INTRODUCTION TO MUTUAL HOME OWNERSHIP SOCIETIES (MHOS)

community led housing.
london

JULY 2020

CONTENTS

GUIDE SUMMARY

This guide aims to provide a plain English introduction to Mutual Home Ownership Societies for interested groups and individuals. In this document you will find answers to the following questions: What is an MHOS (and what is it not); how have different aspects of the model been interpreted; what can existing case studies tell us; and what alternatives are out there?

HOW TO READ THIS GUIDE

Throughout the guide, there are links to useful documents and websites for further reading. These are highlighted in blue

If at any point you would like advice and guidance, you can contact us at info@communityledhousing.london

DISCLAIMER

Our team and associate Advisers encourage groups to think openly and clearly about their objectives and how to achieve them. The information in this guide is for general guidance and is not legal, financial, or professional advice.

Community Led Housing London assumes no responsibility for the contents of linked websites. The inclusion of any link should not be taken as endorsement of any kind or any association with its operators.

You can read our full disclaimer here

WHAT IS MUTUAL HOME OWNERSHIP?

Mutual Home Ownership is a form of collective ownership that allows individual members to accumulate equity shares in a Co-operative Society.

Like other co-operatives, such as fully-mutual housing cooperatives, a "Mutual Home Ownership Society" (MHOS) is a legally constituted democratic organisation regulated by the Financial Conduct Authority (FCA). Every resident is a member of the Society and has an equal say in how it is run. In a MHOS, members are also able to own and accumulate equity shares in the Society, with the possibility of taking this equity with them when they leave.

The model was originally conceived by David Rodgers from CDS Co-operatives working with the New Economics Foundation. Interest in the MHOS model has grown in recent years, due largely to the completion of the UKs first built example, LILAC in Leeds, which delivers permanently affordable housing linked to incomes.

Another attraction of MHOS is the promise of meeting the needs of those who cannot afford to buy a home on the open market, but perhaps do not qualify for social housing, those in so called "intermediate" housing need.

Recent Mutual Home Ownership Societies, such as Yorspace in York and Quaggy in London, have taken different approaches to things like affordability and equity repayment. Understanding the fundamentals of the model can be difficult.

In order to understand the opportunities that MHOS presents we first need to understand the fundamentals of what a MHOS is and, just as importantly, what it is not.


LILAC, Leeds


Yorspace, York


Quaggy MHOS, London

KEY FEATURES OF MHOS

Fully mutual

Every resident of a MHOS is a member of the society and every member is a resident. This means residents are in control of decisions over building management, 'rental' income and resident welfare. How you may go about making such decisions is discussed in our guide to 'Getting your group ready'.

One member one vote

As with all co-operatives, every member has one vote in decision making, irrespective of how much time or money they have put in. MHOS should follow the seven cooperative principles: voluntary and open membership; democratic member control; member economic participation; autonomy and independence; education, training, and information; cooperation among cooperatives; and concern for community.

Flexible apportioned costs and debt

In a MHOS it is the Society that collectively owns any assets (typically homes) and debts (say from building the homes) and has ultimate responsibility for repaying those debts and any other costs such as for building maintenance. How the cost of this responsibility is apportioned between members and the terms of how and when payments are made, is up to the members themselves to decide collectively. Yorspace apportions debts and costs relative to the size of the homes you want to live in, whereas at LILAC there is a further adjustment in relation to member incomes. This flexibility also allows a scheme to accommodate (and may depend upon) members with different income levels, and to adapt to changing household circumstances over time. However, the overall responsibility of the MHOS to repay its debts, does not change.

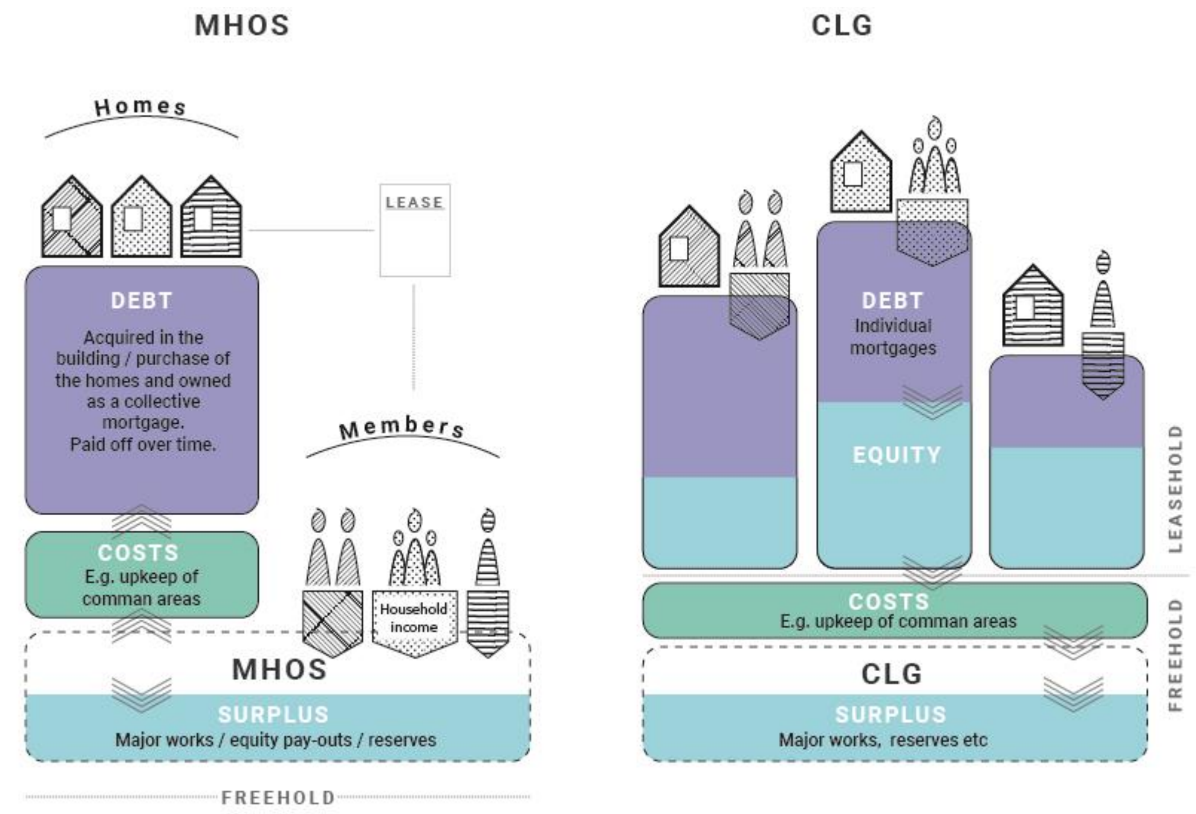


Fig 1. This diagram demonstrates the differences in ownership and collective/individual responsibility for debt between MHOS and a Company Ltd by guarantee.

Equity shares

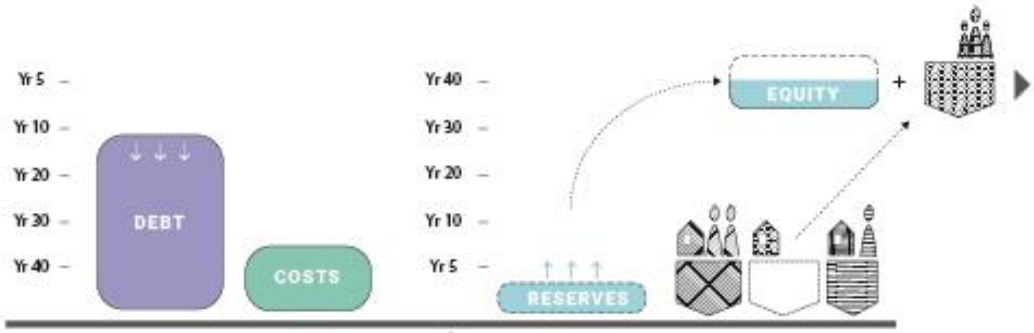
Unlike other co-operative housing societies, MHOS allow members to accumulate equity shares in the society. Shares can be bought up front (similar to a deposit when buying a home) and accumulated as part of monthly 'rental' payments (in a similar way to conventional shared ownership products). Different to conventional property ownership however, the equity owned by members of a MHOS are shares in the society and its assets as a whole, rather than the individual homes themselves. The value of members equity shares may increase or reduce over time, relative to how ever the society's assets are valued – for example linked to average incomes or as a proportion of market value.

One of the appeals of MHOS is the idea that when a member decides to leave, they can take the equity they have accumulated with them. In current property market conditions this can seem preferable to the conventional housing coop model, whereby founding members take on the lion's share of the coop's debt but have little financial security should they decide to leave. Upon leaving a MHOS, you may be entitled to receive your equity shares as a payment. However this is only if the co-op can fund the buy-back, or if other residents can take them on, or if you can find a replacement member who can buy you out (or some combination of these). *See Fig 2. bellow and more in the next section*

Affordability in perpetuity

The MHOS must set out how the equity shares with be valued when members leave. Leases typically include a formula linked to average incomes or possibly the consumer prices index. These are intended to ensure people moving in do not have to find large deposits and have access to housing that is affordable in perpetuity.

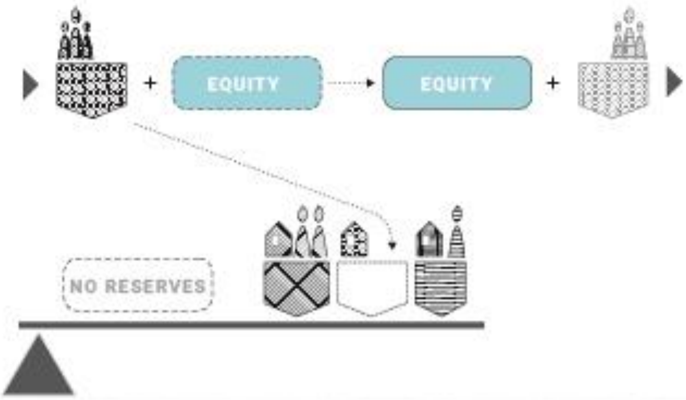
MANAGING EQUITY SHARE PAY-OUTS TO A DEPARTING MEMBER



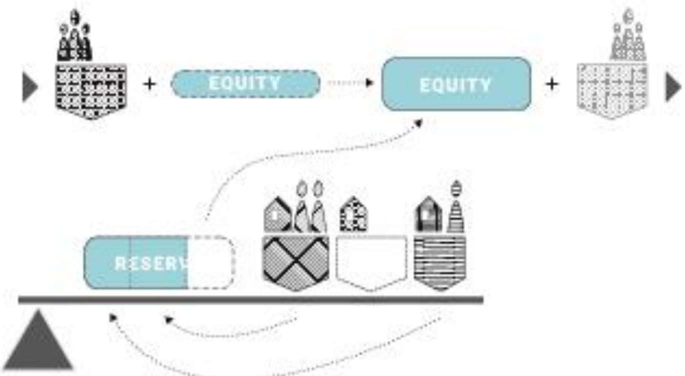
Covering equity payments for depart-ing members can be challenging

Particularly early on, when minimal surplus has buit up to cover the pay-out

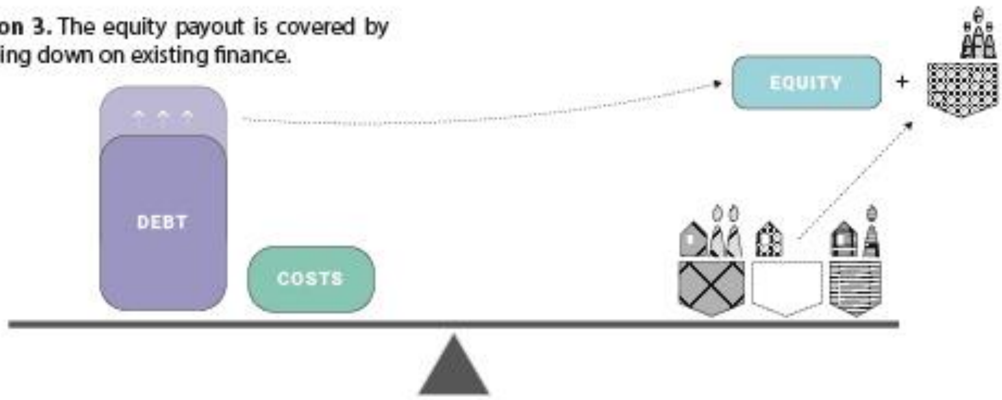
Option 1. If the MHOS can't afford to cover the pay out, an incoming member can contribute the same equity as is owed to the departing member. This can be a barrier to affordability in the long-term though.



Option 2. The incoing member contributes a standard amount of equity upon joining (e.g. 10%), with existing members buying more shares of their own to cover any adition required by the departing memberor retain healthy researves is covered by .



Option 3. The equity payout is covered by drawing down on existing finance.



WHAT MHOS IS NOT

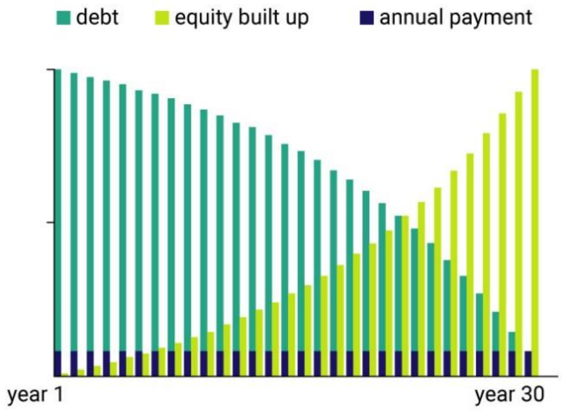
Affordability is not inherent to the model
A MHOS is a way for people to collectively own their homes. How they pay for those homes and make them affordable is a different question. Although members / residents are in control of setting monthly payments or 'rent', but this doesn't happen in a bubble. The big costs like purchasing land or buying/building homes are still subject to the same economic forces as if you were building conventional flats. There may be savings to be made, and if you already own the land, or can acquire it at a discount, this can help a lot. But even with the grant funding currently available, achieving a viable and affordable scheme can be a challenge.

Of the existing examples, affordability is achieved in different ways, each with their own trade-offs. Overall viability in LILAC is achieved by working backwards to ensure costs are covered by 35% of incomes. However there are a mix of higher income members and a requirement for a minimum of 10% deposit to make it work. Quaggy on the other hand doesn't require a deposit as it is more reliant on various loans but has fewer guarantees around how and when a member's equity shares can be paid back when they leave.

MHOS is not the best of both worlds
Where MHOS has the potential to work well is in schemes where members are bringing different amounts of equity and have different income levels. This is because the flexibility in how debt and costs are apportioned means higher earners can help cross-subsidise greater affordability for other members. However, for those bringing equity to a scheme (e.g. as a deposit or to help finance construction), shouldn't expect its value to rise at the same rate as it would if you were to invest in market property. One of the main aims of MHOS is to effectively protect housing from the speculative forces of the property market, meaning your equity could rise (or fall) in relation to an indexed formula set by the MHOS, for example in relation to local average incomes.

MHOS is not a ready pot of cash
The ability of a MHOS to move equity around and pay out a departing member or support a member on hard times, for example, depends largely on the scale of the society and the number of members/households making regular payments. The fewer members you have, the greater the risk of destablisation by the changes in circumstance of individual members/households, not being able to move equity around. Having more members spreads the impact of such risks to the Society, making it easier to build up reserves or secure ongoing finance agreements with lenders.

Making equity pay-outs to departing members can be difficult early on in the life of the Society. The graph shows the ratio of debt to equity over a 30-year period, demonstrating the slow buildup of equity due to the way that interest is compounded in the early years.



VARIATIONS AND INTERPRETATIONS OF MHOS

One of the defining features of MHOS compared to traditional fully mutual rental co-ops is the ability for members to accumulate equity shares and the flexible apportionment of debt and equity between members of the Society.

The way in which these and other aspects of MHOS have been interpreted by the three existing examples vary from case to case.

The following details the key differences in how the MHOS model has been interpreted in the LILAC, Quaggy and Yorspace.

New groups may choose other ways to set monthly payments and to value equity shares, and may even consider other ways of providing mutual intermediate housing.

INDEXED 'RENT' / INCOME

What is the value of a home? In the conventional housing market values are defined by an assessment of similar properties in the area, inflated or deflated according to demand. As an MHOS is intended to protect homes from the speculative forces of the property market, the 'value' of a home is typically what it cost to build or purchase, together with the land it sits on. As this is likely to be financed by the MHOS through debt, the question then becomes how to determine how much 'rent' payment members should contribute to repay this debt.

In the three existing examples of LILAC, Yorspace and Quaggy, the debt the MHOS holds is apportioned between households or members, relative to the size of the home or room they occupy. The amount each household or member pays per month is calculated differently in each example.

- At **LILAC**, payments are calculated as 35% of monthly household income. This creates some risk within the business model (should individual household income change over time, for example). However this risk is offset by the number of units within the scheme (22) reducing the overall impact of missed payments voids or other bad debts from individual units. If you have a bigger home with a lower income it takes you longer to accumulate shares – *see diagram in Appendix 1*
- At **Quaggy**, with only six tenancies across the scheme, the impact of someone leaving is much higher. Here monthly payments are indexed to 1/3 of average incomes in the borough (at the time of purchase), providing a more stable income to the MHOS to repay its debts.
- **Yorspace** on the other hand indexes its monthly payments to the Net Development Costs (ie costs after any grants, equivalent to the total scheme borrowing) of each property, effectively selling homes at cost + management and maintenance costs, spread over a fixed period, with no relation to household or local incomes.

REDEEMING EQUITY SHARES

The value at which any accumulated equity shares a departing member can be paid is based on a formula defined by the MHOS. Whether this is actually paid depends on the financial stability of the Society. The scale of a MHOS has a significant impact on its ability to move equity around easily. The examples of LILAC and Quaggy demonstrate the difference here.

- With six tenancies, the impact of a member leaving **Quaggy** and withdrawing the full value of their equity shares at once would be significant. The fact that members do not need to make a down payment or deposit when joining also means that the amount of equity the MHOS holds, particularly in the first 5-10 years, is likely to be limited. For this reason they can only offer a limited guarantee regarding pay-outs to departing members.
- Whereas the scale of **LILAC** and the fact they require a 10% deposit to join means they have more scope to adjust the long term loan from their lender, allowing them to borrow more or extend the repayment to respond to changing financial situations. However members still only get an increase in the value of equity shares if they leave after 3 years, and the increase is based on average local income growth, rather than the increase in house prices.

NESTING MHOS IN A CLT

In this variation, a Community Land Trust owns land across multiple sites. Different MHOS can lease homes on a site by site basis. This is the approach that **Yorspace** is taking and provides two key benefits,

- providing a way of raising finance from the wider community through community shares, (although the MHOS can itself raise loanstock) and
- the CLT can leverage finance for future development against the multiple sites owned by the trust without affecting the MHOS. (Although there may be greater stamp duty in taking on built homes).

SUMMARY OF CASE STUDIES AND RESOURCES

MHOS	Key features	Deposit?	'Rent' indexed to...	Equity shares indexed to...
LILAC, Leeds www.lilac.coop	20 units. Mix: 1,2,3 & 4 bed homes Eco new-build	Yes. 10%	Cost of building the homes and 35% of member's individual incomes	Average local incomes
Quaggy, London	6 bedroom shared house.	No.	1/3 average incomes in London	Average local incomes
Yorspace, York www.yorspace.org	19 homes (1-4 bed) and a common house. Development undertaken by CLT and leased to MHOS upon completion.	Yes	Net Development Costs (ie costs after any grants, equivalent to the total borrowing on the scheme)	

Wrigleys Solicitors have been involved in LILAC and Yorspace www.wrigleys.co.uk

Transition by Design offer training on MHOS and have gathered the following resources https://www.notion.so/Mutual-Home-Ownership-8680400d12054d92aab4205b0393f81d

LILAC can be contacted through lilac.learning@mail.com and have the following resources https://drive.google.com/drive/folders/0B9_dS0hF7G0KYUpxRHhHb1pqdzA

OTHER MUTUAL INTERMEDIATE HOUSING

While MHOS has some unique and defining features there are other ways of achieving mutual intermediate housing which groups might want to consider.

‘MUTUAL’ COMPANY WITH INTERMEDIATE LEASES

The freeholder or head-leaseholder of the scheme is a Company Limited by Guarantee, where all the individual flat leaseholders are directors of the company. The individual leaseholders have their own mortgages for their homes. They may also pay a service charge to the company if this provision is in their leases.

The lease from the company can include restrictions on the resale price, potentially linking it to a formula or percentage of market values, and some criteria around who is eligible to purchase this leasehold. This would allow the benefit of any original subsidy to be protected and passed onto others. It would need to be imposed externally, for example by the council/landowner through a section 106 agreement, to ensure the directors of the company do not decide to vary their own leases, and sell without such restrictions.

It is also possible for the company to let some units as they wish, or lease to a housing association to let.

LEASEHOLDER CO-OP

See Glenkerry Co-operative Housing Association glenkerry.org.uk
The freeholder or head-leaseholder of the scheme is a Co-operative Society, where all the leaseholders of flats are members. The leaseholders have their own mortgages for their flats, and they also pay a service charge set by the freeholder (ie the co-op of which they are members, and therefore responsible for setting the service charge and ensuring the maintenance in relation to that)

The residents own the leasehold fully. However they have restrictions on who they can “assign” or sell their lease on to. So that they are only sold to people within a certain income eligibility bracket. In theory leaseholders could ask the co-op to vary this restriction, so again this is probably a grant or sale condition, ie legal protection of benefits in perpetuity is imposed externally.

SHARED OWNERSHIP CO-OP

See Shearwood Housing Co-op, Crayford
cds.coop/for-co-ops/co-op/shearwood/
The freeholder of the scheme is a Co-operative Society, where all the shared-ownership owners are members. The shared-owners have their own mortgages for their share of ownership, and they also pay a rent to the co-op (of which they are members) for the share they do not own of their individual flats, and they also pay a service charge set by the freeholder (ie the co-op of which they are members, and therefore responsible for setting the service charge and ensuring the maintenance in relation to that).

The co-op also has its own long-term loan for the “unsold” share of ownership, which the rents help to pay down.

Again, the legal protection in perpetuity is probably imposed externally through a grant condition (although it may allow staircasing).

CO-OPERATIVE SOCIETY (WITH LOAN STOCK FROM MEMBERS)

The freeholder or head-leaseholder of the scheme is a Co-operative Society, where all the residents are members. Residents have tenancies from the co-op. They do not have their own individual mortgages. The payments they make under their tenancies are made to the Society and help to pay down a single long-term loan and any other loans held by the Society, as well as any maintenance costs etc.

The Co-operative Society can issue “loan stock” as a way to raise money from supporters. People can lend money for a set period defined by the Co-op typically 5, 10 or 15 years, and are paid interest at a chosen rate, typically 0% to 4% a year. At the end of the period lenders can have their original investment back. This is not the same as buying equity shares; as lenders don’t have a say in how the co-op conducts its business. Lenders are effectively providing an unsecured loan. However the Co-operative should set aside money from the rental income to cover the loan stock interest and repay the loan stock at the end of the term, as well as long-term bank borrowing etc.

If a resident-member provides loan stock to the co-op, this could function in a similar way to equity in a MHOS. Although they would only get their loan stock repaid at the fixed term, not necessarily when they leave. Although there would be no increase in the value of original loan repaid, they would have received interest payments over the course of the loan term, which is similar to linking equity share payments to an index, which is not the house price index.

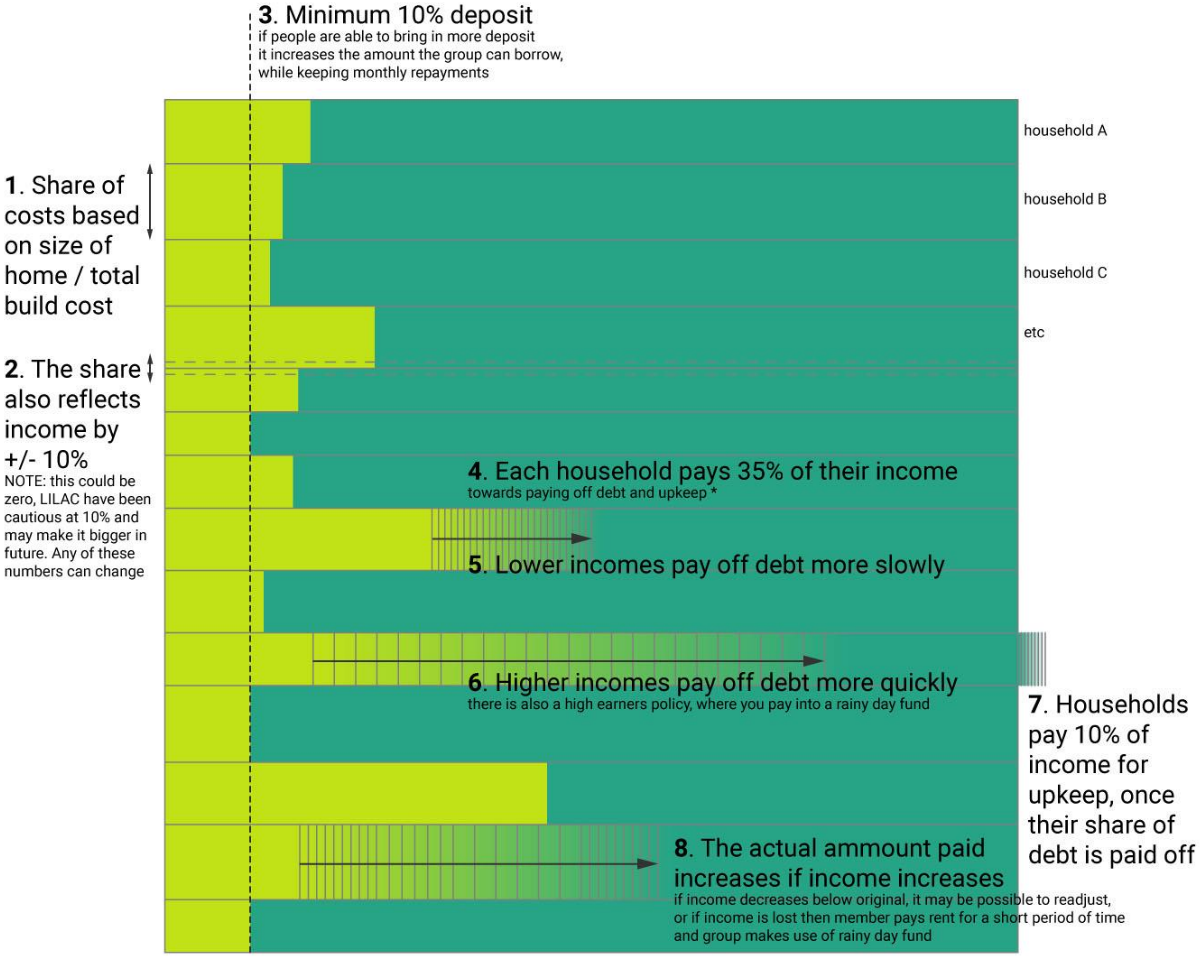
APPENDIX: LILAC RENT / EQUITY DIAGRAM

key

total square = total cost of scheme minus grant [this is still key for overall viability and affordability]

'equity' or 'deposit'

'debt' or 'loan' - LILAC have a 25 year loan from Triodos at 4.4%



9. If you leave within 3 years, someone replaces you, and you get back your original deposit + the equity shares you have accumulated (debt paid off).
If you leave after 3 years, you get deposit + equity shares accumulated + an increase on the value of equity based on average earnings, rather than the increase in house prices.
If the new household cannot replace the outgoing equity, bank borrowing can be increased *- this makes it affordable for others in the long term, but you miss out on capturing the full market value for yourself (even though you do get some increase in equity)*

*Total payments need to cover the costs of upkeep and paying off debt over the time period. So this is calculated backwards from income, ie asking "how much debt can 35% of incomes service?" That's how much you can afford to build/buy.

Contact us

7-14 Great Dover Street

London

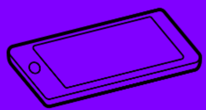
SE1 4YR

020 3096 7769

info@communityledhousing.london

Follow us on social media

@CLHLondon



community led housing.
london