an LLP over a company limited by shares is the way in which it is treated from a tax perspective. The LLP is treated for tax purposes as a traditional partnership, and members are treated as traditional partners. Therefore, unlike a limited company, it is tax transparent and any trade, profession or business carried on by an LLP with a view to profit will be treated like a traditional partnership. Since the tax status of the partners determines how much tax is paid, the Council's share of any profits should be corporation tax free. The vires for a local authority to participate in an LLP is not free from argument and specific legal advice on the Council's power to participate in an LLP would need to be sought if this was the Council's preferred model.

3.3 A structured example of a joint venture LDV to remodel/regenerate an estate



This would be a joint venture vehicle set up with an RSL or other partner. This model has been considered by local authorities interested in remodelling/regenerating estates and, in so doing, offering the opportunity of generating receipts which the authority could use either towards other affordable housing or regeneration projects (including subsidy of its Housing Revenue Account) or otherwise towards support of its General Fund.

The model would include the following features:

- The model assumes the transfer of land to the LDV with vacant possession. The council would be responsible for decanting its tenants and rehousing them in other nearby council accommodation and, if necessary, promoting a compulsory purchase order within the project area in order that it could then transfer its land with vacant possession to the LDV for full value (taking into account any obligations contained in the transfer agreement).
- If appropriate the RSL/partner would transfer its land within the project area to the LDV. Further, the RSL/partner may be required to offer accommodation from its stock to any leaseholders within the project area who have exercised their right to buy, either acquiring at a discounted purchase price or under shared ownership arrangements (ie as an 'inducement' to enable the council to transfer land with vacant possession).

- Following transfer of the vacant properties and land, the LDV would enter into a building contract with a developer or building contractor to demolish (or refurbish if appropriate) the existing buildings and redevelop the land. The funding would come from either private finance or possibly from prudential borrowing by the council.
- The regenerated estate would include a mix of tenures through the provision of some housing for private sale and some intermediate housing (such as shared ownership schemes) with the aim of maintaining the original amount of social rented accommodation. Obviously this could only be achieved if it is possible to increase the overall number of units on the estate through efficient use of space.
- On practical completion of the new properties the LDV could transfer the social rented housing to an RSL and/or enter into a management and maintenance agreement with a third party (which could include the council (subject to the applicability of the EU procurement rules)) to manage and maintain its affordable housing stock (i.e. the social rented and intermediate housing).
- On practical completion the LDV may also enter into a nominations agreement with the council for the affordable housing.
- The completed affordable housing properties (if not transferred to an RSL) would be let by the LDV, either as assured or assured shorthold tenancies or on shared ownership (or other forms of intermediate housing) terms. The income from the properties would be used to pay any management and maintenance fees and any loan repayments. Any profits could be shared between the partners in the joint venture, including the council.

4 Setting up an LDV – formation requirements

- 4.1 Registration of a company limited by shares or by guarantee requires the initial subscribers (there need by only one subscriber) to sign the memorandum and articles and to submit these together with various forms signed by the proposed board members and secretary to Companies House together with the registration fee of £20 (or £50 for the same day service). Registration is usually completed within one week to ten days of the application.
- 4.2 Registration of an IPS requires three founder members to sign the rules and to submit these together with two forms relating to the IPS's proposed activities together with the registration fee of around £1,000. Registration is usually completed within about three weeks.
- 4.3 Registration of an LLP requires at least two subscribers to submit an incorporation document setting out the name, registered office and details of the proposed members of the LLP (which must be signed by all of the proposed members) to Companies House together with a registration fee of £20 (or £50 for the same day service). Registration is usually completed within one week to ten days of the application.
- 4.4 If the Council wished to set up the LDV as a shelf company in order to protect the name, Trowers & Hamblins could apply to register a company with the chosen name or, alternatively, the Council's legal officers could set up the company instead. If the LDV is to remain dormant for a period we would recommend setting it up as a CLG or CLS rather

than an IPS or an LLP. To set up an IPS there must be a reason as to why it is being set up as a community benefit society rather than a company, which is more difficult to demonstrate if it is to be dormant and the specific purpose to which the LDV will later be used has not been identified. If the Council later decided that it wanted an IPS, it may be possible to convert the LDV from a company into an IPS subject to Financial Service Authority clearance. The difficulty with setting up an LLP which is to be dormant for a period is that an LLP must be set up with a view to making a profit. Therefore the LDV could be set up as an LLP if a future use is identified and the LDV would definitely be used with a view to making a profit but an LLP could not be set up simply to save a name. Thus it would be simpler to incorporate the LDV as a company and at a later date, if the Council wished to use an LLP, an LLP could be set up and the company's name could be swapped with that of the LLP.

- 4.5 With regard to the fees incurred following the incorporation of a vehicle, even if it is to be dormant, whichever form of vehicle is chosen there will be an annual fee. The annual fee for a company limited by shares, a company limited by guarantee or an LLP is £30 and the annual fee for an IPS ranges from £50 to £395 based on a sliding scale depending upon the vehicle's total assets.

Trowers & Hamlins
August 2008

