

<b>Report of:</b>	Executive Director for Growth and Place: Kevin Parkes Executive Member for Economic Development and Infrastructure: Councillor Lewis Young
<b>Submitted to:</b>	Executive, 18 <sup>th</sup> December 2018
<b>Subject:</b>	Housing Delivery Vehicle (HDV) – Preferred Delivery Model

### Summary

#### Proposed decision(s)

It is recommended that Executive approves:

- a) the creation of a Housing Delivery Vehicle in the form of a Wholly Owned Company Limited by Shares;
- b) the Business Plan (attached as Confidential Appendix 1 to Part B of this report), which proposes the development of three Council owned sites, Gresham (Phase 1), Beechwood and Hemlington North, subject to satisfactory due diligence;
- c) the establishment of a Company Board to provide strategic direction and set operational parameters, with the following interim Directors: Kevin Parkes; Councillor Lewis Young; and, Councillor Denise Rooney;
- d) delegate the appointment of the Company's Secretary to the Council's Monitoring Officer;
- e) a budget for up-front costs incurred prior to the Company set-up, (funded from Section 106 affordable housing resources), as referred to in Paragraph 47 of Part B of this report;
- f) a funding package of up to £10m, comprising part equity, part loan, on terms to be compliant with state aid regulations and subject to satisfactory due diligence of individual site proposals as referred to in Paragraphs 15 to 23 of Part B of this report;
- g) delegation of the approval of the terms of the funding package to the Strategic Director of Finance, Governance and Support, following consultation with the Executive Member for Finance and Governance;
- h) delegation of the Council's function as Company shareholder to the Elected Mayor; and,
- i) the commencement of a process to appoint a Managing Director of the Company.

Report for:	Key decision:	Confidential:	Is the report urgent? <sup>1</sup>
Decision	Yes	N/A	Non urgent

Contribution to delivery of the 2018-22 Strategic Plan		
Business Imperatives	Physical Regeneration	Social Regeneration
Ensuring that the Council operates efficiently and effectively so that physical and social regeneration outcomes are maximised.	Investing in Middlesbrough to provide and improve facilities which act to increase the town's reputation, create social opportunity and improve the Council's finances.	Assist in delivering the Council's Social Regeneration agenda, ensuring a steady supply of affordable housing to meet the needs of its emerging and aspiring population.

Ward(s) affected
Confirmation of the establishment of the Housing Delivery Vehicle will affect all wards.  All Ward Members were invited to a briefing on the proposals outlined in this report.

### What is the purpose of this report?

1. To seek approval to establish a Housing Delivery Company and endorsement of the associated Business Plan.

### Why does this report require a Member decision?

2. Following a decision by Executive in June 2018 to intervene in the housing market in order to exert greater control over the pace and quality of housing development across the town, a Shadow Board was established and an options appraisal undertaken to identify a preferred delivery model. The report stated that the preferred delivery model would be presented to Executive.

### Report Background

3. This part of the report provides an update on the option appraisal undertaken to consider potential delivery models for the HDV and recommends a preferred option that will achieve the objectives established by the Shadow Board.
4. Part B of the report will summarise the key elements of the HDV Business Plan, which will set out the initial scale and scope of the Company.

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<sup>1</sup> Remove for non-Executive reports

5. The June 18, Housing Delivery report to Executive set out that the Council was embarking on the most ambitious house building programme in recent history and was committed to ensuring that housing growth occurs in a more balanced way, and is based on the principles of well-designed neighbourhoods with a sense of place and identity, with access to schools, green spaces amenities and transport.
6. The report stated that to ensure this commitment is reflected in the housing product being developed, and to facilitate the sustainable growth of the town, there is a need to take a pro-active role in determining what is built and where. It was concluded that some form of 'special purpose' housing delivery vehicle would provide the Council with the ability to exert influence over the market, and address the identified gaps.
7. The report further advised that work had been commissioned to explore the potential for the Council to proactively affect the housing product on offer and achieve greater control over delivery through its own land holdings by considering the actions being taken by local authorities across other parts of the country. The research undertaken concluded that the majority of local authorities were pursuing wholly owned companies, and that Middlesbrough would be well placed to consider this option strongly, as it offers the greatest scope to meet the Council's objectives.
8. The recommendations of the Housing Delivery report were that the Executive:
  - a) endorses the need for the Council to intervene in the housing market in order to exert greater control over the pace and quality of development;
  - b) approves the establishment of a Shadow Board to consider a detailed option appraisal of housing delivery models; and,
  - c) identifies three Members to sit on the Shadow Board.
9. In November 2018, the Economic Development, Environment and Infrastructure Scrutiny Panel concluded an investigation into HDVs to ascertain their effectiveness in addressing local housing market needs. The Final Report of the Panel recommended that In order for Middlesbrough Council to take a pro-active role in re-shaping the local housing market, as well as Middlesbrough's landscape, the Council should establish its own HDV in the form of a wholly owned Company Limited by Shares.
10. This report will provide an update on the option appraisal undertaken to consider potential delivery models for the HDV and will recommend a preferred option that will achieve the objectives established by the Shadow Board.
11. The report will also set out the initial scale and scope of the Company, including the first phase of development of the Council owned sites at Gresham, Beechwood and Hemlington North.
12. Additionally, the report will set out the requisite governance arrangements that will be implemented from the perspective of both the Company and the Council.

### **Option Appraisal**

13. Following the approval of the June 18 report, a Shadow Board was established, comprising three Elected Members and three officers, to consider the options at the Council's disposal, and the governance, management and financial arrangements.

14. The Shadow Board has subsequently developed objectives for the HDV and engaged an experienced consultant to lead the implementation process, working alongside Council officers from appropriate services including: Regeneration; Planning; Finance; and, Legal. The objectives of the HDV are to:
  - a) deliver homes to buy or rent, that meet the needs of our aspiring population;
  - b) accelerate delivery of the housing required to support population and economic growth;
  - c) create quality places to live that act as a catalyst for further regeneration and investment; and,
  - d) increase long-term income streams that support the Council's Medium Term Financial Plan (MTFP).
15. The Consultant has undertaken a review of the initial research, and the stated objectives, to determine whether the creation of a Wholly Owned Company would be the most appropriate structure for the HDV. The review determined that the Council can take two alternative paths to achieving the objectives:
  - a) try to influence the housing supply market through engagement with the volume house builders and Registered Providers (RPs); or,
  - b) direct intervention.
16. The ability to influence the market is clearly limited. There is more power to do this on disposal of Council owned sites, for example by issuing development briefs to cover the nature of projects, but these tend to be loose controls rather than being prescriptive. In this approach, delivery is still reliant on developers wanting to do those types of project and in some cases this can be unpopular, especially in challenging market areas. Other than an initial capital receipt there is no income stream for the Council and, if a prescriptive brief is enforced, this can severely reduce the land value.
17. The second option is for the Council to intervene directly. The Council can rely upon the general power of competence within the Localism Act 2011. A local authority may exercise the general power of competence for its own purpose, for a commercial purpose and/or for the benefit of others i.e. this includes the setting up of a Housing Company. The HDV objectives clearly involve carrying out a commercial activity. This must therefore be done through a Company.
18. The Consultant's review concluded that the creation of a Wholly Owned Company Limited by Shares is the most appropriate way forward in terms of meeting the Council's objectives. The benefits of this route are clearly stated as opposed to other structures. It is not without risk but these can be mitigated against through proper governance and a robust Business Plan. Again, it is this route that has ultimately been chosen for direct intervention housing delivery by many other local authorities. This has been considered, and endorsed, by the Shadow Board.

### **Review of Proposed Structure against Objectives**

19. Considering each objective in turn, the proposed structure of a Wholly Owned Company Limited by Shares is the favourable option for many reasons.

**20. To deliver homes to buy or rent, that meet the needs of our aspiring population**

- a) The HDV will be flexible enough to provide a mix of housing tenures and types in the locations required by the Council.
- b) It can be innovative in its approach and look at sites that the market may not consider viable or attractive. This would not be possible relying on the market alone, even with RPs.
- c) There can be a mix of capital return projects and those built for long term rental returns. Individual projects may contain several tenure types and there could be interplay between these depending on market response.
- d) There can be cross-subsidy of projects where some schemes have a 'profit for purpose' outcome which in turn is used to pump-prime other more financially challenged projects.
- e) The structure is also appropriate as this commercial activity requires a Local Authority Trading Company (LATC) for delivery and autonomy of decision making to maintain choice and control.
- f) The HDV can also procure homes via construction contracts with partner companies who will be able to be eager to work with a trading Company operating on commercial principles.

**21. To accelerate delivery of the housing required to support population and economic growth**

- a) The HDV can set its own build rates, which the market may not have been willing to consider.
- b) Multiple sites can be pursued at the same time all with differing financial metrics and outcomes.
- c) Cross-subsidy can assist the delivery of poorer sites increasing output.
- d) Construction contracts can be placed with multiple contractors ensuring a spread of the resource and build risk.
- e) Innovative build techniques through modern methods of construction can be stipulated to speed up delivery where many developers would only be comfortable with slower traditional methods.

**22. To create quality places to live that act as a catalyst for further regeneration and investment**

- a) The design and layout of homes and neighbourhoods can be entirely under the control of the HDV.
- b) Good design and higher quality can result in additional costs which developers are unwilling to burden their schemes with. The HDV can take a different view.
- c) A holistic approach to the development of a site can be taken with the regeneration and investment goals put to the fore.
- d) Poorer sites can be developed to stimulate investment and regeneration in areas that a developer or development partner would not consider.
- e) The Council can deliver good quality housing and become an exemplar landlord, setting the benchmark for the town.

### **23. To increase long-term income streams that support the Council's MTFP**

- a) The HDV can deliver projects for sale and rent thus recycling capital and building up a portfolio of low risk income generating assets.
- b) The Council can take a longer term view with the outcomes of the HDV than a pure developer.
- c) Income and profit from the HDV can be taken in a variety of forms to best suit the needs of the Council. This flexibility is deemed crucial.
- d) The HDV will be operated on a commercial basis but with a social goal. This will ensure it is sustainable in the long term.
- e) Long term funding can be made available to the HDV via a variety Council sources in a cost effective manner, thus ensuring stability

24. The Consultant appraisal concluded that the Council should pursue the set-up of a Wholly Owned Company Limited by Shares and that this is the most appropriate method of achieving the stated objectives. This has been considered by officers and the HDV Shadow Board and there is an agreement that this is the most appropriate Company structure.

### **HDV Business Plan**

25. The HDV Consultant, working alongside Council officers from appropriate services including: Regeneration; Planning; Finance; and, Legal, and following discussion with the Shadow Board, has developed a Business Plan for the HDV that will enable the objectives set out in Paragraph 14 of this report to be achieved, and establish the initial scale and scope of the Company.

26. The Business Plan proposes the development of three Council owned sites, Gresham (Phase 1), Beechwood and Hemlington North. The schemes will deliver 100 units over two years, including 37 units for low cost affordable rent, 35 units for market sale and 28 mixed tenure units respectively.

27. The sites are in Council ownership and will be bought by the HDV, subject to the granting of planning permission. The purchase will take place following the granting of planning consent and procurement of a building contractor and prior to construction commencing. The price will reflect the open market value of the sites.

28. Formal approval to sell the sites to the HDV will be sought from the Council's Executive Sub-Committee for Property.

29. The HDV Business Plan and associated appendices are attached as Confidential Appendix 1 to Part B of this report.

### **MBC Governance Arrangements**

30. The HDV Business Plan establishes the Structure, Management, Governance and Resource requirements of the Company, but the Council must also ensure that there are robust governance arrangements in place to protect its own interests.

31. The HDV will be a local authority trading company limited by shares, with the Council as the sole shareholder. As the Council is the instigator, owner and controller of the HDV, it will be required to:

- a) approve the Memorandum and Articles of Association, Shareholder Agreement, Business Plan and Loan Agreement;
  - b) appoint the Board of Directors;
  - c) approve draw-downs from the Loan;
  - d) monitor the Board and HDV through regular reports and updates; and,
  - e) approve key decisions, such as changes to the Business Plan.
32. The recommendations of this report will seek Executive approval for the HDV Business Plan and for a funding facility to support the development and construction of 100 units across three sites.
33. This report will recommend that the approval of the exact terms and drawdown of the funding package is delegated to the Strategic Director of Finance, Governance and Support, following consultation with the Executive Member for Finance and Governance, subject to satisfactory due diligence of individual site proposals.
34. There is also a requirement for the Council, as the sole shareholder, to be able to approve business critical decisions, such as amendments to the Business Plan, within acceptable timescales.
35. It is, therefore, proposed that the discharge of the shareholder function will be facilitated by Executive approving delegated authority for the Elected Mayor to approve key decisions, such as the amendment of the Company Business Plan.

**What decision(s) are being asked for?**

36. It is recommended that Executive approves:
- a) the creation of a Housing Delivery Vehicle in the form of a Wholly Owned Company Limited by Shares;
  - b) the Business Plan (attached as Confidential Appendix 1 to Part B of this report), which proposes the development of three Council owned sites, Gresham (Phase 1), Beechwood and Hemlington North, subject to satisfactory due diligence;
  - c) the establishment of a Company Board to provide strategic direction and set operational parameters, with the following interim Directors: Kevin Parkes; Councillor Lewis Young; and Councillor Denise Rooney;
  - d) delegate the appointment of the Company's Secretary to the Council's Monitoring Officer;
  - e) a budget for up-front costs that will be incurred prior to the Company set-up, (funded from Section 106 affordable housing resources) as referred to in Paragraph 47 in Part B of this report;
  - f) a funding package, comprising part equity, part loan, on terms to be compliant with state aid regulations and subject to satisfactory due diligence of individual site proposals, as referred to in Paragraphs 15 to 23 in Part B of this report;
  - g) delegation of the approval of the terms of the funding package to the Strategic Director of Finance, Governance and Support, following consultation with the Executive Member for Finance and Governance;
  - h) delegation of the Council's function as Company shareholder to the Elected Mayor; and,

- i) the commencement of a process to appoint a Managing Director of the Company.

### **Why is this being recommended?**

- 37. Following an options appraisal, a Wholly Owned Company Limited by Shares was considered to be the most effective delivery model for successfully developing and operating a Housing Delivery Vehicle.
- 38. An experienced consultant has been appointed who has led the development of the HDV to this point, subject to due diligence by Council officers and the Shadow Board. It is considered imperative that the MD is in post when the Company starts trading in April 2019.
- 39. The Council's Housing Strategy (2017-20) refers to the Strategic Housing Market Assessment (2016), which identifies a need for an additional 200 affordable homes per annum over the period 2016-34. The HDV will help achieve the need for more good quality affordable housing in the town.

### **Other potential decisions and why these have not been recommended**

- 40. Other delivery models were considered but not recommended as the specialist advice and subsequent due diligence confirmed that a Wholly Owned Company Limited by Shares would best achieve the Council's objectives.
- 41. Furthermore, in November 2018, the final report of the Economic Development, Environment and Infrastructure Scrutiny Panel's investigation into HDVs recommended that in order for Middlesbrough Council to take a pro-active role in re-shaping the local housing market, as well as Middlesbrough's landscape, the Council should establish its own HDV in the form of a wholly owned Company Limited by Shares.
- 42. The Scrutiny Panel's Action Plan is attached as Appendix 2.

### **Impact(s) of recommended decision(s)**

- 43. The impacts of the recommended decision(s) are to:
  - a) ensure that the most effective HDV operating model is adopted;
  - b) assist with the physical regeneration of the town, creating places where people want to live and employment opportunities that will contribute towards the social regeneration agenda;
  - c) maximise income streams to the Council in terms of the capital receipt, Council Tax, New Homes Bonus, rental income and house sales - central to the Medium Term Financial Plan and the ongoing support of core Council services;
  - d) increase the pace of housebuilding to ensure that the Council maintains a high level of housing growth that both supports population and economic growth;
  - e) assist in delivering the Council's Social Regeneration agenda, ensuring a steady supply of affordable housing to meet the needs of its emerging and aspiring population; and,
  - f) set the design bar for other housebuilders, creating quality places where people want to live, and act as a catalyst for further regeneration and investment.



## **Legal**

44. As set out in Paragraph 17, the Council can rely upon the general power of competence within the Localism Act 2011 for its own purpose, for a commercial purpose and/or for the benefit of others i.e. this includes the setting up of a Housing Company. The HDV objectives clearly involve carrying out a commercial activity and this must therefore be done through a Company.
45. By adopting the preferred delivery model the Council will be the sole shareholder of a local authority trading Company limited by shares. As part of the governance arrangements, Legal and Democratic Services will draft the requisite Memorandum and Articles of Association.

## **Financial**

### Due Diligence

46. Due diligence has been considered by the Consultant and Officers, including the Principal Solicitor and the Finance Business Partner, throughout the development of the HDV Business Plan, and has been incorporated into the reports that have been appraised and approved by the Shadow Board, including:
  - Company Structure – KT Financial Solutions;
  - Site and House Type Drawings – Logic Architecture;
  - Cost Plans – Todd Milburn Partnership;
  - Marketing Reports – Kier;
  - Tax Advice – PWC; and,
  - State Aid Advice – DWF Solicitors.
47. The Company will be required to provide annual audited statement of accounts in sufficient time to enable the Council to submit its own final accounts by the statutory deadline. Furthermore, the Company will be required to provide the Council with any financial information needed, upon request, to verify that the business is meeting expectations.
48. In addition to the direct financial returns, the HDV would deliver the following benefits to the Council:
  - Regenerating neighbourhoods and communities;
  - Addressing housing shortages in the types and tenures proposed;
  - Disposal of surplus Council land, currently with a maintenance burden;
  - Giving a return to the Council on its investment;
  - Increasing the Council Tax base and New Homes Bonus payments;
  - Making a positive statement of intent by the Council in housing;
  - Demonstrating the ability of the Council to deliver new homes; and,
  - Positively impacting on the local and wider economic situation through property and construction related business and employment.

## ***Policy Framework***

49. The decision will not amend the Council's policy framework. The decision is aligned to the Mayor's Vision for a Fairer Middlesbrough as it would assist with the provision of fair access to high quality homes. The decision would also contribute towards the priority to strengthen our city through bold and innovative regeneration and help create a Stronger Middlesbrough.
50. The decision is also aligned to the Medium Term Financial Plan as the proposed housing development will generate income from New Homes Bonus and Council Tax.

## ***Equality and Diversity***

51. The attached IA, attached as Appendix 1, has concluded that the decisions would not have any disproportionately negative impacts.

## ***Risk***

52. The following high level risks, which are identified in the Strategic and Directorate Risk Registers, will be reduced as a consequence of the direct housing market intervention enabled by the recommended decisions:

O1-005 - If poor economic growth occurs, then this will reduce public and private sector investment in the town, including town centre retail, housing development and business.

O1-004 - If the New Homes Bonus funding is reduced, due to a change in the funding regime or the Council failing to build new homes at the targeted rate then Council Tax receipts will not be maximised, impacting upon the Council's MTFP.

O1-045 - If delivery of the new housing programme does not meet the projected targets then this can have a negative impact on the assumptions within the MTFP.

53. By recommending the creation of a HDV in the form of a Wholly Owned Company Limited by Shares, the following positive impacts will be realised:

Flexible and Familiar Structure – the structure is widely used and enables the Council, as the sole shareholder, to retain day to day Board control.

Joint Ventures – the HDV can participate in future Joint Ventures (JVs).

New Equity – provides a simple mechanism for the introduction of new equity and equity transfers.

Risk Sharing – split role of Board of Directors and Council as shareholder is well understood.

Independence – structure allows a degree of independence although the Council ultimately has control and can alter the management of the business through amending Articles of Association.

## **Actions to be taken to implement the decision(s)**

54. A key event and timescale schedule has been produced to ensure that the recommended decisions are implemented. The headline dates are as follows:

Jan 2019	Register Company, appoint Council Board Members
Jan to March 2019	Drafting of HDV structure, systems, policies and agreements
Jan to March 2019	Recruit MD, Admin, Finance Controller, Chair / Non-Exec
March 2019	Loan agreement signed, policies adopted
April 2019	Equity input, appoint staff and commence trading
April to Sept 2019	Appoint project teams, design projects and planning process.
July to Sept 2019	Construction tenders and contractor procurement
Oct 2019	Land transfer and commence construction
Jan 2020	First Development Loan drawdown
July 2020	First unit practical completions, first sales and lettings.
Dec 2020	Construction completes
March 2021	Final unit sales and lettings
April 2021	Development Loan repaid, Rental Phase commences

## **Appendices**

Appendix 1: Housing Delivery Vehicle Impact Assessment.

Appendix 2: Economic Development, Environment and Infrastructure Scrutiny Panel – Housing Delivery Vehicles (HDVs) – Action Plan.

## **Background papers**

<b>Body</b>	<b>Report title</b>	<b>Date</b>
Executive	Housing Delivery	12 June 2018