

# Merantun Development Limited Sub-Committee

**21 December 2020**

Wards: Cricket Green, Figges Marsh, Ravensbury

## Merantun Development Ltd: Company Progress Report

Lead officer: Chris Lee, Director of Environment and Regeneration  
Lead member: Councillor Mark Allison, Leader of the Council  
Councillor Martin Whelton, Cabinet Member of Housing, Regeneration and the Climate Emergency  
Councillor Tobin Byers, Cabinet Member for Finance  
Contact officer: Chris Lee, Director of Environment and Regeneration

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### Recommendations:

- A. To note the decision of the Merantun Development Ltd (MDL) Board that the business case is no longer viable and not to proceed with the development of sites.
  - B. Note that LBM owned land will not be transferred to MDL.
  - C. Note that the business case for the development of Private Rented Sector housing at the scale set out in MDL's business plan is no longer viable and to commence the process for closing down the company.
  - D. The Sub-Committee agrees in principle to wind up the company and to authorise the Shareholder Representative (Chris Lee, Director of Environment and Regeneration), in consultation with the Chair of the MDL Sub-Committee, the s151 officer and Monitoring officer, to agree the process to be followed with regards winding up the company and act on behalf of the Shareholder with regards any resolutions that may be required.
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### 1. PURPOSE OF REPORT AND EXECUTIVE SUMMARY

- 1.1 The purpose of this report is to update the Shareholder Sub-Committee on the outcome of the review of Merantun Development Limited's business plan and board decisions to halt development of sites at Farm Road, Canons Place, Elm Nursery and Raleigh Gardens and the review of MDL's business plan.
- 1.2 Merantun Development Ltd was incorporated to deliver a mix of private rent and affordable housing on small sites that would contribute towards Merton's housing targets and generate a revenue return to the Council's general fund.
- 1.3 The original Business Plan anticipated that there may be a need to exit or 'jump off' at various points depending upon market conditions and the financial outlook of the Council. MDL now believe that one of those points has been reached
- 1.4 A number of factors have impacted on the original business plan such as increases in costs of construction, costs of borrowing, Covid-19 and Brexit

impacts leading to a softening in the housing market. Collectively, these impacts mean that the business case to deliver private rented sector homes as set out in MDL's business plan is no longer viable. This alongside the financial challenges facing all Local Authorities as a consequence of Covid and other matters means that the appetite for risk is reduced.

- 1.5 The Board of MDL has approved the 'jump of point' – receipt of planning approval – to not progress the development further and, as a consequence, determine that the closure of the company should be undertaken.

## **2. DETAILS**

- 2.1 Good progress was made in the preparation of the development of MDL's first four sites; successfully securing planning permission in July 2020.
- 2.2 External factors, many as a consequence of Covid-19, are having an impact on the economy and the housing market. MDL as a matter of course, undertook a review of its business plan following the successful granting of planning approval.
- 2.3 MDL's business plan recognised that there would be a number of main decision points as to whether it should progress from design, development and planning to construction tendering and then to construction and letting.
- 2.4 The company reached a decision point and reviewed its income and cost projections, particularly in light of COVID 19, and the ensuing macro-economic risks. Following on from the Sub-Committee report of 12<sup>th</sup> October; MDL's board in dialogue with Merton Council as shareholder and funder undertook a review of Merantun's business plan and determined that the project is no longer viable.
- 2.5 It is important that the Merantun Sub-Committee recognises that the state of the housing market is currently very fluid and challenging and that in the business plan review one of the key 'jump off points' was considered by MDL. The returns to MDL no longer meet the Company business plan objectives and that the purpose in the short to medium term was no longer viable. In dialogue with the Council as shareholder and funder, it has been proposed that the Company should be voluntarily wound up.
- 2.6 Covid-19 has also had an impact on the Council's finances and the Council's appetite for risk and investment has diminished when considered alongside the review of the MDL business case.

## **3. ALTERNATIVE OPTIONS**

- 3.1 Whilst the Merantun Board and Shareholder representative have recommended closing down the company and its activities the alternative options included:
  - Develop 3 sites for full market sale (High risk in the current housing market and requires significant capital outlay)
  - LBM sell all sites with planning permission for maximum capital receipt; transfer of the four sites to MDL would only have been undertaken had there been a viable business plan after the receipt of planning permission. As the

sites are not being transferred it will be for the council to dispose of the sites with the benefit of planning permission.

#### **4. CONSULTATION UNDERTAKEN OR PROPOSED**

4.1 None for the purposes of this report.

#### **5. TIMETABLE**

5.1 The timetable to conclude the Company's business will be determined by the process that is followed and requirements of Companies House. Some time will be needed to conclude the planning s106 agreements and reconcile any outstanding invoices for creditors.

5.2 The timetable will be reported to the Council's Shareholder Representative.

#### **6. FINANCIAL, RESOURCE AND PROPERTY IMPLICATIONS**

6.1 The following tables highlight the financial implications of the proposal for LBM to borrow to lend to MDL to facilitate the construction of homes to generate a financial return to the Council.

6.2 The original business case contained a number of assumptions for financial return which, in light of emerging events, have now significantly and adversely moved. This has led both the MDL Board and Council Officers to conclude that the scheme is no longer financially viable for both parties and that the opportunity to 'jump off' as included in the original business case should be enacted

6.3 The tables highlight the movements in the key modelling assumptions from the original business case to the latest projections. It can clearly be seen that the costs have increased and the potential return to the Council significantly reduced.

6.4 Members will also note that under present circumstances the Company will not be in a position to fully meet its interest payments until 2039/40. The loan from the Council will not be repaid until 2049/50. It should be noted that no loan has been made, but if a loan was to be made at this point in time it would not be repaid until 2049/50. This contrasts to the modelling done in 2017 where the loan would have been paid by 2039/40.

6.5 This, together with the significantly reduced return on investment (6.48% reduced to 2.94%) over a 30 year period, leads to the conclusion that this project represents too high a risk for it to remain a viable proposition.

6.6 In addition to the above the experience of Croydon Council and the problems it has with its Housing Company, together with the restrictions Central Government are placing on Councils to prevent 'speculative investments', will act as a deterrent to investments of this nature going forward.

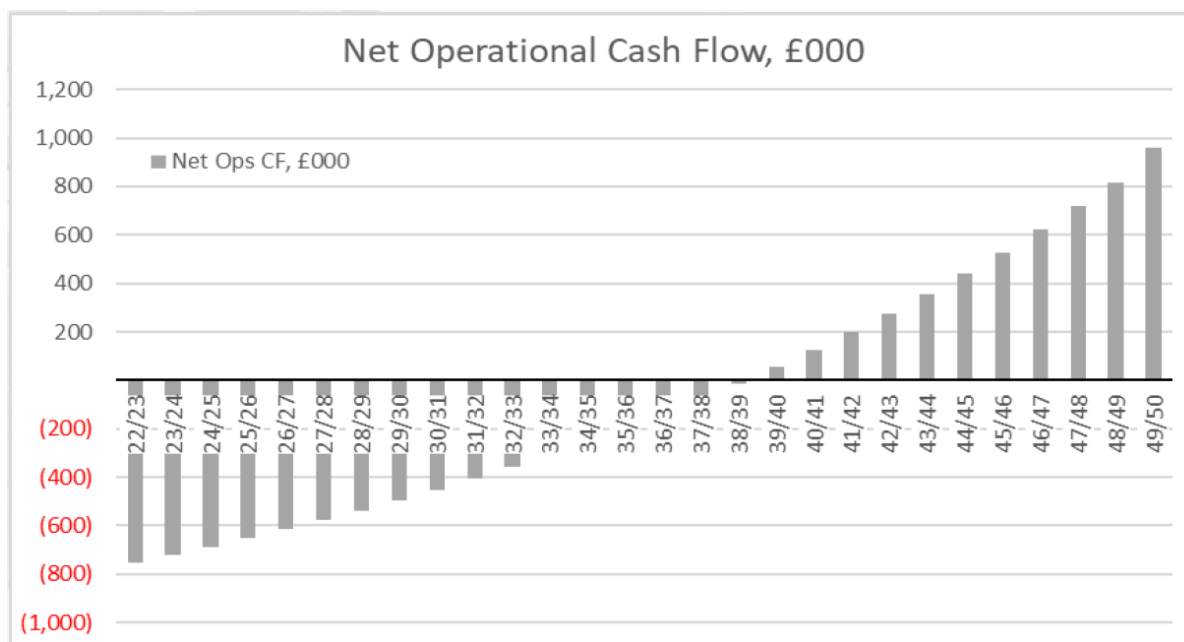
6.7 Finally, the Council's current budget constraints, due in some part to Covid, has significantly reduced the risk appetite for such investments.

6.8 **Key Modelling Assumptions (2017 vs 2020 Models)**

<b>Assumptions</b>	<b>APR 2017</b>	<b>JUL 2020</b>	<b>Change</b>	<b>%, change</b>
Private	2	10	8	400%
Affordable	20	0	(20)	(100%)
PRS	53	62	9	17%
Commercial units (trading space)	2	0	(2)	(100%)
<b>Total units</b>	<b>77</b>	<b>72</b>	<b>(5)</b>	<b>(6%)</b>
<b>Unit sale proceeds</b>	<b>5,953</b>	<b>5,253</b>	<b>(700)</b>	<b>(12%)</b>
<b>Development costs</b>	<b>18,383</b>	<b>19,470</b>	<b>1,086</b>	<b>6%</b>
<b>HPI (% p.a.)</b>	<b>4.50%</b>	<b>2.00%</b>	<b>(3%)</b>	<b>(56%)</b>
<b>Rent (% p.a.)</b>	<b>4.30%</b>	<b>4.30%</b>	<b>0%</b>	<b>0%</b>
<b>Interest rates:</b>				
PWLB loan to GF interest rate	2.76%	3.76%	(1%)	(36%)
GF loan to WOC margin	3.74%	3.74%	0%	0%
<b>Borrowing rate</b>	<b>6.50%</b>	<b>7.50%</b>	<b>(1%)</b>	<b>(15%)</b>

<b>Modelling results</b>	<b>APR 2017</b>	<b>JUL 2020</b>	<b>Change</b>	<b>%, change</b>
PWLB draw down	16,278	19,426	(3,148)	(19%)
PWLB loan retirement	31-Mar-38	31-Mar-46		
<b>Loan to WOC</b>	<b>13,022</b>	<b>15,541</b>	<b>(2,519)</b>	<b>(19%)</b>
Cash equity in WOC	3,256	3,885	(630)	(19%)
Land equity in WOC	8,190	4,970	3,220	39%
WOC loan retirement	31-Mar-42	31-Mar-50		
<b>Cumulative I&amp;E Impact (project end)</b>	<b>67,451</b>	<b>31,852</b>	<b>(35,600)</b>	<b>(53%)</b>
Cumulative I&E impact (year 5)	1,214	1,665	452	37%
Equity IRR (cash and land)	<b>6.48%</b>	<b>2.94%</b>	<b>(3.5%)</b>	<b>(55%)</b>
Interest cover (max in year shortfall)	<b>(286)</b>	<b>(636)</b>	<b>(350)</b>	122%

## 6.9 2020 Model Cash-flows (operational less annuity loan repayments)



6.10 The Company will determine any remaining liabilities and reconcile outstanding payments and invoiced as part of the closure process.

6.11 Should Members agree to the winding up then officers will ensure the final accounts reflect this and liaise with the Company's external auditors. We will also need to reflect any losses resulting from winding the Company up into the Council's accounts.

## 7. LEGAL AND STATUTORY IMPLICATIONS

7.1 Under the Shareholder Agreement, it is a reserved matter (Reserved matter 8) that it is for the council as shareholder to make the decision with regards passing any resolution for winding up or presenting any petition for its administration (unless it has become insolvent).

7.2 If the Council as shareholder decides to wind up the company, the process by which this is done will be dependent on the assets and liabilities the company holds. If the company has no assets or liabilities, then a voluntary strike off would be available and this would not require the instruction of a liquidator. This process is relatively simple and could be commenced on the Shareholder passing a resolution to institute a process leading to the winding up of the company. If the Company does have assets and is solvent, then the process to be followed would be a member's voluntary liquidation, which is a longer process and involves the appointment of a liquidator.

7.3 With regards recommendation D, S101 of the Local Government Act 1972 permits the sub-committee to authorise an officer to act on its behalf in relation

to the Reserved Matters contained in the Shareholders Agreement including the making of resolutions in relation to the winding up of the company.

**8. HUMAN RIGHTS, EQUALITIES AND COMMUNITY COHESION IMPLICATIONS**

8.1 None for the purposes of this report.

**9. CRIME AND DISORDER IMPLICATIONS**

9.1 None for the purposes of this report.

**10. RISK MANAGEMENT AND HEALTH AND SAFETY IMPLICATIONS**

10.1 None for the purpose of this report.

**11. APPENDICES**

- None

**12. BACKGROUND PAPERS**

- None