City of Westminster Cabinet Report

Meeting or Decision Maker:	Cabinet
Date:	12th July 2021
Classification:	General Release *(Appendix 2– Exempt from public disclosure)*
Title:	Westminster Builds Business Plan 2021/22
Wards Affected:	All
Cabinet Member/Lead Member:	Cabinet Member for Communities and Regeneration
Key Decision:	Yes
Financial Summary:	The Westminster Builds Business Plan sets out the planned activity of the company over a 15 year period. Through a £0.8bn capital programme funded by £0.5bn of income, the company plans to deliver 2,000 new homes.
Report of:	Debbie Jackson, Executive Director of Growth, Planning & Housing and Gerald Almeroth, Executive Director Finance & Resources

1. Executive Summary

1.1. The report sets out the context of the Westminster Builds business plan being brought forward for approval. The business plan sets out the direction and planned activity of the Council's wholly owned housing and development company Westminster Builds over the next 15 years. The plan is considered annually by the Council as sole shareholder and lender so that the company has authority to proceed with work progressing schemes.

1.2. The business plan includes an intention for Westminster Builds to develop a pipeline of activity within Westminster but also outside of the borough. After further consideration the Council has taken the decision to pause this activity at the current time with the need to focus on Council led schemes. Further work will now need to be carried out to ascertain the impact on the business plan of this change. This will feed into the next refresh of the plan and the Council's budget setting process.

1.3. Given the scale of investment required into the company over the longer term the Council commissioned an independent review of the business plan and this report sets out the key findings from that. Overall, the plan was assessed as sound but with a few areas for consideration or action which are being addressed.

2. Recommendations

2.1. That Cabinet is recommended to:

a) Approve the Westminster Builds Business Plan as outlined in Appendix 1 to this report excluding the out of borough 'pipeline' element.
b) Note that the Business Plan will be revisited to consider the implications of the removal of the out of borough pipeline element to feed into the forthcoming budget setting process and the approval of the 22/23 Business Plan.
c) Consider the findings from the independent review of the business plan and note the actions being undertaken as a result of that review

3. Reasons for Decision

3.1. To agree the Business Plan for the Council's wholly owned housing and development company Westminster Builds. It is a requirement that Westminster Builds seeks approval of its business plan on an annual basis so that it has the authority to proceed with work on progressing schemes and incurring operating expenditure contained in the plan. It should be noted that further approval is required from the Council in respect of each capital scheme before committing financially to these, in accordance with the Council's capital scheme governance processes.

4. Background, including Policy Context

4.1. In December 2017 the Council took a decision to set up a wholly owned housing company to help deliver the Council's ambition to increase the supply of affordable housing within Westminster. At that time, it was also agreed to set up a second wholly owned housing company where appropriate for tax efficiency purposes.

4.2. In June 2018 Westminster Housing Investments Limited (WHIL) and Westminster Housing Developments Limited (WHDL) were incorporated at Companies House. Both WHIL and WHDL are now collectively known under the trading name of 'Westminster Builds'. This single brand creates an identity which is distinct from the Council whilst remaining part of the Westminster family.

4.3. Westminster Housing Investments Limited (WHIL) is an investment vehicle designed to own completed properties to generate net rental income for the longer term. Westminster Housing Developments Limited (WHDL) is the development vehicle acquiring land and developing properties for a range of tenures.

4.4. The Council owns 100% of the shares in WHIL and WHIL owns all of the shares for WHDL. The Council is currently the sole shareholder and principal lender to WHIL and indirectly to WHDL. The company is funded by a mixture of quasi equity or shareholder's loans and debt financing which is provided through the Council's General Fund.

4.5. The Council's objectives in setting up the company were set out in the 2017 Cabinet report as follows:

Wholly Owned Housing Company Objectives	
1.	Extend the Council's resources by working with the Council (where the Council's view is that other delivery partners are neither available nor appropriate) to deliver the regeneration, and new build or acquisition opportunities being identified by the Council.
2.	Operate on a commercial basis but offering new tenures and, in particular, intermediate tenures to extend the range of provision available for Westminster residents
3.	Work to the scale and pace set by the Council.

4.	Work to the Council's quality standards to help ensure quality housing is provided for all income ranges

4.6. Company directors are all appointed by the Council and the management and day to day operation of the company is undertaken by Council officers under a Service Level Agreement (SLA) with the Council.

4.7. Structures and processes have been put in place within the company to ensure that its activities are adequately controlled. Whilst ultimate responsibility remains with the Council, day to day control of Westminster Builds is the responsibility of the company's board of directors.

4.8. The board is responsible for the delivery of the business plan. This includes decisions regarding development and acquisition and changes to project/scheme appraisals and financial modelling. However capital schemes and their investment requirements follow the Council's normal approval and governance processes and as such the annual approval of the Business Plan is 'in principle' and subject to subsequent Council approval processes for each scheme. Also, any changes to the Business Plan and/or additional funding requirements would require further council approval.

Introduction to the Business Plan

4.9. The Westminster Builds Business Plan sets out the activity that the company plans to carry out over the next 15 years in order to achieve the objectives that have been set for it. These plans are subject to Council decision at every stage, first via this report and then individually for each scheme. In addition, for schemes on Westminster land, the Council will approve the preferred delivery route for each of the specified schemes. The full business plan document is set out in Appendix 1.

4.10. At the heart of the business plan is the delivery of an ambitious programme to deliver 2,000 homes through a £0.8bn capital programme funded by £0.5bn of income. Delivery of these homes is either through direct development undertaken by the company on behalf of Westminster Council, development in partnership with an external entity or through acquisition of units outside of Westminster or from council led schemes.

4.11. The overall company vision is stated as:

'By delivering high quality, modern homes for people from all backgrounds, the Company aims to: Build better homes, Build a better city, Build a better future".

4.12. Since the Council is about to embark on a number of large regeneration and development projects and a role is envisaged for Westminster Builds, it seems sensible to revisit the purpose and objectives for the company as part of the review and agreement of this business plan and consider whether the business plan will enable Westminster Builds to deliver the role envisaged.

Business Plan headlines

4.13. The key planned activity for the company over the next 15 years as set out in the Business Plan is:

- Plans to develop 1,656 homes across a mix of tenures (market sale, market rent, intermediate and social rent) and acquiring a further 291 intermediate rent units
- Retaining a management portfolio of 921 homes let at either intermediate or market rent with an annual turnover of £21m
- The company can repay its borrowings in 2058, which is within the 40 year cashflow period
- At the end of the development and acquisition programme in March 2030, Westminster Builds holds assets valued at over £400m

4.14. Obviously the removal of the out of borough pipeline will change these numbers.

4.15. The company has a funding requirement from the Council through a debt and equity injection of £797m over the next 15 years. The company plans to make repayments back to the Council through sales receipts and development profit of £468m during that same period. The Council funding request from the current Business Plan has been included as part of 2021/22 budget setting process.

4.16. The company is projected to return a loss on its profit and loss account for the current year and up to 2023/24. This position reflects the normal development cycle whereby the company is in the development phase for a number of projects and is incurring the normal running costs of the company without any contribution from scheme profits or asset rental income. This position will change as receipts are achieved from sales and the company begins to hold completed income returning units.

4.17. Individual scheme approval and financing requirements will be assessed through normal governance routes for the Council capital Business Cases (if over £10m), which is reviewed by the Capital Review Group and then decision via Cabinet Member Report.

4.18. In addition to Council led schemes, the Business Plan also includes an intention for Westminster Builds to develop a pipeline of activity both within Westminster (beyond the Council-led schemes) but also outside of the Borough. This is to support the long-term growth of the company, to provide affordable homes for those who live and work in Westminster but wish to live outside and commute to their jobs, to diversify risk and build a longer term revenue stream. This element of the business plan has been given further consideration by the Council and is not deemed a priority for the company at this time given finite capacity and the need to focus on the Council-led schemes; a recommendation is therefore sought for approve of the business plan excluding the “out of borough” pipeline. Further work will need to be undertaken to fully understand the risks and benefits of these proposals before any commitment is given to an expansion of activity beyond Westminster.

4.19. Whilst the business plan will need to be revised following this decision, other schemes ready to progress within the plan will continue to be assessed and approved individually on their own merits as they come forward for decision through the Council’s capital scheme governance processes.

Independent Review of Business Plan

4.20. Given the scale of investment required into the company, the Council commissioned an independent review of the Westminster Builds Business Plan.

4.21. The Council commissioned 31ten consulting to undertake the review which was agreed to cover the following scope:

- Comment on quality of the business plan
- Review of underlying assumptions supporting the business case
- Review of risks and mitigation measures
- test robustness of business plan through stress testing

Headline Findings from the Review

4.22. The review looked at the quality of the Westminster Builds Business Plan and the financial model and assumptions that underpin and supports it. Overall, the review found that the structure and the narrative of the Business Plan was clear and includes the majority of the aspects that they would expect to see. However, they raised a number of areas for consideration or action as outlined below.

Objectives

4.23. The business plan would benefit from giving the reader a clearer narrative around the objectives of the company to include how these reflect the Council’s initial objectives for the company. The objectives should represent SMART targets that ultimately can be used to judge the performance of the company.

Risk

4.24. Although included throughout the report, the narrative that sets out the company's risk management strategy, its identification and management of risk, and the overall impact of risks could be improved. It is usual for a Business Plan to have a stand-alone section on risk.

Assessment of Financial Model

4.25. The model was found to be technically correct and did not show any mechanical or formula-based issues. However, there was an element of hard coding found within the model which makes assumptions harder to track, sensitivity testing more difficult to perform and increases the risk of errors in future updates/changes.

4.26. In addition, several tax treatments need to be reviewed throughout the model.

Stress Testing

4.27. When assessing the sensitivity of the model to changes in assumptions it was found that inflation was a key driver in the future success of the company. The business plan assumes that market sales and market rent growth out strips cost inflation. Whilst this may be true over the longer term, there is significant risk that short term implications could negatively impact on both the company and the return to the Council.

4.28. Sensitivity analysis on the key drivers of the business plan model showed most risks were categorised as low or low to medium. Those risks that were categorised as medium or medium to high were the impact of market sale inflation and an increase in the funding interest rate. It is suggested that it would be prudent for Westminster Builds to set out in the business plan ways in which it would seek to manage this impact.

Next Steps

4.29. Overall, the findings from the review show that the business plan is broadly sound with a number of areas of improvement highlighted. These have been discussed with company directors and an action plan is included within Appendix 2 to outline how these key risks and recommendations will be managed going forwards.

5. Financial Implications

5.1. The business plan sets out the capital expenditure plans and revenue running costs for the company over the next 15 year period. The annual running costs of the company are estimated at £750k per annum and the capital expenditure plans total £0.8bn over the period. At the end of its development and acquisition programme in March 2030, Westminster Builds holds assets valued at over

£400m. These figures include out of borough activity contained within the current business plan.

5.2. The company requires funding from the Council in the form of debt and quasi equity totalling £0.8bn over the period. The company’s debt peaks at £270m in 2026/27 whilst delivering two of the largest schemes in the business plan, Church Street and Ebury Phase 2. Under current assumptions, Westminster Builds can fully repay its borrowings in 2058 demonstrating that the Business Plan is self-sufficient within the 40-year cashflow period.

5.3. The funding requirement from the council through loans and quasi equity was included within the Council’s general fund capital programme as part of the 2021/22 budget setting process.

5.4. The recommendation not to progress the out of borough pipeline will reduce the capital expenditure requirement of the company by £5.5m in 2021/22 and £147.7m over the life of the business plan. Withholding approval of this element will necessitate an updated version of the business plan to be brought forward in 2021/22. However, since none of those affected schemes are planned to complete until 2023/24, in the Council’s opinion there is no short-term detriment to the plan. The Directors of Westminster Builds have signalled that this is anticipated to impair the longer-term profitability of the company but that this is not currently quantified and so will require further review. It has been agreed by the Council that this can take place as part of the next annual cycle of the business plan.

5.5. The Council will be regularly monitoring a range of key performance indicators for the company in its role as shareholder and lender. Overall, the Council will be monitoring financial performance against the business plan in terms of quantum and timing of expenditure and income, the company’s annual profit and loss position and the funding requirement from the Council and planned loan repayments. Other areas to be monitored are the company’s Interest Cover Ratio (ICR) and Loan to Value (LTV).

6. **Legal Implications**

6.1 The Council has the power to set up companies or bodies, which they own. Section 1(1) of the Localism Act 2011 introduced the “general power of competence” for local authorities, defined as “the power to do anything that individuals generally may do” and which expressly includes the power to do something for the benefit of the authority, its area or persons resident or present in its area. The generality of the power conferred by subsection (1) is not limited by the existence of any other power of the authority which (to any extent) overlaps the general power.

6.2 Section 4(2) of the Localism Act 2011 provides that where, in exercise of the general power, a local authority does things for a commercial purpose the authority must do them through a company.

6.3 Section 95 of the Local Government Act 2003 authorises the Council to do for a commercial purpose anything which it is authorised to do for carrying on any of its ordinary functions (other than where it is under a statutory duty to provide that function) however, this power is only exercisable through a company such as Westminster Builds. The Council needs to articulate clearly its objectives to justify the use of a Westminster Builds and to demonstrate that it is not seeking as its prime purpose in setting up a WOC to avoid legal or policy constraints that would otherwise apply.

6.4 Section 111 of the Local Government Act 1972 enables the Council to do anything which is calculated to facilitate, or is conducive to or incidental to, the discharge of any other of its functions, whether involving expenditure, borrowing or lending money, or the acquisition or disposal of any rights or property.

6.5 The Council has power to borrow under the Local Government Act 2003 subject to complying with the rules on prudential borrowing and provided that any borrowing is in line with the Council's treasury management policy and budgetary frameworks, and in particular the setting of the Council's overall capital financing requirement.

6.6 Separate powers are available to the Council in relation to the funding of the Westminster Builds for the provision "privately let housing accommodation". For the privately let housing accommodation (which would include both market and affordable rented housing), the Council may also rely on both:

- Section 1; and
- Section 24 of the Local Government Act 1988 – power to provide financial assistance for privately let housing accommodation. (The provision on of financial assistance under section 24 requires Secretary of State consent if utilised)

If you have any queries about this Report or wish to inspect any of the Background Papers, please contact:

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APPENDICES

Appendix 1 -Westminster Builds Business Plan 2021/22

Appendix 2 -Action Plan from Independent Review (Exempt)

BACKGROUND PAPERS

Review of Westminster Builds Business Plan (Exempt)