

### Other considerations

This appendix summarises some of the wider considerations that will form the work streams of the Council in setting up the HIC. These have been built in to the Implementation Plan in Section 12 of the main report Considerations include:

#### **State Aid**

When providing resources to the HIC, in the form of debt or equity, the Council must be careful not to set an artificially low interest rate or advantageous loan terms, as it must be satisfied that its on-lending does not constitute State Aid i.e. that it does not provide an unfair advantage to the SPV by offering loan finance at a lower interest rate or on better terms than would be secured by commercial competitors.

Any loan would have to be tested with regard to State Aid by reference to the "Market Economy Lender Principle" (MELP) similar but not identical to the Market Economy Investor Principle (MEIP). That is to say, provided that the Council could demonstrate that it was acting as any comparable lender in the commercial market would do then no unlawful State Aid would arise. This is typically assessed by comparison to the EU reference rate for comparable loan arrangements, and by comparison to market rates secured by similar entities (for example Registered Providers delivering affordable housing and more recently the use of loans by the HCA and LEP network).

In practice any loan provided to the entity will be at a margin to the PWLB rate at which the Council borrows. This margin would provide a revenue return to the Council's General Fund.

The Council would need to consider the SPV's business model and its ability to meet loan repayments from the returns generated by its business activities once it has taken account of all other costs.

The Council may also wish to consider the overall structure of the HIC. Under certain circumstances, the Council may be able to provide finance on a level below market levels, when delivering affordable housing units. However, the construct of this, with the dilution anticipated by the private for sale and rented units would need to be further considered.

#### **Legislative change**

The Government suggested that in future the role of these companies would be scrutinised with powers to either inhibit the use of these companies or indeed return any affordable housing held within these companies back to the HRA.

To date, it is unclear whether the government would make a change in legislation to allow this intervention, however, it remains a risk that the Council must consider.

#### **Legal challenge of tenants**

As a relatively new vehicle for local government, it is unclear as to whether the legal framework that prevents tenants acquiring affordable units held within 100% owned housing companies under RtB legislation is robust and would withstand challenge.

There has yet to be a case against a LHC and given the recent Government directives there remains a risk that a challenge could be successful.

### **Local Authority Land**

In relation to land held in the Housing Revenue Account (HRA land), Section 32 of the Housing Act 1985 allows Local Housing Authorities to dispose of housing land but only with the consent of the Secretary of State. The Secretary of State (DCLG) has published a series of general consents since 1985, the latest being The General Housing Consent 2013 published in March 2013. The 2013 General Consent is split into four separate consents. The most relevant is "A: The General Consent for the Disposal of Land held for the purposes of Part II of the Housing Act 1985-2013."

The General Consent draws a distinction between vacant land and dwellings. A Local Housing Authority may dispose of a dwelling provided it is at market value. However there is an important exception to this: a consent is required where the transfer of a vacant dwelling is to an entity in which the local authority has an interest (whether majority or minority) if it is the sixth or later such transfer of a dwelling (taken individually) in the relevant financial year. Therefore, the Council would only be able to dispose of up to five dwellings to the HIC in one financial year before having to obtain DCLG consent.

The disposal of non-housing (non-HRA) land is covered by separate legislation:-

- Section 123 of the Local Government Act 1972
- Section 233 of the Town and Country Planning Act 1990 where the land is held for planning purposes.
- Section 123 states that local authorities, except with the express consent of the Secretary of State, cannot dispose of land (other than a short tenancy not exceeding 7 years) for a consideration less than the best consideration reasonably obtainable.

For non-HRA land, the Secretary of State has issued a General Disposal Consent, known as "the Local Government Act 1972: General Disposal Consent 2003" (CLG Circular 6/03). The 2003 consent allows local authorities to dispose at up to £2 million less than best consideration if the purpose for which the land is disposed of is likely to contribute to the promotion or improvement of the economic, social or environmental wellbeing of its area (subject to compliance with the State Aid rules).

Section 24 of the Local Government Act 1988 provides the Council with the power to provide a wide range of financial assistance to the HIC, including making a grant or loan to it. As the HIC is a body corporate, the Council may under Section 24(2)(d) acquire share or loan capital in it. Under Section 1 of the Local Government Act 2003 a local authority can borrow for any purpose relevant to its functions under any enactment. The Council can therefore borrow with a view to making loans by way of financial assistance under Section 24 of the Local Government Act 1988.

Any capital funding requirements for the HIC in any financial year will need to be allowed for in the Council's budget strategy (including its annual borrowing limit). Whilst borrowing may be undertaken by the Council at generous rates from PWLB, any loan from the Council to the HIC must be at rates and on terms which are State

Aid compliant. This will mean a margin can be achieved by the Council on the borrowing and lending rate.

### **Key operational considerations**

The SPV. would assess viability and risk through the development of a business model.

The financial model must be robust and prudent, recognising operational risks and providing financial resource to minimise such risks. Key considerations include:

- Management Structure of the HIC
- Responsibility for the management and maintenance services required for the properties;
- Influence of the Council in the operation of the HIC;
- Management of the records of the HIC;
- Staff structure;
- Contractual relationship with external suppliers;
- Flow of funds between the HIC and the Council; and
- Use of surpluses within the HIC.

### **Risk and mitigation**

HIC directors have a responsibility to the HIC for ensuring that the HIC remains a "going concern". In some instances the HIC may operate at a loss in the early years but as a going concern, the HIC would be assumed to be able to continue in business for the foreseeable future and able to realise its assets, discharge its liabilities, and obtain refinancing (if necessary) in the normal course of business. This would be managed through regularly reviewing performance against the business model and ensure there is sufficient contingency and risk mitigation in place.

There are a number of material risks that the Council must consider when operating a housing company model. Each risk will not be unfamiliar to the Council, as they are similar risks that the Council manages through its HRA housing stock. However, in order to make each scheme self-sustaining there is a need to manage each of these risks on a scheme level rather than across a portfolio.

The risks include all the general operational risks of a housing developer, but also include the significant political risk of the local authority as a public body. How the HIC manages these risks are key to the success of the HIC going forward.