# Co-op Clusters

## Round table report

**By Radical Routes**

Supported by Friends Provident Foundation

# Introduction

## Purpose of the report

To present findings from research conducted into the problems restricting the growth of co-operative housing and to review a range of possible solutions to those problems, including - but not limited to - Radical Routes' proposed 'co-op cluster' model.

In December 2014, a briefing report was presented to a round table meeting of specialists in housing, co-operatives, finance and the law to critically examine the emerging findings and to help draw together conclusions and recommendations on the best way forward. This report takes account of suggestions and discussion at the round table.

Radical Routes is disseminating this final report to help find funding to pilot and/or roll out their solution to the issues highlighted.

## Key points

- Housing in the UK is in crisis. Social housing is in decline, private ownership is rising and capital is accumulating unequally.
- Fully mutual housing co-ops provide a sustainable middle ground. They are a model for renting housing in which tenants have control and security. This security is accessible without capital investment from the individual and at rent levels affordable for people on housing benefit and/or on very low incomes.
- Housing co-operatives are not always making full use of their assets. Properties are sometimes demutualised for private gain, or rent is lowered so individual members can profit disproportionately. These assets and incomes could be directed to growing the co-operative movement.
- Models used in the past to start up new housing co-ops are no longer working in today's housing market.
- Radical Routes has identified a possible legal structure to solve these issues. The Co-op Cluster model encourages co-ops to band together, sharing assets and income to buy new properties and found new co-ops. This could eventually start growing incredibly efficiently.
- We have looked at a range of similar models and projects, and are hoping to work with them to create a system that will work for the broadest range of projects and communities.

## About this report

The report will start with a discussion of our proposed model, the Co-op Cluster. Unfamiliar terms and ideas will be explained in the background information and context that follows.

## Radical Routes background

Radical Routes is a secondary co-op founded in 1992. Radical Routes aspires to see a world based on equality and co-operation, where people give according to their ability and receive according to their needs, where work is fulfilling and useful and creativity is encouraged, where decision making is open to everyone with no hierarchies and where the environment is valued and respected in its own right rather than exploited.

Radical Routes members in 2013 consisted of:

- 27 housing co-ops with 186 individual members
- 5 worker co-ops with 24 individual members
- 2 social centres with 49 core members active in running the social centres
- Rootstock investment co-op.

Radical Routes has helped many new co-ops start and develop through various methods, including creating its own investment co-op and loan system, loaning just over £1 million since 1992, and providing free training, support and advice to non-members and prospective members. All our full member housing co-ops have rent levels within the Local Housing Allowance (LHA) – the rate set on a location basis by the government, which dictates the amount allowable for housing benefit.

We are self-funding for our ongoing activities (our members pay service payments), but often seek grant funding to work on broadening the scope of our work, and influencing the wider co-op sector.

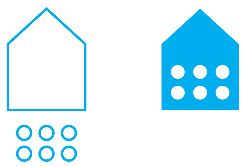
The main mechanism for mutual aid in the Radical Routes network is through work commitment, currently set at 4 hours/week for housing co-ops with over 5 members and 2 hours/week for those with 5 members or less.

Radical Routes is formed as a co-operative because it is a model of increasing resilience through self help and mutual aid. It provides a support network for its member co-ops, in the same way that a housing co-op supports its members. A co-op helping its members is its members helping themselves. This increases personal resilience, while providing a structure for people to fall back on in difficult times. Co-ops are almost by nature self sustaining local projects. Radical Routes works by taking that local model and applying it at a larger level.

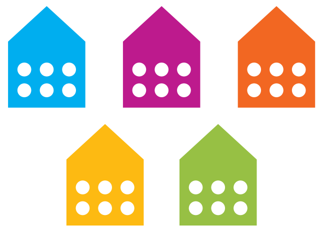
More information about Radical Routes can be found in the Social Audit overview in the appendix.

radicalroutes.org.uk/publications-and-resources

# The co-op cluster model

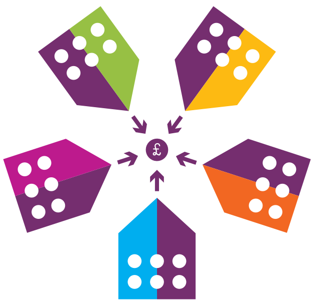


A group of people get together, form a housing co-operative, and buy a house.



They find a few other housing co-ops that want to work together.

The co-ops transfer ownership of part of their property to the cluster.

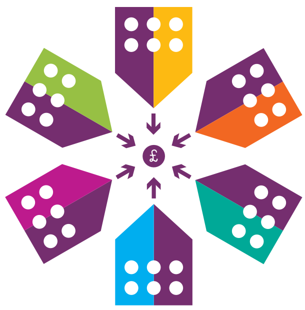


The co-ops pay rent to the cluster

This pot of money builds up over time

After a while, the pot of money is big enough to buy a new house

The cluster finds a group of people, and a house, and buys it for them, bringing them into the cluster.



The process repeats, with the cluster able to buy its next property quicker.

Radical Routes proposes a new system for supporting and expanding housing co-ops: a secondary housing co-op which would own a proportion of the freehold of housing co-op properties, and lease that portion long-term to the primary co-op in exchange for rent. The cluster of primary housing co-ops would all be members of the secondary co-op, so individual tenants would retain ultimate control over their housing.

Co-ops in the cluster would have some oversight of one another, specifically over issues relating to the sale of property. This is the primary defence against carpet bagging or demutualisation. We plan to build a legal structure in which this is the primary power that is held by the secondary co-op, unless the primary co-ops all decide to give it more. Individual clusters could decide how much interaction they want, but we see them primarily as mutual aid networks, like Radical Routes, but smaller.

The cluster would grow by buying out the debts of more co-ops. Once enough co-ops within the cluster have paid off all their debts, the shared pot of income would be used to buy new properties for more housing co-ops joining the same cluster. The individual co-ops would be obliged to continue paying into the larger structure, and use the funds generated to further the goals of the whole cluster. There would be a default expectation to use this to fund more housing co-ops and set up new clusters, but as long as the individual co-ops were in agreement, other common ownership projects could be developed and financed.

The co-op cluster could set rent levels in the leases to its members. This would allow it to set a minimum rent level expected for the primary co-ops, and dictate how quickly it would save up enough money to grow further. This would prevent 'passive' carpet-bagging, where rent levels are set artificially low to allow members to accrue private assets personally. Clusters would be able to set these levels appropriately for their community, but there would be a built in assumption of rent increasing in line with inflation, Local Housing Allowance or other relevant metric.

A major advantage of clusters is that they would accrue large amounts of capital, which would make it easier for new co-ops to form and buy more varied properties, without having to meet banks' business model requirements. From self build projects to large renovations, from sheltered housing to land projects, the type of purchases available would no longer be restricted by the need to get risk averse lenders on board with taking property into common ownership.

Once a co-op cluster became too large, it would split into separate clusters or provide seed money to a new cluster. Over-large structures can create a lack of member participation and a reduced feeling of ownership as well as leading to increasing use of a staff-based system, which increases costs and reduces participation.

Our research into Fair Ground has shown us a few interesting ways of ensuring this splitting can happen, including requiring regular discussions about size and manageability at AGMs, and a splitting clause to allow groups of co-ops within the cluster to request asset transfers into new clusters. This also provides individual co-ops with greater levels of autonomy.

We believe our new structure would create the stability of a single large organisation, while maintaining the member participation of small co-ops. Our financial projections suggest that this could lead to a significant increase of co-operative housing year-on-year after an initial start up phase, while improving the retention of co-operatively owned, fully mutual, self managed housing stock.

A co-op cluster would have control over how it spent the money it raised, but it would be harder for an individual or small group to dominate the decisions for personal gain. It therefore provides a positive way for mature co-ops to stay in the movement and be encouraged to grow the movement, increasing the amount of property in co-op ownership.

A key element being designed into this structure is that it will be hard for co-ops to leave (and therefore hard to demutualise) without the approval of the secondary co-op. At the end of every lease period they would have the option to buy back the leased portion of the property, but will have had to save up enough money to do so. If they wanted to leave before then, the contract could require penalty fees equal to more than the value of the portion. It would always be possible for co-ops to leave, but it wouldn't always be financially sound, making it much harder to carpet bag. Coupled with the mutual aid and clear benefits to new co-ops we think this will motivate people to stay engaged. Creating a suitable financial structure to maintain this is the main part of this project. We believe we have a technical model that could work, but need legal advice and expertise to make this robust enough to support a new organisation.

Radical Routes already operates on a similar model: using a combination of financial interest and mutual aid support to keep functioning. We have seen how it is able to build a strong network of co-operatives, working together, and keen on expanding the co-op network. The key difference here would be that the financial interest would be much longer term, which should lead to a stronger network, without the risk of co-ops drifting away once loans are paid off.

We are seeking funding to create a set of FCA approved model rules for co-op clusters, along with the relevant model tenancy and lease agreements, and guidance on how to create these co-op clusters. Once these are in place, we will promote the final model, using our existing structures of support for new housing co-ops. We have already identified several potential groups of existing co-ops who are interested in forming these clusters. We are hoping to support some of these groups in piloting this project.

The honey-comb structure of independent co-ops, partially owned by relatively small self sustaining clusters, means that a failure of a single project will not affect other clusters, while the cluster itself can act to support an individual co-op experiencing difficulties. This builds local resilience directly into the model. Radical Routes is based on a system of mutual aid, and this will be built into the model, along with the seven co-operative principles.

For different groups it may be necessary to design different variations of the cluster, particularly with regard to ownership of the freehold of the properties. We favour a model with a split freehold, owned half by the cluster, and half by the co-op itself. This gives each body a concrete interest in the property, allowing for a combination of security and autonomy. The ability to maintain ownership would be particularly important to established co-ops starting the cluster. The legal implications of this model needs to be looked into. There is definitely scope for some clusters to be based on full cluster ownership of the freehold.

It is very hard to project the impact that this could have on co-operative assets or the wider housing market. Some early projections based on buying out the mortgages of current nearly mature Radical Routes housing co-ops, had an initial cluster having accrued over £400,000 surplus ready to buy property outright in its first fifteen years, while growing from two co-op members to seven, without any outside investment. With less established co-ops, this would take a longer time, but with a large amount of take up, very large impacts could be made.
The model is based on taking a while to start up, but eventually earning money at a much faster rate, and theoretically doing so in perpetuity. If uptake was broad enough, co-op housing could potentially become a viable enough option to start driving rent levels down. None of this is likely to happen soon. We would instead prefer to focus on the smaller gains of allowing more people to control their housing, in a way that sustainably grows into the future, while maintaining the autonomous governance the co-operatives provide.

# Co-operatives and the housing crisis

## What is a housing co-op?

At its simplest, a housing co-op is a group of individuals forming a corporate body to act as their own landlord. A co-operative is an organisation run according to the seven co-op principles[1]. Co-operatives are run for the benefit of their members, but membership is free and open (although different co-ops will have different membership procedures). They are also committed to working together to improve the lot of co-ops worldwide. In fully mutual housing co-ops individuals are not allowed to profit from co-op assets, and when co-ops are sold, the profits should be pushed back into the wider co-op movement.

Co-ops are a form of common ownership, and assets taken on by co-ops are in principle permanently dedicated to the aims and objectives of that co-op. A housing co-op that buys a property now can improve it knowing that there should always be new people becoming members and benefiting from the work done.

Co-ops can be run a number of different ways, most often through direct control by members, or leadership by elected committee. The latter is used more often in larger co-ops, and there have been historical problems with these becoming undemocratic. Radical Routes works with and supports smaller consensus-based[2] housing co-ops (along with social centres and workers' co-ops). We will be focussing on these smaller co-ops, but they are all based on the same legal structure (the Industrial and Provident Society, recently replaced in law by the co-operative society).

More specifically, we are looking at fully mutual housing co-ops. Fully mutual housing co-ops are those where all members are tenants, and vice versa, where all investments made by members are non-transferable and non-withdrawable, meaning that all assets are in common ownership and individuals are not simply using the co-op as a form of personal investment. Traditionally, members buy into a co-op with a nominal share of £1, although this can be a larger amount. Fully mutual co-ops differ from 'buy in' co-ops, where members invest a withdrawable share, and can take it with them if they leave. We believe that while suitable for some, the buy in model is too similar to the traditional 'save up a deposit for a mortgage' model to be useful to the people worst affected by the present state of UK housing.

We believe that fully mutual co-operative-owned housing is a vital tool for creating a fairer society, where housing is a social good rather than a profit-making venture. We have seen in the UK how co-operative housing reduces environmental impacts, reduces social isolation, makes more efficient use of inner city spaces, and acts as hubs for community-based grass-roots organising[3].

Housing co-operatives are able to provide much more affordable housing than the market generally manages. They also foster a sense of community and co-operation that supports personal autonomy while saving money through communal living. Housing co-ops often base some or all of their rent levels on the Local Housing Allowance (LHA)[4], making them accessible to those on housing benefits or low incomes.

The current model for housing co-operatives is for a group of individuals to band together and form a co-op which then purchases property. The co-op then uses this property to provide accommodation to its members, who become the tenants. Generally speaking, the finance for this comes from traditional banks providing mortgages for the majority of the value - although ethical banks such as Ecology Building Society (EBS) and Triodos tend to be favoured - with the remaining portion (usually twenty percent) provided through unsecured loanstock, and/or mortgage type loans from organisations formed specifically to support co-operatives, eg Radical Routes or Co-operative and Community Finance (CCF).

There are existing model rules such as RRFM96 (a set of model rules developed by Radical Routes) 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 make a personal profit from the society's assets. They are less clear on the role of surpluses[5]; and on the issue of members indirectly taking co-operative equity for themselves. Radical Routes has since updated these rules to the new RRFM14 rules, which take account of, and attempt to fix some of these problems.

Radical Routes has been helping co-ops to form, and providing support through the form of loans, since its inception. Our model business plan spreadsheet is recognised by EBS and other lenders as a very useful indicator of the likely success of a co-op. All the individuals working on this project have direct experience living in, setting up or otherwise working closely with housing co-ops and other types of co-op.

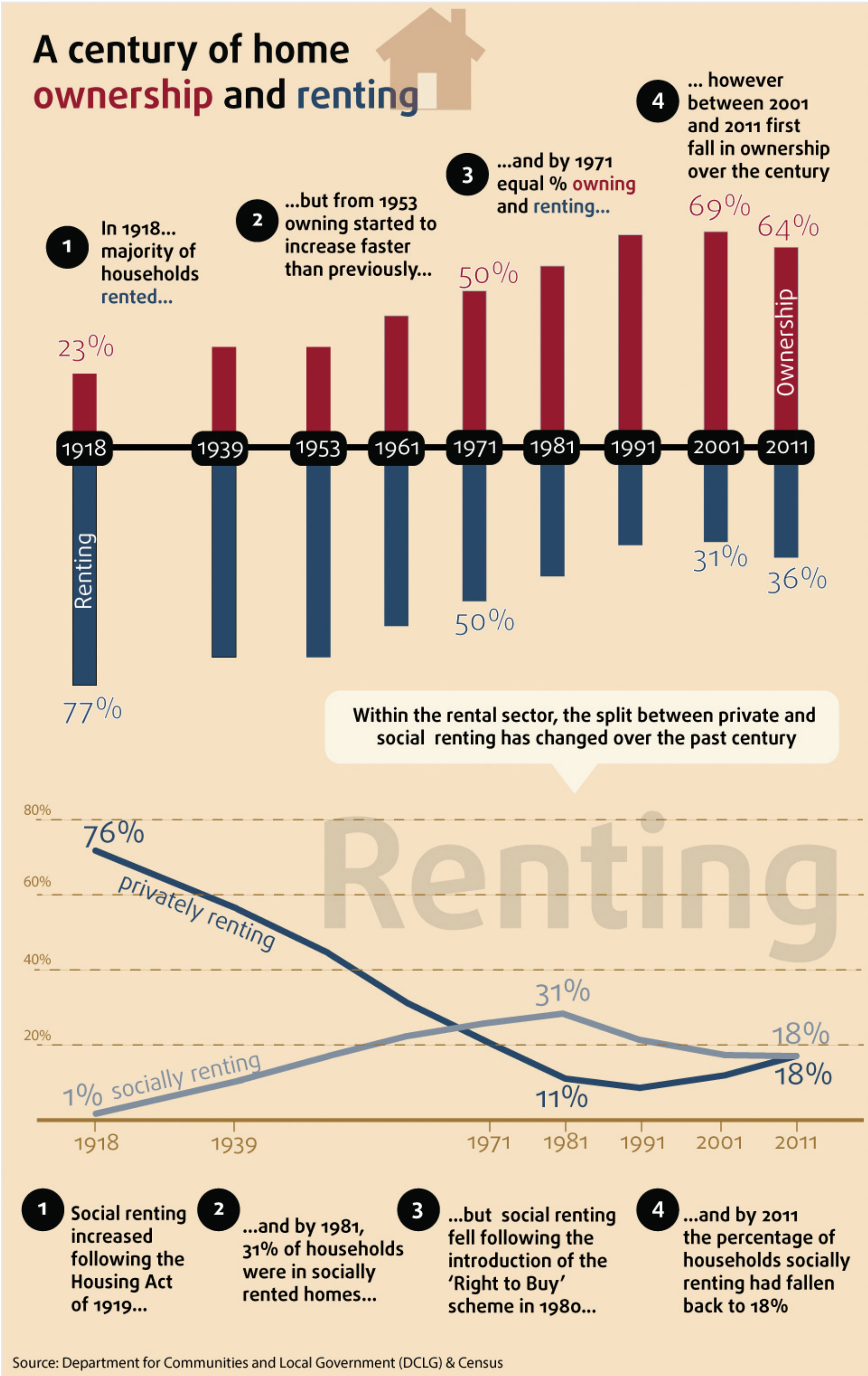
1. The Seven Co-operative Principles are outlined in the appendix radicalroutes.org.uk/publications-and-resources

2. Consensus based decision making seeks agreement among the entire membership, instead of making decisions by majority vote.

3. 'More than Markets report' published Sept 2013 http://bit.ly/1vU0v0x

4. The LHA is the locally defined upper threshold for housing benefit payments, based on the cheapest 30 per cent of properties in an area. Many co-ops base their rent levels on this to ensure that they can be accessed by those receiving benefits.

5. The terms surplus and profits are in many ways synonymous, the only difference being the implication that a surplus is retained within an organisation to further its aims, whereas profit is withdrawn by investors. A co-op may only use its income and surpluses in line with its stated objects (in every co-ops primary rules).



A century of home ownership and renting
1 In 1918... majority of households rented...
2 ...but from 1953 owning started to increase faster than previously...
3 ...and by 1971 equal % owning and renting...
4 ... however between 2001 and 2011 first fall in ownership over the century
23%
50%
69%
64%
Ownership
1918
1939
1953
1961
1971
1981
1991
2001
2011
Renting
77%
50%
31%
36%
Within the rental sector, the split between private and social renting has changed over the past century
80%
60%
40%
20%
Renting
76%
privately renting
31%
18%
1% socially renting
11%
18%
1918
1939
1971
1981
1991
2001
2011
1 Social renting increased following the Housing Act of 1919...
2 ...and by 1981, 31% of households were in socially rented homes...
3 ...but social renting fell following the introduction of the 'Right to Buy' scheme in 1980...
4 ...and by 2011 the percentage of households socially renting had fallen back to 18%
Source: Department for Communities and Local Government (DCLG) & Census

## How do co-ops fit into the current housing crisis?

Co-operative housing accounts for a relatively low percentage of the housing stock in the UK, compared to other European countries[1]. This may be due to the historically large amount of social housing stock. Since the 'right to buy' drive to reduce social housing stock in the 1980s, the proportion of households in social housing has dropped from a high point of 31% to 18%. Private renting has increased from a low of 10% to 18%. Individual home ownership is now a remote prospect for many people starting out today: the so-called 'generation rent'[2].

The private rented sector is currently very much associated with instability and insecurity. Tenants' rights are often secondary to landlords' and there is currently little political will to change this situation. Private renting accumulates capital towards those who already possess it (in the form of a house to rent out), which increases inequality. The increasing profitability of buy-to-let properties also increases house prices across the board. The private rented sector is notoriously bad at providing good quality homes[3].

Co-operative housing isn't always considered social housing, but it is a way of giving people control over their own home without having to take it into private ownership. This can be accessible to a much broader range of people than can afford to get on the property ladder, and co-ops can be set up to actively support and house particular groups. As well as housing co-ops that act as housing associations, and take tenants from local authority housing registers, there are co-ops dedicated to housing marginalised groups, for example Lesbian, Gay, Bisexual and Transgender (LGBT) people, who often face discrimination when looking for housing, or refugees and asylum seekers.

The co-operative model contrasts with the charity model in that it is essentially a form of self help. The co-op structure allows people to learn and take on responsibility for dealing with their own problems. The charitable model can create dependency, whereas co-operatives directly encourage personal participation and resilience. By using charitable funds to build a model for people to adapt and use themselves, it is possible to empower communities and individuals to take control of their own lives and housing.

Housing co-operatives can make renting resilient and sustainable. They give the co-op security of ownership and allow people to improve their homes safe in the knowledge that they and the co-op will benefit, not a landlord who can kick them out on short notice. The landlord role is taken by the co-op, and therefore within control of the tenant members, providing greater security and confidence than most private rented housing.

Once a co-operative has paid off its original financing (usually a mortgage) it is in a position to support new co-ops and enable more people to get to the same secure stage. While this doesn't always happen, a growing co-op network could ensure more and more people are actually paying their rent back into the local co-op economy, using the capital of their home to help other people be housed in the same self-sustaining way.

Co-ops are also well positioned and motivated to charge affordable rent levels. If co-ops became more dominant in the housing market, this could have knock on effects for the market rent levels.

## Advantages of the housing co-operative 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 skills and expertise between them, this model gives them the greatest amount of control over selecting a property to buy, raising finance, 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.

1. "85% of the 35,000 member organisations of the international federations that make up CECODHAS, the European liaison committee for social housing, are housing co-operatives. Most are very small, although some are very large, but housing co-ops own 18% of Sweden's total housing stock, 15% in Norway, 8% in Austria, 6% in Germany and about 4% in Ireland. This compares to 0.6% of housing in the UK." Bringing Democracy Home – Commission on Co-operative and Mutual Housing – edited by Nic Bliss p55

2. "Over a third of 20-45 year olds could be defined as 'Generation Rent' – a group with no realistic prospect of owning their own home in the next five years." - Halifax Generation Rent report 2014 The same report places the average first-time buyer deposit in 2013 at £30,943

3 "All types of damp problems were more prevalent in private rented dwellings than in any other tenure. Some 9% of private rented dwellings had some type of damp problem." & "The private rented sector had the highest proportion of non-decent homes (33%)" - DCLG English Housing Survey Headline Report 2012-13

# Issues in co-operative housing

## Current issues in housing co-ops

Radical Routes, through its experience supporting housing co-ops within and outside its network has identified various issues with co-operative legal and financial models for providing fully mutual housing co-ops.

1) Mature co-ops often sit on large amounts of capital assets, rather than using these to increase co-operative housing stock. This is an inefficient use of resources.

2) Increases in property prices make it more difficult for new housing co-ops to form. Co-ops are usually unable to take advantage of property auctions or self build projects, and are limited to buying properties that fit in a limited model of commercial viability, while competing with private landlords.

3) Carpet bagging - both 'active' carpet bagging, whereby individuals privatise co-operatively owned assets, and 'passive' carpet bagging where a co-op pays off the mortgage, reduces rents and allows under-occupancy of the co-op - can happen with relative ease, and means that the hard-work put into creating co-operative assets is lost.

4) New co-ops are reliant on loans from banks, meaning that often much of their rental income is spent servicing debt. It also means all co-ops have to fit into business plan models that are recognised by banks.

There is a clear need for a mechanism to allow and encourage co-ops dedicated to co-operative principles of common ownership to use their common assets not for personal benefit, but for expanding the amount of property in common ownership. This could drive the whole movement into a more resilient model of expansion. The instability of the housing market is a real threat to current methods of expanding assets in common ownership.

## Mature co-ops and unused equity

Once a housing co-operative has paid off its mortgage it generally finds itself with a significant drop in costs, and an ability to continue generating income at the same level. Maintenance and management costs must still be covered, but the bulk of a young co-op's costs are keeping up with mortgage payments. The successes of the co-op movement in the 1970s and 1980s left an array of large projects with paid off mortgages, capable of generating large surpluses. While some of these projects are using their surpluses to support new co-ops with grants, loanstock and loan guarantees, Radical Routes has observed that this is not always the case, and it is certainly not built in systemically to most business plans or rule structures, despite being a theoretical requirement of the co-operative principle: co-operation amongst co-operatives. We believe there is scope to create positive structures can allow co-ops to commit to investing in other common ownership projects in the knowledge that their investment will be bound by the co-operative principles.

## Changing property market

Traditional small scale co-op business plans are effectively based on the 'buy-to-let mortgage' model. As the rental market is increasingly popular amongst investors, lettable properties rise in price. The increased competition makes it very hard for co-ops to get their foot in the door, and as increasing offered prices is often not an option, they can be outbid even when not at auction. Self build and renovation projects also require major outlay, which can make business models tricky to structure. Add to this the pressures of wider increases in property prices, and housing co-ops are increasingly limited to only the least fit accommodation available. This problem is magnified by regional inequalities in the housing market, particularly in London and the South East.

## Carpet bagging

Explained further below, 'carpet bagging' is the process through which individuals take profits from common assets. This is relatively rare in its more direct form, where assets are sold off and the profits pocketed, but more common in its passive form, where rents are artificially lowered to far beyond sensible levels, to allow current residents to profit indirectly. It is perhaps worth noting that this is not necessarily coming from selfish intent, but often just because the governance systems encourage a maintenance of status quo over pushing outwards. We hope that models and rules can be changed to make co-ops default to supporting growing the wider movement, rather than simply waiting for inflation to push them into de facto carpet bagging. RRFM14 is a first step down this road.

## Limited to specific business models

On a fully mutual basis, it is challenging to create a buy-to-let business plan for a co-op that works with anything other than large, run down Victorian properties. There is a real drive within the fully mutual housing co-op movement to enable the purchase of more family homes, adapted accessible flats, sheltered housing, retirement properties or other properties that might be able to help a much broader range of people than those used to living in shared houses. Because these are likely to be less profitable, or based on properties with higher prices, they are not normally available for our current models of financing. Most mortgage lenders are incredibly risk averse when it comes to co-operatives, and it is only the robustness and track record of already tested business plans that allows them to be trusted. Widening the range of properties available will require increasing the amounts of initial capital available to new co-op projects. Particularly, if buying a property outright, the range of properties that could be made financially viable becomes huge.

# Further issues in co-operative housing

(adapted from 'Rebooting the co-operative movement'[1])

## Property purchasing is difficult for new groups

The majority of would-be co-operative members don't have previous experience of buying property and the many challenges this can throw up - for the inexperienced, this is often stressful and prone to error. Groups like Radical Routes aim to alleviate this problem, but can only offer so much support, and by their nature are required to focus on those in their network, or intending to join.

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.

Most estate agents don't understand what a housing co-op is and, as a newly incorporated entity with no track record, co-ops are often not perceived as credible buyers.

## Locked out of auction purchase

Suitable properties are often sold at auction, and new housing co-ops are normally 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.

## Issues with capital repayment mortgages

Mortgage repayments cover the interest on the loan, plus an amount to reduce the balance of the loan. This is unsuited to a co-op that is supposed to operate on a not-for-profit basis, as paying off the capital portion of the mortgage increases the worth of the co-op, by increasing the amount of money needed each month to make the payments. The result is that the rent levels the co-op needs to charge members in the early years are higher than needed to cover the costs of borrowing (as inflation occurs, mortgage payments remain static, so although this is still the case later on during the life of the mortgage, it is less problematic)

In the past, there was enough 'slack' in the finances that this was not too problematic. Current challenges of the property market, for both purchase and rental, mean that 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 order to help with those most affected by the current housing crisis, a housing co-op providing housing on a rental basis should be able to function without requiring any capital from its members, even on a loan basis. The easiest way to make sure co-operative housing is accessible to those in the greatest housing need is to not require initial capital investment.

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

Housing co-ops sometimes remortgage existing properties, or expand by buying additional ones - in which case they can present a good financial history. Normally though, 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 lend to new housing co-ops at present, they do so at an increased rate of interest compared to normal owner-occupier mortgages - and the amount of capital available from them is finite

1. Robert Morris, 2012 – see appendix for full document: radicalroutes.org.uk/publications-and-resources

## 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 the type and condition of property that new housing co-ops typically have access to.

Housing co-ops that start up today typically find themselves with an undermaintained Victorian property. Without the funds to do justice to the ongoing maintenance needs, a large amount of DIY is often required. 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.

With energy costs set to increase over time, 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 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. This 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[1].

When the RRFM96 rules were developed, it was envisaged that the Registrar of Friendly Societies[2] 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 co-op, you need to have a legal interest, and in the current model each co-operative is a legally self-contained and independent entity. A member of the co-op can bring this legal action against the co-op itself, but outside interests (such as those looking to protect co-operative assets) are unable to do so. Radical Routes has been approached by former co-op residents who are unhappy that current members are winding down the co-op with an aim to keep the assets for themselves. Currently, both we and the former members are unable to do anything to prevent this.

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 is small, if any - and under the terms of the mortgage, the lender must then release the charge on the property). Currently, there is no statutory entrenchment or asset-locking available to co-operative societies.

We conclude 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.

1. As no-one has a statutory obligation to deal with this, there are no statistics collated on the prevalence of this, however Radical Routes has dealt with several cases of this happening

2. The statutory role of the former Registrar of Friendly Societies is now undertaken by the Mutuals team at the Financial Conduct Authority

# Other solutions, examples and models

## The current mutual aid model - Radical Routes

Radical Routes already works to help new co-ops buy housing. We take investment from a member investment co-op (Rootstock) and use that money to loan to new housing co-ops, on the basis that they become, are accepted and remain as members of the network. We offer a mutual aid support network to our members and associates, finance properties beyond traditional banking's loan to value ratio and hold co-ops accountable to the wider network as long as they have a loan with us. Since we founded in 1992 we have lent over £1 million, mostly to housing co-ops. Co-ops can and sometimes do leave the network and unfortunately a few have gone on to passively carpet bag the assets acquired with Radical Routes support.

Radical Routes provides finance to support traditional housing co-op business models, but is increasingly hampered by the present financial climate and housing crisis. We are able to help new co-ops gain the trust of banks and other investors, but are still forced to focus on properties that function on a relatively straightforward buy to let model, and so are unable to currently support co-ops to deal with many of the issues raised above.

More information on Radical Routes can be found in the Social Audit overview in the appendix.

radicalroutes.org.uk/publications-and-resources

## Model Rule re-writing

Most of the fully mutual housing co-operatives registered in the last 20 years have used the model rules developed by Radical Routes. RR have recently finished writing a new set of model rules with more emphasis on stopping demutualisation and carpetbagging.

The new rules include a 'rule-lock' – so that key rules (e.g. asset lock, one member one vote, all tenants must be members and all members must be tenants or prospective tenants) can only be changed with the agreement of Radical Routes. The new rules also include attempts to tighten up the 'paper members' issue (where a co-op reduces to one or two bona fide members, but they get a friend to sign up as a member on paper, in order that the co-op can remain legally registered). Radical Routes is also named as the default receiver of dissolved co-operative assets, which would give us a legal interest in the assets, giving us a foothold to challenge any demutualisation. New co-ops and established co-ops with a commitment to common ownership models will hopefully be attracted to this as a method of ensuring that their housing will stay in the commons in the long term.

We hope this will reduce active carpet-bagging, but it doesn't encourage the use of capital assets or make it easier for new co-ops to access finance or buy a wider range of properties. During the model rule re-write project we concluded that it was not possible to address these issues merely by changing the rules alone.

One advantage of the model rules re-write is that it is relatively straightforward for existing co-ops to change over to the new rules - and indeed Radical Routes will be encouraging its existing member co-ops to do so.

## Co-operative Freehold Societies

In general terms, a co-operative freehold society is a legal entity which holds the freehold to multiple properties that are occupied by housing co-operatives. There will be a lease between the freehold society and the co-operative to effect this. The housing co-op then gets to operate on a day-to-day basis largely as if it owned the property directly.

However, for non-day to day activities, it is the freehold society that is in control. The governance of this organisation is therefore key. The existing co-operative freehold society models we know of (see below) as well as our own proposal are all based around the freehold society itself being a co-operative (with the housing co-ops each being corporate members); but it is also possible in theory for it to be a charitable organisation.

The advantages of this two-tier structure, in the context of growing the housing co-op movement and protecting existing assets, are:

- → When adding a new property to the freehold society, unused equity in existing properties can be easily leveraged - as is commonly done by both housing associations and 'buy-to-let' landlords
- → Over time the freehold society will develop a financial track record and improved credit risk, which should enable it to unlock further funding and/or lower its cost of borrowing. This in turn opens up possibilities for subsequent properties that remain out of reach with the current model.
- → Because several co-ops are joined together via the freehold society, in the event of one of them running into difficulty there will be ready access to a support network that has good motivation to provide support and assistance; these relationships will likely be closer and more accessible than with a national body like Radical Routes.
- → It isn't possible for the people living in one house to carpet-bag by selling the property, because they have to go to the freehold society's board meeting and convince all the others to agree to this (and there could be exceptional circumstances in which this makes sense, of course).

## The Co-operative Living Freehold Society

CLFS was set up by some Radical Routes people (plus one other) to implement some of the ideas in Rebooting the Housing Co-op Movement. In conjunction with being a co-operative freehold society, CLFS has focussed on developing the idea of a co-operative eco-house: in other words, of purchasing property in need of refurbishment and doing a comprehensive eco-refit before handing the building over (by way of a lease) to a housing co-op. Although these two concepts could operate separately, they work well together because of the additional funding challenges and complexity of doing eco-refits.

Registered in April 2013, CLFS has already completed the eco-refit of one property (located in Manchester), which is now fully occupied by a housing co-op under a multi-year lease.

The co-operative eco-house model works together with Ecology Building Society's C-Change Retrofit mortgage product, which provides interest rate reductions according to energy performance improvements undertaken.

CLFS is currently in the process of identifying a possible second property and talking to potential co-op groups. The launch of an 'ethical investment' scheme is planned for 2015, to compliment mortgage finance from EBS.

CLFS is a co-operative freehold society that has as its initial membership three housing co-ops. The first has now leased the property in Manchester mentioned above, and the second and third properties to be purchased and renovated will be leased to the other two initial member co-ops; thereafter the freehold society can grow by additional co-ops being admitted to its membership. The society is run by a management committee comprised of one representative from each housing co-op, plus secretary and treasurer (these positions are elected annually at the AGM, and in due course it is hoped will be filled by members of the housing co-ops).

### Students for Co-operation

Recent years have seen a huge rise of interest in housing co-operatives amongst students, with three new student housing co-ops obtaining property (in Sheffield, Birmingham and Edinburgh) in the last year. In addition, a number of new student co-ops across the country are in the process of setting up with the aim of running property by the 2016-17 academic year. These include groups in Bradford, Sussex, Aberdeen and London. However, groups working to set up student housing co-ops face a number of barriers to their success. These included difficulties accessing finance, lack of experience within the group, and time-lag, with the length of time taken to set up a co-op often longer than the length of a university course.

To overcome these problems Students for Co-operation (with the support of East of England Co-op) have funded a feasibility study into the creation of a National Body of Student Housing Co-ops (NBSHC) that will arrange finance and purchase new co-operative properties. It will then lease them to its member co-ops, the new student housing co-ops. It will also provide support in setting up the new co-ops as well as training in the required administrative skills or back office services for those co-ops that need it.

### Fair Ground 'Maxi Co-op'

Fair Ground was a historical attempt to create a model similar to the co-op clusters/co-operative freehold society structure. Set up in the late 1970s, a number of existing co-ops and communities aimed to pool their resources, giving ownership of their properties to the Fair Ground 'Maxi Co-op', which would collect rent from all of them to pay off their loans, and eventually build to function as an alternative building society. Despite several years work and a lot of good intention and ambition the co-op failed to get off the ground. It was a precursor to and clear inspiration to Radical Routes, but may have had ambitions that were 'too much, too soon'. We do not believe that the attempt failed because of the model itself, but issues surrounding the way it was attempting to form.

We have completed a case study into what happened with Fair Ground. In particular, we've looked at the problems it ran into and what can be learned from them. See appendix for more information.

radicalroutes.org.uk/publications-and-resources

## Past and foreign structures

### The Mietshäuser Syndikat (Germany)

A German organisation with much in common with the Cop-erative Freehold Society model is already thriving. 'Mietshäuser Syndikat' (apartment-house syndicate) brings together 88 housed projects and 27 new housing initiatives in a solid network.. Each of the projects is autonomous - a separate enterprise that owns its own property - and has the legal status of a limited liability company (LLC; German: GmbH). Mietshäuser Syndikat welcomes new, self-organized housing projects as well as those that are still to take on a property. As a result, the network is still expanding. It currently has 400,000 Euros in deposits from members.

The syndicate operates in a different way to our model, but mostly only in terms of legal structures. The local tax regime and laws have encouraged German projects to develop LLCs rather than co-operatives, leaving each member project with full ownership of their property and autonomy, while maintaining a legal interest for the syndicate to prevent assets from being removed from common ownership.

While based on a different legal system, we feel this model demonstrates that this sort of solution can work and thrive even on a very large scale. It is hard to translate specificsbut it is inspiring to see such a similar model already addressing the same problems

More information can be found on www.syndikat.org.

# Bringing the solutions together

| | Advantages | Disadvantages | Who is it for? | What does it fix? |
|---|---|---|---|---|
| **Co-op clusters** | → Creates oversight.<br>→ Tax efficient.<br>→ Built in splitting points.<br>→ Grows sustainably long term.<br>→ Full member control. | → Complicated structure.<br>→ No existing version in the UK.<br>→ Requires initial buy in from existing mature co-ops. | Existing co-ops, new co-ops. | → Ensures efficient use of equity.<br>→ Opens up a range of different housing options.<br>→ Acts as mutual aid network.<br>→ Prevents carpet-bagging. |
| **Co-operative Living Freehold Society** | → Creates oversight.<br>→ Relatively simple structure and relationships.<br>→ Grows sustainably long term.<br>→ Can build in splitting points.<br>→ Tax efficient | → Cannot access equity of pre-existing housing co-ops. | New co-ops only | → Opens up range of different housing options.<br>→ Prevents carpet-bagging.<br>→ Acts as mutual aid network. |
| **Student Co-ops** | → Creates oversight.<br>→ Well supported by co-op sector. Makes it easier to offer housing to a new generation of co-operators. | → Maintains some of traditional landlord model | Student co-ops | → Allows stability of management of co-operative student accommodation |
| **Radical Routes model rules changes** | → Creates oversight<br>→ Work completed.<br>→ Prevents carpet bagging. | → Co-ops must change rules. | New and existing co-ops | → Prevents carpet-bagging.<br>→ Gives legal interest in co-ops on dissolution. |
| **Radical Routes current model** | → Proven track record.<br>→ Creates oversight.<br>→ Full member control. | → Limited by business models.<br>→ Oversight only lasts as long as loan. | New and existing co-ops | → Supports new co-ops.<br>→ Acts as mutual aid network. |
| **Mietshäuser Syndikat** | → Proven model | → Based on German legal and tax positions | Existing co-ops and new co-ops (in Germany) | → Ensures efficient use of equity.<br>→ Prevents carpet-bagging. |

## Oversight and autonomy

One key difference between various different models is the way that power is shared between the different elements. There is a tension between the need to prevent co-op members profiting from common assets and wanting to ensure that co-ops have autonomy and their members are directly in control of their own housing.

Students for Co-operation actually need to favour external governance, as they face a challenge of high natural turnover. By targeting students, membership of individual co-ops is likely to change relatively rapidly (two-three years is likely to be the average tenure of each individual student member). In order to maintain consistency and growth, it will need to find ways for the co-op network to have more consistent leadership and governance.

The co-op cluster, on the other hand, is focussed on maintaining as much autonomy as possible. Each cluster is governed directly by its member co-ops, and so every individual still has a direct say in how their housing is operated. The oversight is provided through mutual aid and co-operation, rather than from an external body of any kind. We believe this is a more sustainable and fair model, and particularly, much more likely to be used by current mature co-ops, who could already be difficult to convince to give up assets for the sake of a 'nebulous' common good. Balancing individual autonomy at the co-op level, whilst providing oversight through collective ownership at the cluster level is the key to this model.

At its heart, the model is designed to ensure a cluster would be unable to evict member co-ops in a way that would leave them without assets to support themselves. This autonomy and ownership also means that if the cluster is at risk of collapse, the assets would be able to more easily return to the primary co-ops.

# Questions and Answers

This is a selection of key questions and answers that were raised during the round table event.

### Will co-op clusters increase housing supply, or just make more housing co-ops?

We believe different clusters will have different priorities, but that the model can  help achieve both goals. A lot of clusters will initially be focussed on bringing privately owned housing stock into common co-op ownership, but mature clusters will be able to support a much broader range of projects. A successful cluster could easily fund self build projects, eco-renovations, care homes and land projects. The flexibility of stability allows clusters to make a much bigger impact, not necessarily just for the co-op movement. The beauty of the model is it allows financial stability in the long term, so a cluster can do what it wants.

### Which index of inflation should rent levels be linked to?

In some ways this is irrelevant. The difference between the two main indicators is nominal at this level. In fact, it would be possible to link it to a range of indexes, LILAC links to wage levels, and Radical Routes have discussed linking to the local housing allowance (itself based on local market rents). The key element is that there should be an annual increase by default. This can be amended by consensus of the co-ops in the cluster, but the norm should be an increase. This ensures that co-ops don't accidentally slip into 'passive carpet bagging', ie paying significantly less rent than is appropriate, and thus profiting from the capital, instead of pushing the capital into furthering the aims of the co-op.

### What are some of the risks of living in a co-op?

Housing co-ops provide accomodation that is simultaneously more and less secure than other types of renting. Co-op tenancy agreements, by necessity, tend to have less rights than other sorts of tenancy (particularly those with registered social landlords), but this loss of security is balanced by member control. It is easier for your landlord to evict you, but you have direct democratic control of the landlord, your co-op. This allows members to manage their households, while giving everyone a say.

Most co-op business models account for a certain amount of empty rooms in a given period (voids). Disputes between members can end up leading to several members leaving, and this can exceed even planned for voids.

Radical Routes (and sometimes mortgage lenders) can often support a co-op in a difficult time by relieving some of their capital repayments. Clusters would be in an even better position to do this, having a great amount of flexibility to relieve rent pressure on co-ops in any sort of crisis. It's also noted that the presence of a support network makes a great difference to all sorts of issues that can come up. The co-ops (and individuals) that get into trouble with debt and finance, tend to be the ones who don't have people to talk to about it. Clusters provide that additional informal support network.

### Why split the freehold?

The model calls for houses that are owned partly by the primary co-op and partly by the secondary co-op. This is based on the assumption that current co-ops will be unlikely to want to give away their whole freehold, but that there is a need for equity between initial members and later members. This introduces a range of challenging legal issues that are a big part of the future of the project. This model may not be necessary in every situation, and we hope to build structures that will suit a range of different project types.

### Could the clusters idea be applied to other types of collective ownership?

At a basic level, co-op clusters is about profit sharing to grow the co-operative movement. This can  be applied to a range of different models, and we would welcome queries and questions about ways of doing this. The present project is focussed on housing specifically because of the dormant capital in the sector, and the problems we have seen and highlighted. The specific legal structure is very much based on the quirks of the housing sector, and so it is unlikely the documents could be directly applied to other types of cluster, but we expect elements to be useful and inspirational to a larger range of groups.

### Who will form clusters?

We have already seen a wide range of interest in the clusters project. We suspect most clusters will form over a pre-existing bond or affinity. The simplest and most obvious of these will be geographical. It would be very straightforward for a group of co-ops in a particular city or region to band together. We also believe it is likely that clusters based on political motivation or co-operative identity may also set up. We have already seen Students for Co-operation embark down this route. We can imagine an LGBT cluster, focussed on housing specific marginalised groups. Radical Routes is already linked by a collective political vision, and is likely to spawn a cluster based on those ideals. It is possible that interested funding bodies will fund clusters with a specific set of aims, housing the elderly, for example. We are hoping to model a whole range of different starting points for clusters, and create a structure that will work for a wide range of groups.

# Conclusion

We believe the co-op cluster model is a self sustaining method for increasing resilience in the rented housing sector. It is a complement to other models, and way of challenging the dominance of privately owned housing. By using present co-op assets to increase co-op assets, and bonding groups of co-ops together, we believe that in the long term, a large amount of properties could start coming into common ownership, and have significant impacts on the future of housing in the UK. Working with the other projects to build a variety of legal structures and possible co-op entitities to fit a range of different local and structural situations enables us to make this possible for a much wider range of people and communities.

Our next step is to work with the various projects identified, and hopefully partners like the Friends Provident Foundation, to develop robust legal documents and structures to make this a reality. Radical Routes will be able to directly support at least one pilot project, and demonstrate the viability, but we hope the work will be available to a much wider range of groups and communities. Established co-ops will be able to support local housing projects, finding a way to invest in new projects that they know will be sustainable and driven towards the same goals indefinitely. This builds a momentum of sharing and common ownership that we feel could be very powerful.