Income generation from property and housing

CIPFA Society of District Council Treasurers

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What problem are you trying to solve?

- Balancing budget?
- Reducing demand?
- Resetting the relationship with communities?
- Social returns?
- Other benefits?

Income can be the key to doing more with less

Most councils continue to manage their finances proficiently and have become lean, but with large funding deficits still looming, income generation is an essential part of the solution to sustainable resource provisions of local services in the future.

Income generation has been made increasingly possible by:

- The General Power of Competence introduced following the Local Act 2003 and Localism Act 2011 which gives councils a greater degree of freedom to trade and charge
- The Public Services (Social Value) Act 2012 which provides councils with new commissioning powers to benefit from responsible procurement
- Recent cross sector market reforms which present councils with new opportunities to commercialise their services, ranging from housing and utilities to banking and international market trading.

Crucially, councils do not have to compromise their core principle of supporting their local communities. These social returns range from supporting local business employment and apprenticeships, paying a Living Wage and stimulating more affordable housing, through to protecting vulnerable communities and safeguarding the natural environment.

Different ways to generate income

Fees and charges

A fairer system where funding for core services can be protected, while discretionary services enjoyed by some but not all continue to be delivered at a reasonable price to the user. These may also be subsidised or delivered on a cost recovery basis.

Typical fees and charges include car parking, green waste

New areas include and developer planning applications, and private use of open spaces

Example: Cambridge sustainability design advice

Asset management

The council ensures that the fixed assets at its disposal generate revenue where possible to subsidise services while also supporting local employment, local business and other council priorities.

Typical assets to be sweated include buildings, and land.

New areas include water, wifi concession licensing, and sponsorship

Example: Cheltenham HQ purchase and lease

Commercialisation

There are some services that the council does or delivers well or where it has a competitive advantage. The council uses these to generate revenue by providing services to other parts of the public sector and private businesses.

Typical commercial services include utilities and leisure.

New areas include lettings agency, and interim workers

Example: Harrow Help-2-Let

Investment and ADMs

There is a variety of traditional and new innovative types of instruments for the council to fund and deliver income. These range from equity and debt through to council-owned or joint ventures, respectively. Different types will afford more control and social benefit to stakeholders.

Typical investments include housing and real estate.

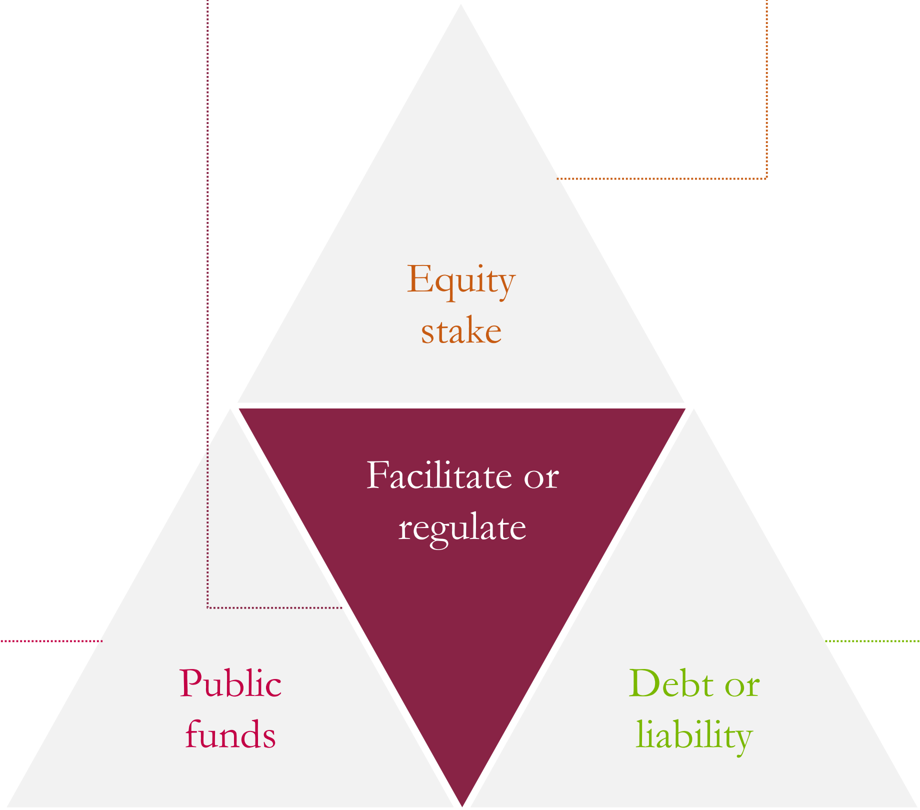
New areas include P2P green energy bonds and local development banks

Example: Warrington loans to housing developers

How to fund and deliver new income proposals

- Land Value Capture or developer tariffs
- Local taxes (eg BRR)
- Services fees
- Pollution charges
- Sustainability Supplementary Planning Guide (SPG)
- Place-based Corporate Social Responsibility
- Crowdfunding and open source

- Revolving funds or cost recovery
- Joint purchasing agreements
- Pooled financing agreements
- Local development banks/funds from muni pensions
- Government grant and EU growth funds



- Financial contribution to PPPs or Special Purpose Vehicles (SPVs) delivering infrastructure, delivering services or developing land
- Equity funding from investment banks
- Enterprise Zones (EZs) whereby the council owns the land or contributes other asset

- Municipal bonds or unitary funds
- Climate derivatives
- Public or private loans (eg PWLB)
- Social impact investors and micro-creditors
- Sukuk
- Tax Increment Financing

Aspects in a strategy to make opportunities a reality

- **Your goals aligned to core mission** (vision of success, financial, delivering social value)
- **Political dimension** (buy in and journey of change as a 'commercial council')
- **Baseline of your current position** (current activities and gaps, sector performance benchmarks)
- **Prioritisation of new opportunities** (gateway process, risk-reward criteria, long list to short list)
- **Budget** (P&L analysis, forecast, funding model)
- **Capacity building** (fill skills gap, raise awareness vs. self sustain, culture change)
- **Governance** (implementation plan, member scrutiny)
- **Communications** (internal vs. external, brand)

Income generation: A housing development vehicle

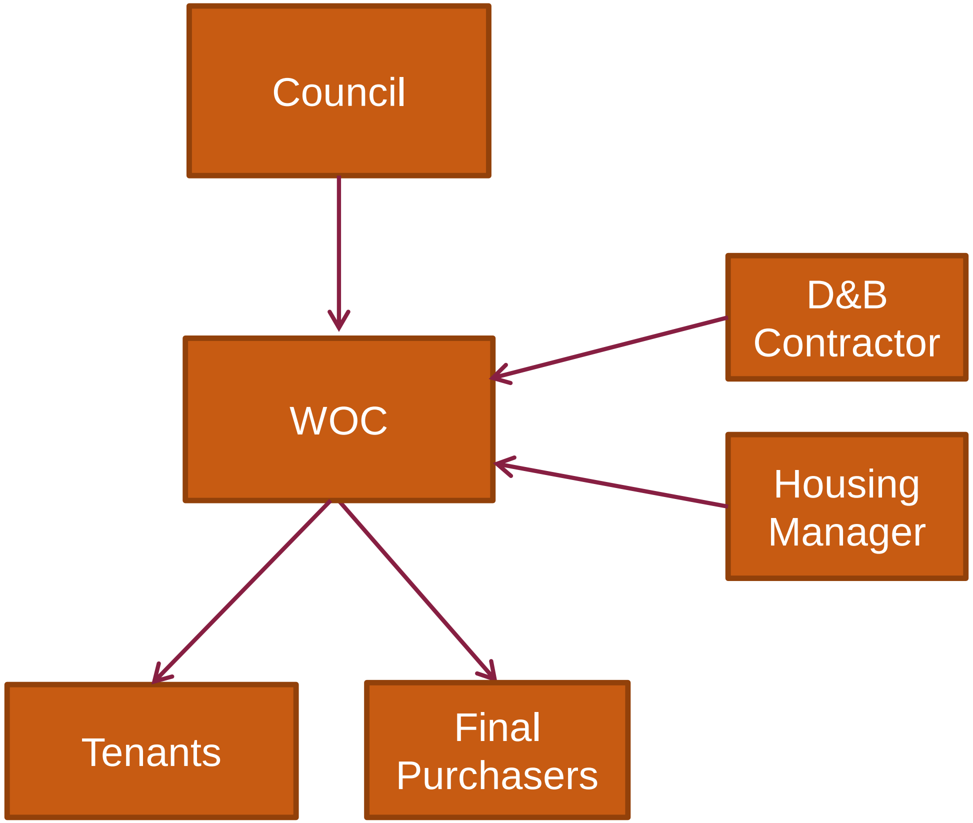
What is it?

- a corporate entity which acts as a housing developer
- will have its own Board of directors
- takes on development risk (and lettings risks for rental stock)
- Council has an ownership stake – possibly 100% depending on approach
- Council may invest land/cash – receives share of profits

Why?

- to generate an **on-going revenue stream** through rental income
- increase **housing supply**
- better control over **tenure and quality**
- create homes **outside the HRA**
- make good use of **surplus Council owned land**
- use **Right to Buy receipts**

Example 1: Wholly Owned Company (WOC)



WOC – key features

- Set up as a trading vehicle as a Company Limited by Shares
- Council transfers land/assets into WOC at best consideration
- WOC funded by prudential borrowing on-lent by Council or 3rd party funding
- Council on-lends at PWLB rate + margin, to ensure State Aid compliance
- Council may also provide equity via the purchase of share capital
- WOC sells market and shared ownership units; retains private and affordable units
- WOC may contract with housing management agent for management and maintenance services
- Net operating cash flow repays the WOC debt
- Distributions made to the Council or held in the WOC to fund

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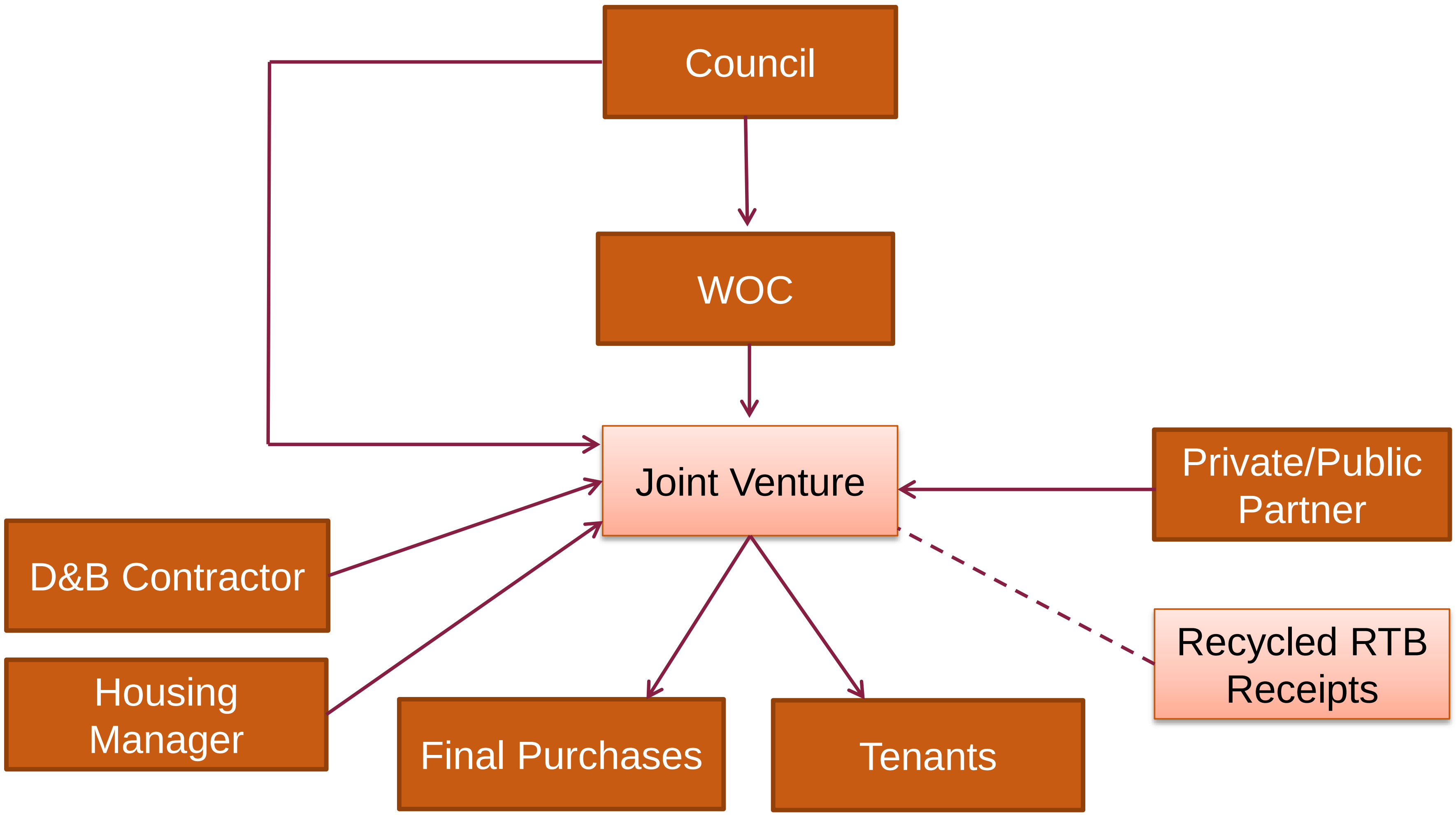
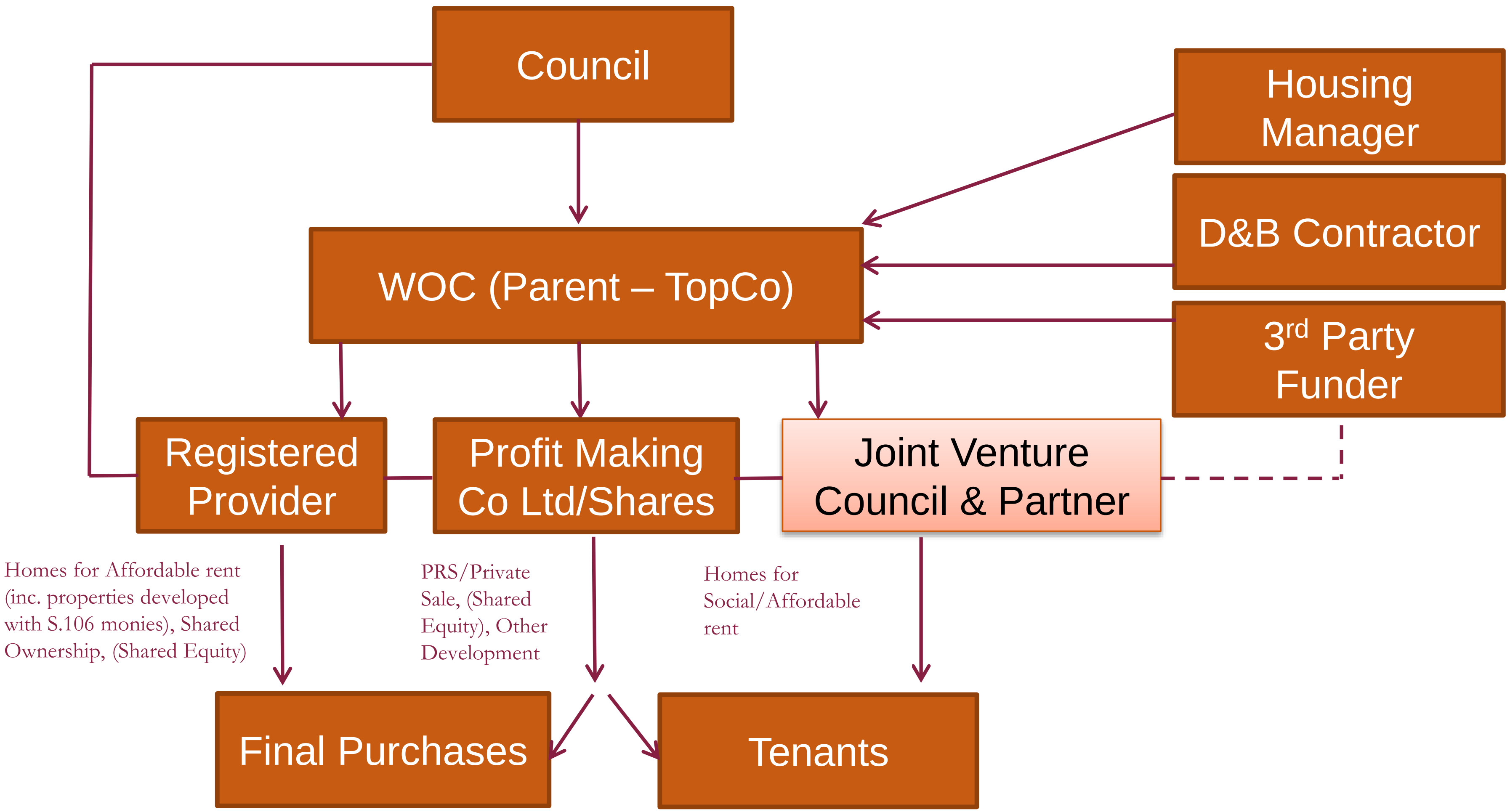
Example 2: Corporate Joint Venture (JV)



JV – key features

- JV may be structured as a Company Limited by Shares or a Limited Liability Partnership (LLP)
- Council transfers land into the JV as its equity contribution
- Council's land value recognised as a loan note which accrues interest payable to the Council
- Private sector partner provides equivalent equity investment into the JV, also as a loan note with interest payable
- Alternatively a public sector partner may provide land/assets or funding equivalent to the Council's investment
- Right to Buy receipts may also be used if JV not controlled
- Additional development finance secured through senior debt procured by the private sector partner; Council also has the option to provide additional funding
- JV sells market and shared ownership units; may retain private and affordable units or sell to third party investor/RP
- Cash waterfall repays senior debt, loan notes, and then profit distribution

Example 3: Hybrid Structure



Hybrid structure – key features

- Council sets up "TopCo" as a wholly owned subsidiary (company limited by shares)
- Flexibility to establish a Registered Provider (RP) to hold affordable housing, a "profit making" company limited by shares, and a JV (which could be a LLP) with either a public or private sector partner as subsidiaries of the TopCo
- Can choose which structure to use on a development by development basis, rather than lock into a single structure with potentially a solitary partner
- Options to fund entities via Council on-lending, equity contributions from Council and partner, and 3rd party debt.

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Key considerations

	Wholly owned company	Joint Venture	Hybrid structure
Company structure	Typically company limited by shares (CLS)	May be company limited by shares or limited liability partnership (LLP)	TopCo will be CLS, options for CLS or LLP below
Funding	Council on lends PWLB and provides equity as share capital Options for 3rd party funding	Partner provides cash equity; JV raises senior debt	Could be combination of WOC/JV approaches
Control	High	Medium	High/Medium
Risk	High	Medium – shared with partner	High/shared with partner depending on project
Return	Takes 100% of profit	Shares profit 50/50 partner	100% or 50/50 depending on project
Resourcing	Reliant on Council resourcing and experience or will need to buy in services	Levers in development experience of partner	Can be tailored to requirements of project

Summary - choosing the appropriate structure

"Stand-alone" WOC

- popular with councils as it maximizes control and return without sharing profits with a partner;

JV

- more prevalent for larger long term phased development and regeneration projects over a number of years;

Private sector partner

- brings development experience and reputation in the property market;
- enhances confidence of funders and end-purchasers in deliverability and value;
- the Council must accept dilution of profits and control;

Public sector partner

- provides opportunity to pool resources such as land and funding
- reduces reliance on external funding which may carry higher risk or interest.
- RTB receipts available could be used within a property vehicle if council does not control.

Hybrid structure

- more flexible and enables Council to respond to the nature of the development opportunity
- allows for engagement with an RP, which could also be a subsidiary of the Council.

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He is the team lead on Income Generation, leading assignments for the City of Wolverhampton, Warrington Borough Council, Sefton Metropolitan Borough Council, Greater Manchester Fire & Rescue, and Watford Borough Council

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Robin is a qualified Chartered Accountant with many years experience of housing, development and regeneration projects. He has previously worked for the HCA (and its predecessor, English Partnerships) where he was responsible for establishing public:private delivery vehicles for development and housing projects. Having then been the finance director of a city development company, he now leads advisory assignments on a range of real estate development related projects for clients across the UK, including assisting numerous Local Councils to establish housing delivery vehicles.

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