Rebooting the housing co-op movement

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Introduction

There has been something of a renaissance of interest in housing co-ops in the past few years. The co-op that I am a member of - The Drive Housing Co-operative in Walthamstow, north east London - is part of this recent wave, set up by a group of people who were looking for an alternative housing solution for themselves, and as a potential model for others.

We get a regular stream of enquiries at The Drive from people interested in knowing how we went about setting up the co-op; through my work with Radical Routes and Co-operatives London, I know of yet more groups trying to start up co-ops. But very few manage to proceed to acquiring property and housing their members - and in a number of cases, not through lack of trying.

I am aware that the founder members of the The Drive had a lot of the necessary expertise "in house" or through friends and contacts, and I try to do my bit to help these new groups who don't have such ready access to the expertise they need. Through speaking to them, and my own recent experience at The Drive, I think that I have a good picture of the challenges facing new housing co-op startups at the moment.

Since being involved with The Drive, I've become more engaged with the wider co-operative movement, and I've studied the fact that the housing co-op sector doesn't seem to function as a coherent whole in translating this current level of interest into growth of itself.

The rest of this paper contains my personal views as to why this is currently the case, and what may be done to change the situation.[1]

Housing Co-op vs Co-operative Living

Housing co-ops come in all sorts of different shapes and sizes - from an estate of purpose-built flats in south London to five people sharing a Victorian terraced house in Bradford. Yet all are currently seen from the outside (and even sometimes from the inside too) as the same thing: a housing co-op.

I'd be the first person to admit that being in a housing co-op is not for everyone: whatever the kind of co-op, meetings and administration take time and commitment, and require very good communication skills.

I would also be the first to admit that living in non-self-contained accommodation is not suitable for everyone. But I do believe, for those who can do it, that it can be the closest form of housing co-operation - and it happens to be the part of the housing co-op movement that I am in.

To distinguish between the two, I use the term *co-operative living* to describe co-ops that not only provide housing for the members co-operatively, but where the members live together co-operatively on a day to day basis. In practice, this means living in non-self-contained accommodation with pooled resources that would certainly include food/cooking, but may also extend to other things too. In co-operative living, members apply collective decision-making not just to the running of the co-op which provides the accommodation, but also to the running of the household too.

For example, at The Drive we share the following resources:

- We pay money into a kitty and purchase fresh organic vegetables from a local food-growing co-operative (Organiclea), and non-perishable foodstuffs and household

1 Credit goes to Jon Fitzmaurice for coining the term "reboot", during a discussion we had on this topic

supplies from Suma Wholesale (which is also a co-operative). This gives us affordable access to organic food, supports other co-ops and supports local food-growing.

- We take it in turns to cook dinner each evening. This functions as the social centre of the household, and encourages each of us to develop our cooking skills and eat more healthily than we might perhaps otherwise. It also reduces food packaging and food waste.
- We have pooled together our books and CD collections in the library.
- We have pooled together our tools in the workshop, creating a dedicated space for bicycle repairs or household maintenance; the co-op is also purchasing tools and materials for the workshop.
- Two vehicles - a hatchback car, and a van - are available for co-op members to use.
- One member has made a grand piano available for everybody's use - and there's also a house guitar.

Last but by no means least, we benefit from sharing space: the square-footage in our building would be barely enough to provide very small self-contained units for the ten members, but by taking one room each (it's one bath/shower room between two), we collectively have the use of: a lounge/dining room; library; two kitchens; conservatory; dedicated laundry room; bike workshop; and basement storage. It certainly doesn't feel like people are crammed in, when utilising the space in this way.

Although some of the analysis below would also apply to other types of co-ops too, it is co-operative living that I am particularly focussed on, both out of personal interest, and because I believe that people who want to make a positive choice to live in this way ought not to have to face so many challenges in order to be able to do so.

Housing Co-ops vs Housing Associations

I should also point out that, in the main, I am writing in relation to housing co-ops that are not Registered Providers (AKA Registered Social Landlords). A number of housing co-ops were set up prior to 1990 when they were eligible to receive government funds (Housing Association Grant) and mostly were large-scale new-build schemes, done in conjunction with local authority support, whilst others obtained “short life” leases on local authority owned properties usually at peppercorn rents. The type of organisation thus created is very different in practice, despite the commonality of name, with the much smaller and more recent co-ops that are financially independent of the social housing sector. This type of funding is not available to new co-operatives and therefore small, independent housing co-ops (such as Radical Routes member co-ops) are what I am interested in, as a model for the future.

Current Model of setting up housing co-ops

In the current model, a housing co-operative is registered as a Co-operative Society (AKA "bona fide" co-operative Industrial and Provident Society) with the FSA.

The society then purchases property (usually freehold), and uses it to provide accommodation to its members, who become the tenants. In practice it will almost certainly raise finance from mortgaging the property with one or more "ethical lending" organisations[2], and have a need for some additional unsecured borrowing - which is usually done in the form of "loanstock" (fixed-term bonds). This often comes from the members themselves, their friends and family etc - but could also be raised from members of the public, and other co-operatives.

There are existing model rules such as RRFM96[3] which create this type of co-operative. These rules are clear that the objects of the society are to provide housing to the membership on a rental basis, and that members must not withdraw profits from the society. But they are less clear on the role of surpluses; and on the issue of members *indirectly* taking co-operative equity for themselves (for example, by failing to increase rents in line with inflation over several years, thus depriving the co-op of some of the income it would otherwise be entitled to receive), they are silent.

Advantages of current model

- **Simplicity** - the single entity, one member one vote model is easily comprehensible by members, lenders, and investors (though the landlord/tenant and co-op/member duality is nevertheless a challenge for some)
- **Maximum control by residents** - for a group of residents who do have the necessary financial and property related skills and expertise between them, this model gives them the greatest amount of control over selecting property to buy, raising finance and shaping the financial arrangements of the co-op, managing refurbishments and ongoing cyclical maintenance, etc
- **Well-understood** - co-ops operating according to this model have been doing so for 30+ years, there is fairly easy access to information and support through co-op support organisations, and lenders have developed mature lending decision processes for mortgage applications from this type of co-operative society

Problems with current model

Property purchasing is too difficult for new groups

The majority of would-be co-operative members don't have previous experience of property conveyancing and the many challenges this can throw up - for the inexperienced, this is often stressful and prone to error.

In addition, properties which are suitable for co-operative living are usually also attractive propositions for private sector landlords, which results in housing co-ops finding themselves in competitive situations - even in the present economic climate. Estate agents don't understand what a

2 Currently lending to new housing co-ops are: Triodos Bank, Ecology Building Society, Radical Routes, Co-op and Community Finance, and the Co-operative Loan Fund. Unity Trust Bank and Co-operative Bank are also candidates

3 RRFM96 is a set of model rules developed by Radical Routes for fully mutual housing co-ops in 1996, and which has been used since then for the registration of Radical Routes member co-ops, and many other co-ops too

housing co-op is and, as a newly incorporated entity with no track record, they are often not perceived as credible buyers.

Locked out of auction purchase

Furthermore, these types of properties are regularly sold at auction, and new housing co-ops are presently unable to access funding that meets auction criteria. Auction sales are often at a discount from the open market so, by being excluded from this option, housing co-ops are at a disadvantage compared to private landlords and developers.

Unsuitability of capital repayment mortgages

Mortgage lenders require repayment of capital and interest on their loans, but only the interest is a revenue expense for the co-op; the capital repaid will remain on the co-op's balance sheet. This is inherently unsuited to a body that is supposed to operate on a not-for-profit basis, as it necessitates building up substantial surpluses just to make the cash flow work. The result is that the rent levels the co-op needs to charge members in the early years are dictated by the co-op's cash flow requirement, not by its expense account.

In the past, there was enough “slack” in the finances such that this was not too problematic (and in fact was actually desirable if the rent was being paid by Housing Benefit). But with the current challenges of the property market, for both purchase and rental, many co-operative living projects that would otherwise be viable never go ahead simply because of this mismatch of the financing available with their needs.

Loanstock too piecemeal and complicated

Loanstock was originally intended to raise relatively modest sums of money, by getting a large number of people to invest a small amount each. However, housing co-ops starting up today often face substantial additional costs beyond the funding available from mortgage loans (for example, in some parts of the country it is no longer possible to find suitable property without incurring a substantial Stamp Duty fee). Many new co-op groups don't have the resources to do extensive marketing of a loanstock scheme beyond friends, family, and local contacts. This often results in these individuals contributing significant sums themselves.

In my view, a housing co-op providing housing on a rental basis should be able to function without requiring any capital from its members - not even on a loan basis.

Co-ops have to apply for mortgage without any track record

Of course, housing co-ops sometimes remortgage existing properties, or expand by buying additional ones - in which case they can present a good financial history. But because in the current model every new group starts by registering a new, legally stand-alone entity, it means they will be needing to apply for a mortgage to purchase their first (and often only) property at the stage when this legal entity has no track record. This presents a heightened credit risk to lenders.

Whilst a handful of “ethical lenders” do nevertheless lend to new housing co-ops at present, they do so at an increased rate of interest compared to normal owner-occupier mortgages - and of course the amount of capital available from them is finite.

New co-ops can't access capital for renovation/improvement works

Ecology Building Society do offer a refurbishment mortgage, but this only provides part of the necessary capital to carry out any significant programme of works. The reason development finance is unavailable to new co-op groups is that building projects, and especially refurbishments, are very difficult to keep on-time and on-budget; quite sensibly, the lenders / investors need confidence that the project is going to be completed according to plan. Again this comes down to the issue of the newly-formed co-op having no financial track record, and thus presenting high risk.

Poor standard of accommodation

The issue of renovation/improvement is all the more significant because of the generally poor state of the UK housing stock and therefore the type and condition of property that new housing co-ops typically have access to.

Housing co-ops that start up today (The Drive being a good example) typically find themselves with an undermaintained Victorian property, insufficient funds to do justice to the ongoing maintenance needs, and have to do a certain amount of "DIY" (they may fortuitously have members or friends with building skills, but this is hardly a satisfactory solution!). Many more people would consider co-operative living if they had the opportunity to live in a new-build property or one refurbished to a high standard, than those who opt for it today with the standard of accommodation on offer currently.

However, aside from aesthetic considerations and weekend DIY commitments, with energy costs set to increase year-on-year (the recent announcements of above-inflation rises being an example of this), the ability of the housing co-operative movement to offer low-energy housing will become increasingly important. Across the UK housing sector as a whole, there is increasing recognition that eco-refurbishment of existing housing stock will be needed. There is also a consensus that the best (and often, the only viable) way to achieve this is with a "whole-house" approach - in other words, doing all major building works at once, not in a piecemeal fashion - which of course does not lend itself to relying on weekend DIY!

Vulnerable to "carpetbagging" - insufficient governance

It is in the nature of housing co-op finance (due to the need to build up surpluses and make capital repayments on mortgage loans), that over time the co-op's balance sheet will develop a considerable net worth, which occasionally, despite the clear intent in the rules, members try to take for themselves (a process known as "carpetbagging").

When the RRFM96 rules were developed, it was envisaged that the Registrar of Friendly Societies would take a more active role in ensuring that housing co-ops were run according to the rules than actually occurred. However it is the registrar's prerogative to adopt a more laissez-faire approach, and when it chooses to do so there is, ultimately, nothing any third parties can do. This is the case because, in order to take civil action against a party, you need to have a legal interest, and in the current model each co-operative is a legally self-contained and independent entity.

A mortgage on a property is an interest, but even in these circumstances, the carpetbaggers can arrange for the mortgage loan to be paid off (carpetbagging usually occurs later on in the life of a co-op where the amount outstanding would be small, if any - and under the terms of the mortgage, the lender must then release the charge on the property). And currently, there is no statutory entrenchment or asset-locking available to co-operative societies[4].

It can thus be concluded that, without closer monitoring and intervention by a body with statutory powers, the governance structure in the present model is too weak to protect against activities such as carpetbagging.

4 Though asset-locking is available to Community Benefit societies, as a result of the Co-operatives and Community Benefit Societies Act 2003 and CBS (Restrictions on use of assets) Regulations 2006

"Passive carpetbagging"

Nobody would dispute that actually taking money out of a registered not-for-profit body (whether by going through the technical mechanism of demutualisation, or some other more surreptitious means) would be unethical. But what about depriving that organisation of money that it ought to have received, by not paying it over in the first place? This question does not seem to have been addressed.

Because co-ops have to generate surpluses for cashflow reasons (as explained above), and because the members decide, collectively, on their own rents[5], there is a strong temptation to not increase rents in line with inflation (be that wage inflation or price inflation). And because inflation is fundamentally built in to our economic system, it occurs in most years - albeit just a few percentage points usually - so the cumulative effect over time becomes significant.

This behaviour creates a somewhat perverse effect: often, the rent levels in a housing co-op are not a function of the local housing market, or related to the members' *genuine* circumstances, but in fact are a function of how old the housing co-op is - ie how many years have passed since the rents were last set in accordance with the rest of the housing market! Accordingly, I've seen circumstances such as members of a long-established co-op who are in well-paid professional jobs and paying only 50% of market rent (presumably able to increase their personal savings and wealth by several hundred pounds a month as a result, instead of the co-op getting that money); and housing co-op members on benefits struggling to pay their rent which is now above the new (reduced) LHA levels (set there out of necessity because the co-op is in its early years and needs the cashflow).

Looking at the housing co-op movement as a whole, this does not seem to be a fair way to treat its membership.

Deliberate underoccupancy

This is another form of passive carpetbagging. Here, the members don't necessarily pay less rent than they would be paying elsewhere, but instead they deliberately allow the co-operative's property to become underoccupied, and thus give themselves more space for the same money. I've come across cases of a single parent with two kids living in a 4/5 bedroom house (with two friends as "shadow" members so that the co-op notionally meets the legal minimum of 3); and a co-op that originally provided housing for 12 people in shared accommodation now only housing 6 people - by conversion to self-contained units.

When most of the established co-ops were set up 20 or more years ago, it wasn't envisaged that membership of a housing co-op would become such a scarce opportunity. Setting up a housing co-op today is not easy, and this is not likely to change soon, so it seems appropriate to ensure that the maximum number of people benefit from this opportunity over time. As a founder member of a housing co-op, I'd be disappointed were I to find in the future that the building was occupied (allowing for voids and reasonable changes in use of the space) by significantly fewer people than originally.

With the existing model, the objects of the society could include a clause along the lines of "provide housing for X many people" - but again, without some adequate external governance, there is no guarantee that this would be obeyed.

5 I am, of course, talking here only about non-RP/RSL housing co-ops, whose members are not entitled to social housing

No requirement on established co-ops to release their surpluses back into the network to help new co-ops start up

The sixth co-operative principle is “Co-operation among Co-operatives ” [6]. Whilst the explanatory text for the 6th principle does not explicitly mention financial co-operation, it is clear that the reason for this principle being included is that the co-operative movement as a whole would be strengthened - thus benefiting its members - as a result.

The biggest single expense for housing co-ops is interest on loans. Currently only a small percentage of the total interest paid by co-ops in their early years stays within the co-operative movement - the rest goes to the banks and building societies, exacerbated by them charging higher rates of interest to reflect the credit risk they are taking on (usually, borrowing a lower percentage of the value of the asset gives you a lower interest rate).

As an example, I know of two co-ops less than a mile from one another, where one is over 20 years old and has a house which is now mortgage-free; the other was set up recently and borrowed 90-95% of the purchase cost of their property from the ethical lenders mentioned previously, and is paying in the region of 5-6% interest on that loan. If instead, both properties were offered as security, a loan of 50% of the total asset value could be obtained at say 4% interest. This would reduce the finance costs of the new co-operative by a third! Both housing associations and private sector landlords have been using techniques such as this for many years.

6 The International Co-operative Alliance Statement on the Co-operative Identity is reproduced at the beginning of the RRFM96 rules and therefore, by implication, housing co-ops registered with those rules should be conducting their affairs in accordance with the co-operative principles

Suggestions for new financial and legal models

Stamp Duty fund

In London it is not possible to purchase any property suitable for co-operative living without paying Stamp Duty at at least the 3% rate, possibly 4% or 5%[7]. In the case of The Drive, our Stamp Duty bill was £24,800. Increasingly it is becoming difficult for co-ops outside of London to avoid 3% Stamp Duty too.

Stamp Duty Land Tax is a one-time payment that does not increase the value of the property in any way and thus cannot be borrowed from mortgage lenders. Raising these amounts represents a significant difficulty for new co-op groups.

In a housing co-op operating on a rental basis, it seems to me that the fair approach is for rents to be consistent over time (subject to inflation); members who join at the beginning or in the early days of the co-op should not have to pay extra just because of the stage in the co-op's life that their membership falls. To achieve this, startup costs (of which Stamp Duty is usually by far the largest) would need to be paid for from a source other than rental income. This is an area where the wider housing co-op movement could provide some valuable help.

A fund from which Stamp Duty would be paid for new co-ops (along with, possibly, the usual other startup costs such as FSA registration, solicitor's and surveyor's fees, etc) could facilitate the equalisation of rents mentioned. To be effective, the funds would have to be provided either on a gift basis or a zero interest over long term (eg 30 years).

This could be done on the basis that the property purchased will be staying in co-operative ownership for ever, and possibly in exchange for some manner of asset locking (see below).

Alternatively - and perhaps an even better solution - is that a community benefit society with charitable status can claim exemption from paying Stamp Duty (see below).

Innovative buying and refurbishing

Traditionally, independent housing co-ops have acquired property through the normal means of finding the property for sale on the open market via an estate agent, putting in an offer subject to contract, carrying out a survey etc whilst the estate agent has marked the property “under offer”, then getting a formal offer of loan from the building society (and secondary lender eg Radical Routes or CCF), then proceeding to exchange of contracts and completion. The normal mortgage loan funding used is contingent upon the co-op members being able to move in and start paying rent immediately upon completion - and the choice of property would need to accommodate this (ie no whole-house refurbishment!). It has always been the case that this has represented something of a learning curve for most co-op members; Radical Routes provides support in terms of both written and verbal advice through this process, but the emphasis has been on the new co-ops actually going through this themselves.

Problems with traditional approach

However, in recent years, this process has become increasingly difficult, for various reasons: the number of suitable available properties has gone down, the competitive situation in acquiring them has in the main not reduced, and the legal complexities surrounding them have increased (HMO

7 The rate of stamp duty is based on the purchase price (1% up to £250k; 3% from £250k to £500k; 4% from £500k to £1m; 5% over 1m) but the *whole* purchase price is then subject to this rate.

status, planning permission, Building Regulations); estate agents almost always do not understand housing co-ops, and purchase offers - quite incorrectly - appear to be weak, unless carefully presented (in the case of The Drive, some considerable persuasion was required to convince the estate agent and vendor that our offer to buy was genuine and substantial, despite our inability to provide evidence of us having 10% of the purchase price, as any other purchaser would normally have, because we were using a second-charge loan to provide the money that wasn't coming from the building society).

Furthermore, much of the specialist knowledge required during the property acquisition process is not required by co-op members once the housing co-op is up and running - the dealing with estate agents and solicitors, knowing about legislation, etc. At a few points during the setting up of The Drive Housing Co-op, several members were exasperated by the difficult and tenuous nature of the property-buying process, and it was only due to great persistence and determination that the purchase eventually went ahead. There have been other cases of co-op groups getting as far as putting an offer in on a house, then dropping out for one reason or another during the process. Even when the house purchase is successful, the strain on the group can take its toll: we had at least one member drop out during the purchase process because of the sheer amount of time and effort in everyone having to get their heads around the legal and financial issues. This stuff is not what most people sign up to co-operative living projects for!

From my own recent experience and those of others, I've come to the conclusion that the learning curve has now become too steep as a result of these recent trends to give new co-op groups a fair chance of success, unless there is more *proactive* support available. In any case, as well as providing one-time technical expertise, having someone to take some of this workload off the group would then allow them to focus more on the growing and strengthening of their group dynamics during this crucial setting up phase.

In the co-housing sector, it is recognised as essential that the co-housing group has access to paid-for expertise throughout the planning and design stage of a scheme.

Providing access to expertise

Expertise that could be provided to assist co-ops in house-buying:

- Identification of candidate properties and ability to quickly do a “back of envelope” feasibility analysis
- Placing offers with estate agents and knowing how to get past the challenges that they sometimes present
- Assisting in financial modelling and identifying and applying for suitable funding
- Dealing with any potential HMO planning permission issues
- Instructing and then liaising with solicitors throughout the conveyancing process

Having access to people with expertise moves from being beneficial to becoming essential, in my view, when looking at whole-house refurbishments. As mentioned, the number of properties coming on to the market that are suitable for co-operative living reduces every year (because the majority are bought by developers and split up into smaller units, and converting back seldom makes financial sense). To provide co-operative living opportunities for more people in the future - as well as to provide low energy in use accommodation (which will become an ever increasingly important factor), the housing co-operative movement is going to have to move towards doing substantial refurbishment works to make properties suitable for occupation. This is a huge challenge.

Expertise that could be provided to assist co-ops doing whole-house refurbishment:

- Identification of candidate properties and ability to quickly do a “back of envelope” feasibility analysis; note that two houses in similar cosmetic condition may have substantially different refurbishment costs, due to architectural factors that only someone with “eyes to see” would spot on a viewing appointment
- Producing specification for building works and budgetary costing; assisting in identifying and applying for appropriate development finance
- Liaising with local authority in obtaining applicable Building Regulations and Planning consents
- Running a tendering process and evaluating tenderers, to ensure that the co-op is using appropriate contractors for the work and getting good value for money (note that, as the end result is an asset that is held in co-operative ownership, this is of benefit not just to the co-op members but actually to the housing co-op movement)
- Project-managing the building works

The expertise listed in both sets of bullet points above is too much to be able to be provided on a volunteer basis (I myself have provided some such support *pro bono*, and am at the limit of my capacity to do so). To solve this problem, two things are required: a network of people with suitable expertise and experience; and suitable funding to pay such people for their work.

Proposals for funding

In some circumstances it will be possible to “roll up” any professional fees into the finished value of the refurbished property. The issue is then whether those individuals carry out their work “at risk”, until the project is complete (which may not be appropriate in many cases), or whether there is a fund from which they can be paid, and which then reclaims its money on completion of the building works.

In other cases, either because of valuation issues or for early-stage work that does not result in a completed project, independent funding will be required. This could be done along the lines of the existing Co-operative Enterprise Hub[8] scheme (in fact, that scheme could itself be used to fund the early-stage advice that is being proposed here).

In both cases, some manner of fund, contributed to by the housing co-op movement, would be required to which new co-ops could apply, specifically for payment for expertise and support work during their set-up phase - either on a loan or grant basis, as per their circumstances. The amount of money required would probably be quite small in absolute terms, with quite a lot of reach.

The Centre for Alternative Technology has for some years run an MSc course called Architecture Advanced Environment and Energy Systems (AEES), which is basically a degree in eco-building. Graduates from this course are in many respects good candidates for providing the building works expertise mentioned here, and some would be willing to do so for reduced fees in exchange for having the opportunity to put their AEES learning into practice.

Development Funding, and buying at auction

Funding for building works (known as development finance) has been mentioned previously. Development finance is inherently more risky, especially on refurbishment projects. This is

8 http://www.co-operative.coop/enterprisehub/About-the-hub/

reflected in higher interest rates and other more restrictive terms from commercial lenders, compared to standard mortgages.

In commercial terms, the risk is heightened when lending to a newly-incorporated entity, with no track record. Below, I've proposed a model which means that the freehold to a new co-operative living project could be placed in an existing entity (and then leased to the new co-operative) which could well have a reduced commercial credit risk, but in any case, even a newly-incorporated entity could be assessed on the basis that it has been set up within a known-to-work model, with input from known and trusted expertise from the housing co-operative sector.

A fund of money that could be put in to individual co-op refurbishment projects as and when required, and paid back upon completion, ready to "recycle" for the next project, could be built up on a loanstock basis or similar, and used to deliver much value to housing co-ops during the duration of the money being on loan - though the idea would be that investors were sought on a rotating basis, so that the fund never ran out.

Note that this funding suggestion is different from the second-charge loans made by Radical Routes at present, as these are required to be covered by the existing property valuation upon purchase; indeed, a Radical Routes loan may also be used in conjunction with the development fund suggested.

Alternatively, funds could be provided directly from other organisations' reserves, again borrowed just for the development phase and paid back by drawing down long-term mortgage funds from elsewhere on completion.

Buying at auction

In being able to acquire property for refurbishment, buying at auction is a very valuable tool - because the type of properties suitable for such projects are commonly sold at auction. But auction conditions essentially require access to the capital up-front; there is not time to go through the usual surveying and approval processes for regular mortgage loans. Buying at auction commonly yields a discount of 10-20% compared to buying from an estate agent, and this is often key to making the finances of a refurbishment project stack up.

But co-ops currently do not have access to dedicated finance for auction purchase. Again, a source of funding from which a significant amount of capital could be provided for a short space of time is required to facilitate this route to setting up new co-ops. This would be repaid once the building is completed and ready for occupation, by drawing down a regular mortgage loan at that point.

Professional expertise - danger of pre-committed capacity

There is a danger when setting up any structure that involves paying people for their time, that the vested interests of those people (to be regularly employed and thus have stability of their income stream) are put ahead of the purpose of the organisation.

A "top down" approach was used in setting up housing co-operatives in the 1980s, when plentiful funding was available. At worst, a housing co-op was incorporated with nominee members (who never had any intention of living at the co-op), the whole scheme was carried out by a co-op development body, on a "build it and they will come" approach (and certainly the members did come - but this was grant-funded social housing, with subsidised rents).

Sufficient governance measures would need to be put in place to ensure that funding and professional expertise structures are only responding to *genuine* requests from new co-op groups for support - a "bottom up" approach.

Such measures could include:

- Those who have a decision-making role in the spending of funds are not in paid positions, and have significant experience in the housing co-op movement
- Those who provide expertise on a paid-for basis are either employed by third party organisations (with whom the contract for service is made), or are *bona fide* self-employed, with multiple other clients, thus they do not become entirely dependent on the paid work from the co-operative living projects
- A “Chinese wall” between those who have decision-making role and those who provide paid-for service, for obvious conflict of interest reasons

There is also a difficult issue in terms of not setting up a “closed shop” where a limited number of people get all the contracts for paid-for support on the one hand, and having complete freedom for individual co-ops to contract with whomever they like, with no consistency or guarantee of quality of service[9] on the other hand.

Stronger governance

The suggestions made so far relate to the issues faced in setting up new co-ops; the following section relates to ongoing governance. To summarise, the key issues faced by the housing co-op movement with the current model are:

1. Insufficient protection against carpetbaggers.
2. Disparity of rent and occupancy levels between co-ops; conflict of interest with members making decisions about these things for their own house, sometimes at the expense of the housing co-op movement
3. No structural mechanism for equity generated within the movement to be “recycled” to enable more co-ops to be started up and thus for the movement to grow and reach more people

Charging of Properties

One idea that has been suggested previously is for a co-operative support organisation (eg Radical Routes) to take a legal charge over the properties owned by individual housing co-ops. This has the advantage of not interfering with the day-to-day running of the co-op in any way, but would prevent active carpetbagging, because the property could not be sold or refinanced without the chargee's consent (charges are recorded at the Land Registry).

More research would be needed to establish if a charge could be legally set up in perpetuity (or to that effect) and not able to be settled in any way (usually, charges are taken in exchange for making of a loan, and the charge is released on repayment of the loan).

Unfortunately, this model only addresses the first of the three concerns listed above. But it would be fairly straightforward to implement, and could be implemented retrospectively by existing co-ops too (providing they agreed, of course!).

9 In other sectors, such as CLTs and co-housing, where involvement of professionals is the established norm, work is being done to come up with solutions to this issue - so we can learn from their experience here

Split freehold/leasehold model

In this model, the freeholds to all the properties are owned by the secondary organisation. Each housing co-op has a lease between it and the secondary organisation. The relationship between the housing co-op and its members is unchanged, and the terms of the lease would hand all day-to-day control of the building over to the housing co-op.

This would provide automatic carpetbagging protection because the lease (which the individual housing co-op is in control of) would not have any capital value, and the secondary organisation would have a much larger membership, and stronger governance (perhaps including statutory asset locking), and thus made extremely difficult to carpet-bag.

A number of freehold properties held by the same entity could then be used to raise finance much more effectively - as is common practice with both housing associations and commercial property developers.

Roger Hallam, one of the founders of Radical Routes, now thinks that a leasehold/freehold relationship between the individual co-ops and the network would be more appropriate. Writing in *The Poverty of Post-scarcity Anarchism* (May 2012), he neatly sums up both the financial and governance benefits of this approach:

> "However if I had my way – none of the co-ops in RR would have been independent – their properties would be leased or something equivalent from RR. They would be autonomous except in the circumstances of power abuses such as getting rid of members and running off with the money. [...] And as co-ops paid off their mortgages then the properties could be remortgaged (to the extent of requiring tenants to still pay say a reasonable low market rent) and the money raised loaned back to RR to re-loan out to new co-ops – on the rule-based commitment that these new co-ops do the same."

Lease terms could also make regular reviews of rents, and specify required occupancy levels (short term voids aside, of course), thus ensuring that effective use is being made of the asset, for the benefit of as many co-operators as possible, and protecting against passive carpetbagging.

At the moment there are a number of possible different legal structures that could be use for the secondary organisation, that hold the freeholds, and further work will be needed to establish which is the most appropriate. The remainder of this section is an analysis of some of the possible options.

Difficulties with leasehold/freehold model

- **Danger of infinite growth** As a member of a housing co-op with, say, 10 members, your contribution to co-op decisions is 1/10th of the total; but if the co-operative had 100 members, your contribution would be reduced to 1/100th. There is a balance to strike between having a critical mass of people, to ensure good governance and access to expertise, whilst not having an infinite growth in membership which results in individual memberships becoming so diluted as a proportion of the total, that people do not feel involved.

  To provide enough people, enough inter-personal relationships, and enough different opinions for a group to provide a sufficiently strong set of checks-and-balances, and for there to be likelihood that all the necessary expertise and experience will be present amongst the membership, I would say an optimum size (based on experience, but not on any scientific analysis of any kind) is around 50-100 people.

- **Complying with tax exemption requirements** There are two relevant tax exemptions: a fully mutual housing co-operative is exempt from corporation tax providing that all (and in practice, most) of its income is rents from its members. This is the exemption traditionally relied upon for housing co-ops, and finances would simply not stack up without it (especially as only the interest component of loan repayments is allowable against tax). The other relevant tax exemption is a community benefit society with charitable status, which is exempt from various taxes (see below). It will be necessary to use one or the other of these in order to make a financially viable new model.

- **Leasehold law** The field of leasehold law is a complex one, and a significant amount of work would be required to create the lease agreement in such a way that it performs as expected, within the legal framework that exists. Additionally, the agreement of mortgage lenders will be required, to ensure that the lease meets their possession requirements.

- **Only suitable for new co-ops** This type of model has been proposed some time ago. A network of co-ops called Fairground was set up on this basis, but most existing co-ops were not prepared to join (which required transferring their freeholds). In any case, transfer of freehold would in some cases generate substantial Stamp Duty liabilities. Thus we can conclude this model would only really be applicable to new co-ops, which were being set up in conjunction with one or more of the funding mechanisms suggested above (and the leasehold/freehold structure being made a condition of funding).

Secondary housing co-op

A secondary co-op registered as a co-operative in the usual way, but has as its members the primary co-operatives (who in turn have their residents as members). The number of co-operatives and/or number of residents could be fixed in the secondary co-op's rules, to avoid the infinite growth problem. There would then be potentially several secondary co-ops each with up to this number of co-ops/residents. Could be run by general meeting or committee.

Advantages

- Familiarity (well understood within the co-operative movement)
- Co-operative structure
- Potentially able to use fully mutual tax exemption (providing all members are tenant/leaseholder co-ops)
- Deals with infinite growth issue

Disadvantages

- How to “bootstrap” - minimum three members required to register with FSA, would require nominee members (temporarily breaking the fully mutual rule!) unless there were three housing co-ops set up simultaneously somehow
- No statutory asset lock available, vulnerable until number of housing co-ops reaches a critical mass

Multi-stakeholder co-op

A co-operative society registered with rules that allow both individuals and co-ops as members. The individuals would be people selected for their expertise and/or experience of housing co-ops, and would be responsible for guiding the setup of the first few housing co-ops. Once these were set up (and had joined the secondary co-op), the membership would shift to represent the “steady state” of the secondary organisation supporting the housing co-ops. As an example, the membership could consist of a fixed number of three individuals, and up to 10 housing co-ops. There would then be potentially several such multi-stakeholder co-ops, each with up to this number of housing co-ops/residents.

Advantages

- Co-operative structure
- Decision-making matched to the changing purpose of the organisation over time
- Deals with infinite growth issue

Disadvantages

- Novel (multi-stakeholder co-ops are still a relatively new idea, at least in this sector). Bespoke rules probably required
- Does not fall in to either of the available tax exemptions
- No statutory asset lock available - but presence of experienced co-operators in the initial membership should limit vulnerability

Community benefit society

A community benefit society registered with rules that comply with the the co-operative principles as much as possible, and incorporate asset lock provisions.

Adantages

- Statutory asset-locking
- Decision-making matched to the changing purpose of the organisation over time
- Deals with infinite growth issue

Disadvantages

- Novel (multi-stakeholder co-ops are still a relatively new idea, at least in this sector). Bespoke rules probably required
- Does not fall in to either of the available tax exemptions

Community benefit society with charitable objects

A community benefit society registered with rules having charitable objects and complying with the definition of a charity in the Charities Act, whilst also incorporating the co-operative principles as much as possible. In order for the society's objects to be considered charitable, they should reflect one of the charitable purposes in the Act, for example “the advancement of environmental protection or improvement” (which, according to Charity Commission guidance, includes “the promotion of sustainable development”[10]). There would only be one or a small number (dependent upon charitable purposes) of these bodies set up with this model. This legal structure is the furthest from ideal from a co-operative respect, but it does have some quite significant advantages, which perhaps ought to warrant its consideration.

Adantages

- Tax exemption for Stamp Duty as well as Corporation Tax
- Statutory asset-locking
- Possibility to apply for funding from additional sources as a result of charitable status

Disadvantages

- Decision-making cannot be on a fully co-operative basis, in order to qualify as a charity (though the co-operative principles can be honoured as far as possible)
- Cannot be limited to a fixed number of co-ops or people, as needs to be for “public benefit”
- Custom rules required for registration, additional admin required as a result of charitable status

10 http://www.charity-commission.gov.uk/Charity_requirements_guidance/charity_essentials/public_benefit/Advancing_environmental_protection.aspx

Eco-house Refurb Model

Combining several of these suggestions together, I personally would like to see the following being turned into a viable model for new housing co-ops:

1. Purchasing undermaintained/unfit-for-habitation properties, perhaps with some financial assistance from within the co-operative movement (eg auction purchase fund, Stamp Duty payment scheme)
2. Carrying out an "eco-refurbishment" to upgrade the properties to a high standard of energy efficiency, as well as creating a higher standard of accommodation
3. Engaging professional-level support and assistance in the purchase and refurbishment process
4. Handing over the property on completion of the building works to a housing co-op, on a lease basis, whilst the freehold will be held in one of the suggested legal structures above

The overall cost of accommodation to be cost-neutral to the residents, compared with the alternatives available to them locally in the housing market - yet they get the opportunity of living co-operatively and in a newly-refurbished eco-house

Case Study: Withington Co-operative Eco-house

This project is intended to be a proof of concept for the Co-operative Eco-house model. A summary of where things are up to at the time of writing (Dec 2012):

- A house has already been purchased in Withington, south Manchester. It is a Victorian mid-terraced property in semi-derelict condition, located in an area of high demand, and suitable for a co-operative living group of six.
- A design specification for a whole-house eco-refurbishment has been produced, by a graduate from the CAT AEES course.
- A request for Building Regulations approval for the refurbishment scheme has been submitted to the council. We have had discussions with the building inspector and are awaiting formal confirmation of approval - all building works being carried out will meet or exceed current Building Regulations, and will be inspected and certified as such on completion.
- A number of contractors have been identified and invited to tender informally at this stage (formal tenders to follow upon receiving Building Regulations approval), and budgetary costings have been calculated on this basis.
- Ecology Building Society have indicated that they support this project in principle, and have instructed a surveyor to produce a valuation report; this has come back showing that the current and post-works valuations are consistent with the planned costs of works, and that the rent level post-works is in line with the local market.
- The housing co-op group has been meeting regularly and are in the process of agreeing their rules for living in the house; it is expected that they will register with the FSA early in the New Year, once they have agreed upon a name.

The next steps for this project are:

- Decide upon the legal structure to use and register the freeholding organisation (including the necessary primary rules). Transfer the ownership of the house to this new entity
- Source additional funding for the refurbishment (initial approach has been made to Co-op and Community Finance)
- Formally tender for the works and appoint contractors
- Draw up lease agreement between freeholding organisation and housing co-op
- Carry out building works, and hand over to housing co-op on completion

As there is a housing co-op group eager to move in to this house as soon as the refurbishment is complete, I am hopeful that project will be progressed as quickly as possible in the new year.

Next Steps

More generally, it would be good for more work to be done on developing the ideas mentioned: researching legal structures, deciding which one to use, and agreeing on the wording of the relevant documentation; developing the various funding suggestions; and creating more awareness with existing housing co-ops that they are part of a movement, and of the 6th principle. There are some difficult issues and inherent contradictions with some of my suggestions which need to be worked out, and it would be good to have the input of a group of people into this.