

SOUTH DEVON RURAL HOUSING ASSOCIATION LTD

Board of Management

B221014(2)

Development Company Rural Homes Limited – Consider Confidential

FOR DECISION

Purpose: To inform the Board of Management of progress on key and emerging projects and business opportunities.

REPORT

Rural Homes Limited

Rural Homes Limited was acquired/set up by SDR and is a wholly owned subsidiary, one share issued to SDR. Initially it was set up for use as a potential development company to undertake development projects, which would provide tax efficient savings, for SDR, Cornwall Rural Housing Association (CRHA) and Cornwall Community Land Trust (CCLT). In the event CRHA and CCLT were not supportive and SDR did not have a project which would have justified the start up costs of the company at that time. Since that time the company has been dormant. All background papers relating to the original proposals have been re-distributed with Board papers for information.

As part of the due diligence on the proposed plans to redevelop Brimhay, senior staff looked at the implications of undertaking the whole of the redevelopment itself. Current rules allow housing associations to dispose of assets without tax if they have been previously occupied and used for social purpose i.e Shinnars Bridge Cottages. HA's are also allowed to sell land, without incurring a tax liability if this has also been used or designated for social use (proposal to sell land to facilitate ROC development). However, with the current plans SDR intends to develop and sell up to 12 new homes on the open market. If this continued as an SDR development, SDR would be liable for corporation tax on the profit from open market sales, which could be substantial. Given that we are anticipating 'surplus' of around £1 million the corporation tax payable could be in the region of £230,000. However if Rural Homes develop the homes, they are allowed to gift aid the equivalent value of the corporation tax back to SDR (as a charity) as long as Rural Homes is wholly owned by the Charity. The potential tax advantages could be significant.

There are also VAT savings should Rural Homes be the developer for the project. They would be able to procure services with zero per cent VAT. An independent report has been commissioned on VAT issues.

Traditionally SDR has not included on costs in relation to previous development activity and of course we have not had any dedicated development staff or department. Most HA's would put a cost to this and indeed that cost would form part of the overall cost of development projects. A typical overhead allowance would be approximately 4%. SDR's management costs would be reduced during the development period as staff would be seconded to the project and payable by Rural Homes as part of the development costs. There would also be other cost reductions for services provided to Rural Homes by SDR, whilst these have not been fully assessed they could be significant, with a positive effect on SDR surplus.

Company Structure.

It is proposed that Steve Prime Head up the Company as Managing Director on a short contract (to reflect the development period) with full Contract and Job Description based on the anticipated time he spends on the contract with an agreement from SDR that he is seconded to the company. This will mean a corresponding reduction in his SDR salary. It is further proposed that Alan Fox be appointed a director in the post of Director of Development and New Business, on a zero hours contract, remuneration determined by the projects he will be involved in. Alan will be one of the signatories on company accounts for contracts and finance, and general business. Other services such as finance, payroll and other office services could be by a service agreement with SDR at agreed rates. In respect of Board structure it is proposed that Steve and Alan be board members along with two further board members (yet to be sourced) with one a current SDR board member and another to demonstrate independence from the parent company.

Contractual arrangements with Rural Homes

Subject to independent advice on proposed contractual arrangement between SDR and Rural Homes, it is anticipated that initially, in respect of Brimhay, three contracts will apply:

1. SDR contracts with Rural Homes to construct the intermediate rent units on a project management basis. SDR to be responsible for contractual payments direct to the main contractor and agreeing to pay Rural Homes a fee on a normal contractual basis.
2. Rural Homes develops out the homes for open market sale as a traditional developer, purchasing the land (open market plots) from SDR at open market values. (Supported by loans from SDR at commercial rates)
3. Rural Homes will act as project managers for QSH on normal contractual terms to construct the 15 bed supported housing dwelling to be leased by SDR on a 21 year lease, ROC providing support to SDR tenants.

Other contracts including proposed development contracts for South Hams District Council, could be project managed by Rural Homes. Initial talks with SHDC indicated they would be willing to use this route.

A bank account has been set up for Rural Homes Limited with Natwest at the Local Bank in Totnes. As it is considered a new business, two years of free banking is offered. An operating overdraft is not considered necessary, given the proposed facilities agreement between SDR and Rural Homes.

Supporting Documents and Reports

- | | |
|------------|--|
| Appendix 1 | Independent VAT Report |
| Appendix 2 | Advice on Corporation Tax - to follow |
| Appendix 3 | Proposed changes to Articles and Memorandum |
| Appendix 4 | Proposed facility agreement SDR to Rural Homes |

It is proposed that:

Rural Homes be structured to achieve the above:

Approve appointment of Officers and initial Board Members;

SDR contract with Rural Homes ASAP to develop Brimhay and agree necessary service agreements;

Nomination for an SDR Board member to serve on the Board of Rural Homes Ltd;

SDR provide a £10,000 initial loan to Rural Homes Limited @ 6% to enable them to trade.

All other contractual arrangements to be approved by the board.

Recommendations

Board Members to approve the recommendations.