

Legal Memorandum

Subject: Establishment of a Housing and Regeneration Investment Company

Cabinet is advised that the establishment of either a Lewes company or a joint Lewes/Eastbourne company does not of itself commit the District Council to any particular project or to the development of any particular sites. The creation of a company simply provides the Council with access to a readymade housing and regeneration delivery vehicle which it can make use of quickly in the event that an appropriate opportunity presents itself.

ANY proposal that the council should commit expenditure or resources to any particular project will first have to be the subject of a Cabinet report containing a fully costed business case and viability assessment.

Further, the establishment of a company will be just one tool available to the Council to use for housing and regeneration delivery; its establishment does not preclude the use of other public sector or joint private/public sector partnerships.

1. Information

The Council has adopted a Council Plan for the period 2016 – 2020 and this Plan identifies the delivery of sustainable new housing and infrastructure as a key priority for the Council:

The Council Plan gives examples of current projects which are progressing this key priority. These include the joint venture with commercial partner Santon to develop over 400 new homes (40% affordable) as part of the North Street Quarter regeneration scheme in Lewes, and the Council's Local Growth Fund project.

1.1. National Context

The government encourages the establishment of local housing companies, providing this is done with the objective of providing new homes and not as a means of circumventing established right to buy provisions.

A written ministerial statement (originally dated 20 March 2015 and reaffirmed in March 2016) states:

“It is important that new council tenants should have access to the Right To Buy, and that new homes should not be built by councils which are excluded from the right to buy”

The Government recognise the benefits that public private partnerships can bring in supporting new forms of housing. The Government welcome approaches where local housing companies are developing new homes for market sale or purchasing private

rented homes for the accommodation of homeless households, through an appropriate legal entity structure and/or the borrowing does not count as public sector borrowing.

However, it is not acceptable for local authorities to establish new wholly owned or controlled housing companies deliberately to avoid the Government's reinvigorated right to buy policy and the limits on indebtedness put in place to help address the inherited deficit. Specifically, the Government will not support the establishment of such companies where they are developing or acquiring and retaining new social or affordable units for rental purposes. The Government believe that local authorities should support people to achieve their aspiration for home ownership through the right to buy."

1.2. Ownership Options

There are two primary options available to Lewes District Council in moving forward:

1.2.1. Establish a new joint housing investment company with Eastbourne Borough Council. There is scope for Lewes and Eastbourne to set up a joint housing investment company that create more formalised framework for sharing the skills, expertise and cost of existing officer support. An advantage of a joint company, as opposed to each council establishing its own company is that the larger entity would be expected to have greater market impact and to gain the benefit of economies of scale in procurement. The joint company would have the benefit of "in-house" support from officers at Eastbourne who already have experience of setting up and operating a housing company in a commercial environment.

In this scenario there are a number of options as to how a company is constructed to ensure that each Council's investments are equitable and that the money and assets of each Council are protected against future decisions made by either one.

1.2.2. Establish a Lewes District wholly-owned housing company. This option would not require specialist officers to be employed but could still make use of HEDP expertise, through the existing mutual co-operation agreement which exists between EBC, LDC and Eastbourne Homes Ltd.

In this scenario the two councils would each retain their own separate companies to take forward each authority's projects and to hold its own assets. Possible disadvantage of this option is that officers could have to duplicate work across the two Councils and have to service different companies with very similar objectives.

1.3. Housing Company Advantages

Subject to resource capacity there would be the opportunity to trade and export best practice beyond district and borough boundaries and generate income to the company which might then be invested in new housing and regeneration projects.

Such a company would have the ability to borrow money either from the councils or from the market and would be able to develop new housing and hold ownership of the housing to use or dispose of it as it saw fit.

A council-owned development company (joint or otherwise) would be able to:

- borrow for housing investment without being constrained by HRA borrowing restrictions, although the rules and principles around Prudential Borrowing would be applicable.
- develop a wide range of housing products across rented and owner occupied tenures that could be tailored to meet specific housing needs and priorities and so reduce demand for higher cost services, such as supported housing for older people at local and county level.
- choose to sell properties to residents at a discount if it so wishes, even though housing units built by the company would not carry a statutory right to buy
- choose its own rent levels for those units owned by the company for rent
- use any surplus earned from the sale of homes developed by the company for expenditure on any area of public service it chooses
- A joint approach would serve to share and dilute risks that may come with many potential investments

1.4. Housing Company Risks

However whilst the council (or the two councils in the case of a joint company) remain sole shareholder(s) it/they will carry the full risk of any investments that don't perform as expected or which generate losses rather than surpluses if, for example, the market dips. The company may also be left owning assets that it cannot sell or let. The company will be responsible for the repayment of any loans made to it by the council(s)

A joint approach may also create additional issues around control and governance that would need to be agreed by the District Council and the Borough Council in creating a joint company. Key issues to be agreed would be the precise objects of the new company, the content of the Shareholders' agreement and deadlock arrangements.

1.5. Other Legal Considerations

The interests of the company and each individual council would remain distinct. Internal arrangements would need to be put in place to ensure that both the councils and the company would have their own officer support for legal and financial advice. The company will be a separate legal entity. Decisions about the level of financial and in-kind support to give to the joint company (eg loans made to the company or guarantees given on behalf of the company) would remain as decisions for each individual council's Cabinet to make and there is no expectation that such support would be forthcoming without a rigorous viability assessment of any proposed project. The use to be made of the company's operating budget would be a matter for the company's Board of Directors to make. Directors would need to act in the best interests of the company when making Board decisions even if they are also

council members. Provisions about how to deal with conflicts of interests will need to be put in place.

It would be possible for the joint company to set up one or more individual subsidiary companies either as separate Lewes and Eastbourne asset holding companies or to deal with specific projects. This might be a suitable way forward in the case of major projects which involve an area specific to one of the two councils. This would allow assets and liabilities to be ring-fenced within the subsidiary company. The ability to do this is important to Lewes as it holds more land assets than Eastbourne. Any joint company structure will need to ensure there are mechanisms for agreeing apportionment of risk and profit between the councils. Lewes Council will want to ensure that Lewes District benefits from any profit made from District assets and at the same time does not take on undue Eastbourne risk.

One issue to be sorted in using subsidiary companies will be the extent, if any, to which the joint parent company might/might not be prepared to give any sort of guarantee on a project. This may differ according to the nature of the project. Subject to the content of any Business case it is anticipated that any company would be:

- a company limited by shares
- a wholly owned subsidiary of Lewes District Council and Eastbourne Borough Council
- set up with widely drawn objects but these are to include holding property assets, acting as landlord, selling property assets, providing specialist advice to third party bodies
- constituted so that all board directors to be Lewes and Eastbourne council appointees
- part of each Council's group accounts

In the event that any company is to be established, further thought will need to be given to the various options available to safeguard the interest of both councils. Matters to be considered include:

- objects of the company
- company structure and governance
- branding
- operating budget and funding
- possible secondment of staff to the joint company
- insurances
- directorships
- delegations
- control and minority protection
- shareholder's agreement, deadlock, conflict resolution
- ownership and management of properties developed by the company.
- Exit and termination provisions

In addition, formal agreements between the council(s) and the company will need to be entered into on those occasions when the council(s) provides the company with

financial assistance in cash or in kind eg. grants, loans, guarantees. Internal auditor should be provided with access to information held by the company and its subsidiaries. Procurement and state aid rules will still be relevant.

1.6. Pre-requisites to trading as a company

It is a statutory requirement that any local authority must prepare a detailed business case, including a risk analysis before embarking on trading through a company. That business plan must be approved by the Council (ie by its Cabinet in an executive model) before trading starts.

If the two councils wish to set up a joint company then each council will need to independently consider and approve that business case before trading can start. Government Guidance exists as to the way in which a Business Case and Business Plan should be produced.

2. Legal Implications

- 2.1.** There are a number of powers (including powers under Part II of the Housing Act 1985) that relate to the Council's ability to establish and participate in a housing delivery vehicle, as well as the power to provide financial assistance (eg loans and share capital) and land disposal powers. It will be important to fully address the conditions for the exercise of these powers as the arrangements are finalised as some of the powers (eg power to provide financial assistance for privately let housing and sale of housing land) legislate that any transaction undertaken will be void unless the detailed requirements of the specific provisions are followed. Where this sort of provision applies it will override the use of other more general powers such as the general power of competence referred to below. It is considered that these issues are all capable of satisfactory resolution within the current consent regime.
- 2.2.** Under Part II the Housing Act 1985 the Council has a duty to consider housing conditions in its district and the needs of the district with respect to the provision of further housing accommodation.
- 2.3.** The Council may provide housing accommodation directly but the Housing Act 1985 specifically provides that the Council does not have an obligation itself to acquire or hold any houses or other land for the purposes of its duties as a local housing authority under Part II of the Housing Act 1985.
- 2.4.** Alongside any other powers required for particular elements of this proposal, the Council can rely on its general power of competence under Section 1 Localism Act 2011 as its main power to facilitate the formation of the proposed housing delivery vehicle. This is a very broad power.
- 2.5.** The Council's strategy in setting up a new company and thereby holding some of its housing portfolio in a separate vehicle is, and needs to be, to seek to differentiate between its general needs housing stock and the housing that it develops for affordable rent and sale for the purpose of achieving *wider* community and regeneration objectives. The access routes to the affordable housing provided by the

two legal entities (ie. district council and the company) will be different. Affordable rental properties available through the company cannot be restricted to those eligible for access to the council's general HRA stock. These company properties will be available to economically active individuals with certain minimum income levels.

2.6. The business case needed to support the company's trading plans will need to show that it is capable of achieving wider reaching objectives, such as economic development, creating employment and training opportunities and attracting tourism to a specific geographic area in addition to providing housing.

2.7. Land Transfer Consents

2.7.1. Statutory land transfer provisions exist to protect land held by local authorities. Any proposed transfer of land from the Council to the company will need to be looked at on a case by case basis as different procedures need to be used depending on whether the land is HRA land or General Fund land and whether it is land which it is proposed to transfer at an undervalue.

2.7.2. Depending on the particular circumstances of the proposed transfer it may be necessary to obtain prior Secretary of Consent.

2.8. State Aid and Procurement

2.8.1. If the Council provides aid eg. makes a loan or provides a guarantee to the company, or transfers land to it at an undervalue and thereby favours the new company over other undertakings/organisations then this can amount to state aid. The award of such state aid may be made lawful providing such aid is given in compliance with the "Market Economy Operator Principle" (MEOP) which requires the council to act in a way that a private lender/investor might act in the same circumstances eg provide a loan on commercial terms and at a commercial interest rate having proper regard to commercial risk.

2.8.2. It is suggested this test might be satisfied by ensuring that external expert advice is taken by the council on those occasions it is considering making available a loan or similar benefit to the company to ensure it satisfies the MEOP and by ensuring that legal documentation is always drawn up between the council and the company setting out the specifics of the loan/benefit and a method for monitoring and potentially recovering aid.

2.8.3. It is possible that the Council may properly rely on the "teckal" exemption for services between the company and the Council (the company will need to remain solely in contracting authority ownership with its owners exercising a control which is similar to that which it exercises over its own departments and at least 80% of the company's work must be entrusted to it by the contracting authority owners – regardless of who the beneficiaries might be). This will need to be confirmed once the final structure is determined.

2.8.4. The company may also be a contracting authority in its own right and therefore subject to the public procurement regulations when awarding

contracts. This will depend on it being a “body governed by public law”. The company’s status in this regard will be confirmed once its structure is determined.

2.9. General Consideration of Council's Fiduciary Duty

2.9.1. In deciding whether and how to exercise its powers in relation to this proposal, Cabinet must consider the council’s fiduciary duty to conduct its administration in a fairly business-like manner with reasonable care, skill and caution along with a due and alert regard to the interest of the Council Tax payers.

2.10. Local Government Act 1999

2.10.1. Officers will need to have regard to the need for appropriate consultation during the development of this proposal.