

**Wiltshire Council**

**Shareholder Group**

**25 January 2022**

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**Subject: Stone Circle Company Business Plans 2022/23**

**Cabinet Member: Richard Clewer, Leader of the Council**

**Key Decision: Key**

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### **Executive Summary**

This report seeks the Shareholder Group's consideration of the 2022/23 business plans proposed by the Stone Circle companies as required under the shareholder agreement.

### **Proposal(s)**

The Shareholder Group is asked to:

1. Agree the Stone Circle housing company business plan 2022/23
2. Agree the Stone Circle development company business plan 2022/23
3. To note the Stone Circle companies will be providing more complete Business Plans as identified in the style suggested in the Governance Review over the next 12 months.
4. To note that authority remains delegated to agree the project plan for each development proposed by Stone Circle Development Company Limited to the Corporate Director Resources (S.151 Officer) in consultation with the Leader.
5. To note that authority remains delegated to the Corporate Director of Resources (S.151 Officer) to conclude detailed contract arrangements and serving of required notices under the shareholder agreement with and on the Stone Circle Companies including changes to the resourcing contract.

### **Reason for Proposal(s)**

The shareholder agreement between the Council and the companies requires the companies to present their proposed business plans to the Council at least three months before the start of the financial year in question.

This report is the outcome of that proposal and the consideration by the Shareholder Group of amended business plans for the forthcoming financial year, which follows a review of the governance of the Stone Circle Companies to ensure that they support the growth of the companies and protect the interests of the Council as shareholder.

**Terence Herbert**  
**Chief Executive**

## **Wiltshire Council**

### **Shareholder group**

**2 February 2021**

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**Subject: Stone Circle Company Business Plans**

**Cabinet Member: Councillor Richard Clewer, Leader of the Council**

**Key Decision: Key**

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### **Purpose of Report**

1. The purpose of the report is to seek consideration of the business plans proposed by the Stone Circle Companies as required under the reserved matter 26 of the shareholder agreement after a review of governance was undertaken to support the growth of the companies and protect the Council's interests as shareholder

### **Relevance to the Council's Business Plan**

2. The proposals in the report directly support the Council's business plan to Grow the economy by facilitating the provision of affordable homes and developing new housing on public land.

### **Background**

3. The Cabinet agreed to establish the companies at its meeting on 23 July 2019. Each January Cabinet should consider the business plans proposed by the Stone Circle companies as required by reserved matter 26 of the shareholder agreement.
4. The cabinet agreed a review of governance arrangements for Council owned companies at its meeting in September 2021. Following the review it was agreed to establish the Shareholder Group to undertake the reserved matters for the Council.

### **Main Considerations for the Council**

5. The Cabinet received the business plan proposals from the Stone Circle companies following their board meetings in February 2021
6. Following the Governance Review proposals accepted by Cabinet at its September meeting there was a request for those business plans to be updated.
7. As shareholder the Council should consider the merits of the business plan proposals in line with the strategic plans and priorities the companies were originally set up to achieve. In addition, any specific risk and/or financial

considerations, as well as governance issues, that are specific to the Council in its role as shareholder should also be considered for the year ahead.

8. The Business Plans received continue to grow and build upon the original rationale for the establishment of Stone Circle companies.
9. The following sections pick up the specific proposals in the business plans proposals and any changes from the last business plans approved.

#### 10. **Stone Circle Housing company**

11. The housing company has been acquiring properties in the strongest housing market since 2006. The Nationwide building society identified a 10.4% increase in house price growth in 2020/21. The Company is now making offers for properties at 125% of the original business case. As of January 2022 the company owned 42 properties with the total acquisition price being £ 43k above the original business case. As of January 2022, there are 11 properties under offer albeit at up to 125% of original business case. Within the portfolio there are properties leased to Alabare Christian care to provide accommodation for young people and there are further purchases programmed to be made for that purpose.
12. Appendix A contains the Stone Circle Housing company business plan. The plan is based on acquisition prices at October 2021 prices plus 10% reflecting the strength of the market. Based on the original business plan parameter of 3.6% interest rate the business plan does not break even until 2037/38 and the cumulative break even point (clearing debt accumulated up until 2037/38) is not reached until 2049/2050. The fundamental reason for the change in fortunes of the company is the significant increase in acquisition prices but rents only increased by CPI.
13. As shareholder there are four options available to the Council;- not agree the business plan proposal for 2022/23 in terms of acquisitions so that the company does not grow, close the company and take the properties back and determine next steps as the Council has no defined exit strategy if this scenario were to arise, agree the business plan at the existing rate of interest but indemnify the company for its losses until the break even position is achieved or agree to charge a lower rate of interest on the loans so as to support a more viable business plan.
14. If the Council did not agree the proposed business plan and future property acquisitions the following issues will require consideration. The original purpose of the company was to provide sub market private rented accommodation that could be offered to households outside the Council's allocations policy as well as to grow the value of the company. To date the majority of the properties purchased have been used for homeless prevention and also to provide accommodation for young vulnerable people. The business plans shown that over the 50 year plan the company will have fixed assets of considerable value debt free. The current business plan is a victim of the strength of the market, pausing acquisitions would be a relevant consideration if there is strong likelihood of market correction. Even if that

were the case the Company starting acquisitions again in the future may be faced with similar prospects in relation to the divergence of acquisition price and rents. Moreover, halting the business plan at this stage would mean that acquisitions would not be available to address homeless prevention which in turn impacts on demand for affordable housing and the value of the company would not increase and as such the original objectives of the company would not be met. Thus this option is not recommended.

15. The Council as shareholder could close the company. The company properties are mortgaged to the Council so the Council could take the properties back as mortgagee in possession and employ its homeless powers to retain the existing tenants in the properties until they were successful in receiving an offer of affordable housing to meet the Council's statutory obligations in relation to homelessness. When vacant the properties could be sold so as to redeem the Council's debt. Initial valuation of the portfolio by the Council suggests there would be sufficient value to redeem the Council's debt and costs. Clearly, this option would not achieve the Council's original objectives, would lead to families having to move home , with additional impact on the affordable housing stock in Wiltshire and there would be reputational impact for the Council. Thus this options is not recommended.
16. The Council could indemnify the Company so that it can continue trading on the original business plan. Although this would achieve the original objectives of the company it would expose the Council to significant financial risk and so that options is not recommended.
17. The company is requesting that the Council as funder reduces the interest rate on loans to 2%. As shown in appendix A this will deliver the business plan in terms of acquisitions and long term growth in value of the company and the potential losses of the company are mitigated. This will reduce the margin on the loan that the Council is currently receiving, however that margin was not been factored in to the MTFS in future years. If the company delivers the business plan as proposed it will break even quicker. The shareholder group will need to determine which option they wish to approve as part of the Business Plan approval.

### **Stone Circle Development company**

18. Stone Circle development company business plan is at appendix B.
19. As of January 2022 the company has five sites being progressed which in total could deliver 128 units. Priestly Grove is expected to be considered by planning committee at its February meeting, the planning application for Ashton Street Trowbridge was submitted 15<sup>th</sup> October 2021, Marlborough resource centre planning application has been submitted, subject to board meeting and project plan approval planning application for Tisbury sports centre will be submitted and Stoneover lane Royal Wootton Bassett is subject to pre- application planning advice.

20. It is recommended to include the Council owned site at Horton Rd Devizes in the 2022/23 business plan. This site subject to planning could deliver in region of 42 homes.
21. The base business plan shows loan repayment to the Council at the end of each project rather than the return from a project rolled forward into the next project to offset borrowing costs. A sensitivity analysis is included to show the impact of a 5% increase in costs of construction and a 10% increase in value of property ( the same assumption used for the housing company). This shows a significantly improved return from the projects.

### **Stone Circle Holding company**

22. The business plan for Stone Circle Holding company is not included as all costs are recharged and thus captured in the Stone Circle housing and development company.

### **Resourcing contract**

23. Subject to the previous recommendations concerning the company business plans the companies will enter into a new phase of operation. Stone Circle housing company portfolio will be such that it is viable to employ a dedicated housing manager and that is included in the business plan. As such the resourcing contract will no longer include that function. As Stone Circle development company moves into the delivery phase its is viable for it to employ a construction manager and that is included in the company business plan. It is likely that there may be other functions that the companies will wish to directly provide rather than purchase via the resourcing contract. It is recommended that the resourcing contract provide either party to provide at least three months notice of any changes in the resourcing contract if changes are to be requested.

### **24. Overview and Scrutiny Engagement**

This report has not been considered by financial planning task group .

### **Safeguarding Implications**

25. There are no safeguarding implications stemming from this report.

### **Public Health Implications**

26. There are no public health implications as a direct result of this report.

### **Procurement Implications**

27. There are no procurement implications as a direct result of this report.

### **Equalities Impact of the Proposal**

28. There are no equality impact implications stemming from this report.

## **Environmental and Climate Change Considerations**

29. Stone Circle housing company has committed to improve the EPC rating of the properties it purchases where economic to do so. Stone Circle development company has submitted the first project plan that includes an all electric development installing air source heat pumps. The company aims to build homes for life which minimise the carbon footprint within the overall economics of development.

### **Risks that may arise if the proposed decision and related work is not taken**

30. If the decisions are not taken the companies will not deliver the property acquisition and development proposed. Stone Circle housing company will therefore not be able to meet housing need identified and Stone Circle development company will not be able to deliver the anticipated financial return to the Council.

### **Risks that may arise if the proposed decision is taken and actions that will be taken to manage these risks**

31. The potential risks generated from the proposals are mainly financial. The Council has a number of mechanisms to control and or mitigate the risks if it agrees the proposed business plans. Firstly, the shareholder agreement provides on going oversight of the operations of the companies. Secondly, the Council provides the loan finance for the companies. Lastly, in relation to Stone Circle development company the Council has reserved the right to agree the project plan for each development before it proceeds within the shareholder agreement.
32. There may be financial and reputational risks to the council if the governance of the Stone Circle Companies is not kept under review.

## **Financial Implications**

### **Holding Company**

33. The Holding Company costs are all recharged to Stone Circle Housing and Development Companies. The cost assumptions included have been prepared by the Housing Company and are forecast costs based on experience from trading to date and factoring in an increase in staffing for a Housing manager and Construction manager .

### **Housing Company**

34. Two business plan models have been presented for the Housing company. For both models cost assumptions have been updated by the company and the plans are based on different assumptions to the 2021/22 business plan. The most significant differences are that :

- a. future value gain/loss on property is only being included in the first two years in the new business plan and at a higher rate whereas they were included for all future years in the approved 2021/22 business plan. This could be seen as a more prudent approach or an underestimation .
  - b. A different assumption has been made for repairs and lifecycle costs. The 2021/22 plan made an allowance per property for repairs and lifecycle costs whereas the new model is based on a % of the rental income for both repairs and lifecycle costs, this has generated a significant reduction in forecast costs in the new business plan of circa £19m. It is recommended that the shareholder group seeks assurance on the justification of the revised figures to ensure they are not underestimated.
35. Both models have revised operating costs which include the recharge from the Holding company and includes the increased staffing. The model also assumes an increase in house purchase price from the 2021/22 Business Plan to reflect the current market, the model is based on October 2021 prices plus 10%.
36. The Base model is based on an interest rate of 3.6% which is the approved interest rate. Based on the new assumptions in the business plan this model shows that the company will break even (Profit before Tax, excluding FV gain/loss on property) in year 17, 2036/2037 and cumulatively in year 28, 2047/2048. The comparative figure in the approved 2021/22 business plan was year 14, 2033/2034 and year 21, 2040/2041.
37. At the end of the 50 years in year 2069/70 the business plan shows there will be a loan outstanding of £12m, in the 2021/22 business plan the loan outstanding was £14.7m
38. The interest payable to Wiltshire Council in the 2021/22 business plan was £86.2m for this period, with a premium of 0.7% at £16.8m. The revised business plan shows interest payable of £102m. Assuming the same borrowing rate at 2.9% Wiltshire Council would earn a total interest premium of circa £19.8m for the period 2022/23 to 2069/70.
39. In the business plan the Loan is based on a revolving Loan facility so that any cash surplus over £4m is used to repay the Loan. Interest is compounded so is not paid until the end of the term. This is a similar approach as taken in the 2021/22 Business Plan.
40. The main points for consideration here are supporting a business plan which has reduced maintenance costs and an extended breakeven point as both of these come with risk.
41. Due to the extended breakeven point the Housing Company have presented a second model that works on the same assumptions but assumes a lower



interest rate of 2%. This would see the company breakeven in year 3, which is next financial year 2022/23.

42. The Loan balance in 2069/70 would be £4.6m and would be fully repaid by 2071/72.
43. The interest payable to Wiltshire Council would be £44.7m (period 2022/23 to 2069/70) but crucially given current borrowing rates if Wiltshire Council borrowed now to on lend it would not make an interest premium.
44. Interest premium is not currently built into Wiltshire Council 2022/23 MTFS.

### Summary Table

	50 year Total - to 2069/70			
	2021/22 BP	Base Plan 3.6%	Base Plan - Interest rate @ 3%	Base Plan - Interest rate @ 2%
	£'m	£'m	£'m	£'m
Revenue	£190.364	£219.723	£219.723	£219.723
Operating Costs	£50.085	£47.941	£47.941	£47.941
Interest Payable 2022/23 to 2069/70	£86.223	£102.235	£71.060	£37.284
Corporation Tax	£27.222	£13.241	£19.164	£25.582
Profit Before Tax (excluding FV gain/loss on property) - Break even year	14	17	9	3
Profit Before Tax (excluding FV gain/loss on property) - Break even year	2033/2034	2036/37	2028/29	2022/23
Profit Before Tax (excluding FV gain/loss on property) - Amount	£0.023	£0.023	£0.019	£0.138
Profit Before Tax (excluding FV gain/loss on property) - Cumulative Break even year	2040/41	2047/48	2033/34	2023/24
Profit Before Tax (excluding FV gain/loss on property) - Cumulative Break even Amount	£0.271	£1.057	£0.182	£0.244
Interest Rate Payable by Stone Circle	3.60%	3.60%	3.00%	2.00%
WC Borrowing rate assumed	2.90%	2.90%	2.00%	2.00%
WC Premium	0.70%	0.70%	1.00%	0.00%
Interest Premium	£16.766	£19.879	£1.000	£0.000
Loan balance in 2069/70	£14.664	£12.020	£0.000	£0.000

### ***Changes in Assumptions***

Property Maintenance and Lifecycle Costs	£31.132	£10.985	£10.985	£10.985
FV gain/loss on property	£89.978	£110.266	£110.266	£110.266

### **Development Company**

45. The base business plan model has been updated by the company and the plans are based on cost estimates as of 2022 prepared by the company, with revised operating costs which include the recharge from the Holding company and includes the increased staffing.

46. The base model is based on an interest rate of 7% which is the approved interest rate. In the business plan the Loans are per scheme and interest is compounded and is not paid until all the schemes complete. The Loan principal is repaid as each scheme completes. This is the same approach as taken in the 21/22 business plan and mitigates risk as each Loan is secured to a development.
47. Upon review it would appear that the Sales do not align with current programme delivery and that some may actually fall into the next financial year. It is recommended that this is reviewed.
48. The business plan covers the period up to 2024/25 and shows a total Net income of £1.134m.
49. For this period the company would pay £4.233m in Interest to Wiltshire Council, Wiltshire Council would earn an interest premium of circa £3m.
50. The Net Income of £1.134m could come back to Wiltshire Council as Dividend or be reinvested into future activities.
51. The sites included in the business plan are Wiltshire Council sites that would be sold to the company. The capital receipt earned for these sites would be circa £1.560m, this is assumed to take place at the point of sale.
52. Loan premium and Dividend are not currently built into Wiltshire Councils MTFS.
53. The company has also presented a model where the Loan is not repaid until all schemes complete. It is recommended this model is not accepted. Linking Loans to development mitigates risk.

## **Legal Implications**

54. The Stone Circle housing company and development company business plans must be approved by the Shareholder Group on behalf of the Council as ultimate shareholder in accordance with the Shareholder's Agreements. For the avoidance of any doubt, the holding company business plan must also be approved by the Shareholder Group on behalf of Council as the ultimate shareholder in accordance with the shareholders agreements, however the holding company business plan is set out within the housing company and development company business plans.
55. The financing arrangements have been structured in accordance with state aid law. The Council will need to continue to monitor interest rates to ensure state aid law requirements continue to be met. These arrangements were put in place prior to exiting the EU – so subsidy control (previously called state aid) will apply.
56. The Council needs to continue to ensure that as the companies develop the governance arrangements for the companies are robust, transparent and fit for purpose.

## **Workforce Implications**

57. There are no direct workforce implications stemming from this report.

### **Options Considered**

58. The options available to the shareholder in relation to the Stone Circle Housing company are as set out above and it is recommended that the Council agrees a business plan based on a revised interest rate on loan finance. The Council could decide not to approve the Stone Circle development company business plan but that would lead to the Council incurring cost to address the work that has been undertaken on the sites already agreed to be developed. The Council could decide not to offer the Horton Rd Devizes site to Stone Circle development company but to offer the site to the market for disposal but that would not generate the best overall return for the Council and as such is not recommended.

### **Conclusions**

59. This report proposes business plans for the Stone Circle Companies as required under reserved matter 26 of the shareholder agreement. The revised plans will allow the companies to respond to the changed economic circumstances in Wiltshire in the residential property market.

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Report Author:

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Perry Holmes, Director of Legal & Governance / Monitoring Officer  
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Date of report 25<sup>th</sup> January 2022

### **Appendices**

Appendix A to B – Exempt information – Summary business plans for Stone Circle housing company, Stone Circle development company and Stone Circle holding company.

### **Background Papers**

Business plan and Stone Circle Company board minutes.