Better to borrow?

How development trusts use loan finance to achieve community goals

DEVELOPMENT TRUSTS ASSOCIATION

the community-based regeneration network

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How development trusts use loan finance to achieve community goals

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Introduction

In 2004 we asked development trusts about their attitude towards loan finance.

We discovered that borrowing was at a relatively low level: 79% of development trusts had not used any form of loan finance in the previous year. However, in 2005 the figure was 73%, and in 2006 it was 71%. This suggests a gradual increase in the number of development trusts prepared to use loans.

Some borrowing takes the form of an overdraft facility. Sometimes a bridging loan will meet a short-term need. Most significantly we are seeing development trusts taking on mortgages for capital purchase or refurbishment – in other words to develop community owned assets which can deliver community benefits and at the same time provide the basis for independent income. Our members now have more than £340 million of assets in community ownership – financed by a potent mix of grants and loans.

In this booklet we have selected examples where finance has been provided by NatWest/RBS or Unity Trust Bank. This is because these banks have been pioneers of community enterprise investment – ever since the formation of the Development Trusts Association in 1992 they have supported our movement and built relationships with our members. They helped to grow a market, and so perhaps it is not surprising that they are now the market leaders.

In 2006 over a third of our members said they were 'comfortable' or 'very comfortable' about using loan finance. We hope this booklet will encourage more to consider this route. We believe that loan finance, when used correctly, is one way to help development trusts grow their business, and therefore increase their community impacts.

Steve Wyler
Director
Development Trusts Association

Case studies

Millfields Community Economic Development Trust
Homes for small businesses


The first day of building

As this publication goes to press (August 2006), the Millfields Community Economic Development Trust (MCEDT) is starting work on 14 new business units to house small enterprises and start-up companies in Plymouth. The project aims to contribute towards the regeneration of the inner city ward of St Peter, thereby strengthening the area's economy.

The estimated cost of the project is £1 million, including a £361,000 loan from NatWest. This was the Trust's first real opportunity to secure its own asset, and borrowing made perfect sense to the trustees. They knew that as long as they could retain the rents, repaying the loans would never become a problem. 'It was about time we grew as an organisation and broke our financial dependence on grants', says Roger Pipe, the Trust's Secretary. Although the project is partly grant-funded, the Trust has secured ownership of the freehold, and thanks to the loan it hopes to end up with some very valuable assets.

Work will be completed in January 2007, and rental income from the units will allow the Trust to repay its loan over 20 years, at the same time as generating a healthy surplus for its other charitable activities.

Security for the loan came from the freehold of the site and the projected rental income from the units. It took a while for the trustees to agree on the idea of borrowing such a large sum, but in the end they felt empowered by the success of the Trust's other enterprises, and decided to use an independent broker to look at available deals. The local contact for NatWest was particularly helpful, and this relationship helped to simplify the process.

Project:	Building 14 business units for local start-ups and small and medium-sized enterprises
Lender:	NatWest
Amount borrowed:	£361,000
Achievements:	Helped the Trust secure its first freehold asset
Lessons learned:	(work in progress)
Contact:	Roger Pipe (Company Secretary) rogerpipe@btconnect.com

The Environment Trust
Building affordable green homes for local people

Lambeth Green Homes at New Green Place

The Environment Trust had an overdraft facility to manage cash flows, but to finance its most ambitious projects it chose to borrow from commercial banks.

The Green Homes projects are energy saving and environment friendly apartments and houses built to a specification devised by the Trust. This has been one of its key activities over the years.

Loan finance is at the heart of each Green Homes project, which is repaid on completion of sales for low cost, shared ownership for individuals. This is because the Trust, like many community based regeneration organisations, does not have equity to invest in its projects.

For the Trust's scheme in Lambeth, Lambeth Council provided the land, which acted as security for a £2.5 million loan from Unity Trust Bank. The loan paid for the construction of the green homes, which the Trust then sold to local people at a percentage of the market price (70%). The Trust retained a charge on the properties (30%), to cover the difference in value between the affordable and full market price, and managed to make a profit after repayment of the loan.

Making a profit was always an essential part of the green homes schemes because it allowed the Trust to cover the risk of borrowing and fund its other charitable activities. For example, out of its earned income, the Trust has funded its education team, which carries out independent work locally on environment and education issues.

While owning the land was a key factor in securing the loan, the company's track record and the quality of its board of trustees also played an important role. The trustees were very involved in the whole process. As Jon Aldenton, Chief Executive, puts it: 'You can't possibly borrow that kind of money without the intimate involvement of your trustees; in our case they were involved every step of the way'. His advice to other development trusts considering loan finance is to start with simple projects, develop their board along the way and slowly build their track record. He argues that: 'Ultimately you cannot grow a successful development trust if you don't concentrate on change, and this cannot be done on a grant mentality'.

Project:	Affordable green homes for local people
Lender:	Unity Trust Bank
Amount borrowed:	£2.5 million
Achievements:	Helped generate income for other charitable activities
Lessons learned:	Developing a solid board of trustees is key to success
Contact:	Jon Aldenton (Chief Executive) jon@envirotrust.org

St Aidans Community Trust
Buying the village inn

The Rookhope Inn in St Aidans

Rookhope is an isolated rural community in Upper Weardale, County Durham. The village is located in beautiful countryside but suffers from severe deprivation following the loss of a major employer in the area. In 2003, Saint Aidans Community Trust decided to raise a total of £300,000 to purchase, refurbish and equip the Inn. Of this total, £120,000 was in the form of loan finance from Unity Trust Bank and the Community Loan Fund. The Inn is now fully trading and is an important landmark on the Coast to Coast cycle route.

The trustees felt they had to move quickly to purchase the Inn, and that traditional grant support would have taken too long. Initially, the Trust negotiated to rent the Inn and began trading. Within a relatively short period it secured the £120,000 loan and obtained grants to purchase the freehold and fund the improvement and development stages.

For the Trust's secretary and his trustees, there seemed to be little alternative to loan finance if they wanted to achieve their vision and make the Inn a focal point for the Trust and the village. The Inn has also become a successful enterprise for the Trust, generating income through the pub, bed and breakfast accommodation, and a bicycle rental business.

Borrowing was not without its challenges, and getting all the necessary components in place initially took some time. However, thanks to an attractive business plan the Trust managed to secure the deal and is ready to take on further loans. The latest project is the creation of 'Rookhope Rural Campus', which utilises unused or under-used buildings in the village to attract visitors. The Trust now has its eyes on a former university building and has the opportunity to take out an additional loan to purchase the freehold.

Project:	Purchase of the village inn
Lender:	Unity Trust Bank/Community Loan Fund
Amount borrowed:	£120,000
Achievements:	Turned a derelict pub into a community asset
Lessons learned:	Having all the players and plans in place meant the Trust could seize the opportunity when it arose
Contact:	Chris Jones (Company Secretary) chris@rookhope.com

DTA and *bassac*
The Community Hub

33 Corsham Street

In 2006, the Development Trusts Association (DTA) and *bassac* (British Association of Settlements and Social Action Centres) co-purchased an office building in central London. This 'community hub' is set to enhance organisational sustainability, improve efficiency and help reconfigure resources towards better services for community organisations across the country. Both organisations have a history of working in partnership and are members of the Community Alliance.

The purchase of an asset had been a strategic objective of the DTA for some time. The turning point for the purchase came when the lease on DTA's London office expired, and a break clause date for *bassac*'s south London offices became imminent. A jointly owned company, the 'Community Hub', was set up and purchased the freehold of a three-storey office block of 5000 square feet, conveniently situated in Shoreditch, on the borders of the City. The Hub then 'sold' a 999-year lease to each partner on the basis of identifiable floor space in the building.

The total project costs were £1.5 million, including purchase price, refurbishment costs, professional fees and VAT. This was financed with a £770,000 loan from Unity Trust Bank, a £230,000 loan from Esmée Fairbairn Foundation/Charity Bank, a £483,000 grant from the Home Office and a number of smaller grants from City Parochial Fund, Monument Trust, Gatsby Charitable Foundation and the Baring Foundation.

Joint purchasing enabled both organisations to buy a building big enough for shared offices, plus some capacity for additional lettings. Both organisations are now saving money through shared posts and services, and are using that money to enhance their work. Added advantages include the opportunity to support other community sector agencies, which benefit from the accommodation and facilities, as well as informal exchanges of know-how within the building.

During the lengthy process of purchase and refurbishment, both organisations learned a lot about structures of collaboration in a joint venture, the importance of communication across the staff teams, and the need for a firm brief for professionals. The partners have commissioned an external evaluation to capture lessons learned and share these with others in the sector.

Project:	Purchase of a joint office building in London
Lenders:	Unity Trust Bank, Esmée Fairbairn Foundation/ Charity Bank
Amount borrowed:	£770,000 from Unity Trust Bank and £230,000 from Esmée Fairbairn Foundation
Achievements:	First freehold asset and a more effective partnership
Lessons learned:	The need for a firm brief for professionals
Contact:	Tina Winders (Finance Director) t.winders@dta.org.uk

Royds Community Association
The Enterprise Park

The Royds Enterprise Park

Royds Community Association (RCA) is a community led social enterprise supporting regeneration and renewal in Bradford. The Royds Enterprise Park is a new £5 million development, comprising a range of units designed to accommodate both start-up and established businesses. The Park was largely funded through the Single Regeneration Budget, but when it turned out that the cost of building the Park was greater than the public funding available, the Trust turned to loan finance.

The Enterprise Park was RCA's first project of this size, and although it had built up a portfolio of assets that included two shops, two community centres and a healthy living centre, it had never borrowed. Initially, most trustees on the board, including business representatives, were reluctant to take out loan finance, but in the end everyone agreed that RCA's best option was to borrow £200,000 from NatWest to complete the final stage of the Enterprise Park.

The Royds Enterprise Park has already helped the Trust achieve some of its charitable aims by enabling local people to access business start-up units, and by generating surpluses that subsidise a welfare benefit advice and debt service, a community environmental programme, and a youth engagement programme. Tony Dylak, RCA's Chief Executive, hopes that over time, and with the Park's income-earning potential, the trust will be able to develop a healthy reserve which will help end its dependence on grants and other restricted funding.

The biggest challenge for the organisation in taking on this loan and successfully completing the Enterprise Park was convincing the Treasury and other public funders to relax their tight fiscal interests on properties held by the trust. All of RCA's buildings were subject to legal charges and 'clawback', which meant that for a time the trust was unable to access the loan. Public funders finally agreed to reduce their charge on two of the trust's buildings, which meant that RCA was able to offer the balance between its input and the valuation as a security on the NatWest loan.

The Charity Commission provided helpful support in this matter, and the trust made a strong case to its public funders that it could sustain the Enterprise Park more effectively if it was allowed to borrow against its assets. Tony Dylak would claim that RCA definitely won that argument, and that many other third sector organisations have benefited as a result. His advice to other development trusts is that if they are going to borrow, they should make sure they factor in all the costs, and be realistic about what the organisation can manage in terms of the repayments.

Project:	The Royds Enterprise Park
Lender:	NatWest
Amount borrowed:	£200,000
Achievements:	Managed to win the argument for reducing public charges on community buildings
Lessons learned:	Seek clarity on any clawback restrictions on your assets and don't take no for an answer!
Contact:	Tony Dylak (Chief Executive): tony@royds.org.uk

West Itchen Community Trust
The St Mary Street Business Zone

The St Mary Street Business Zone, in West Itchen

The West Itchen Community Trust (WICT) is an independent company that was initially set up as part of the exit strategy for Southampton's inner city Single Regeneration Budget (SRB2) Programme, which ended on 31 March 2003. The Trust became operational the same month, and benefited from an innovative funding mechanism, via the South-East England Development Agency (SEEDA) and Southampton City Council. The mechanism was designed to allow WICT to invest in commercial property in order to generate a rental income and achieve sustainability. Early on, the City Council gifted the Trust the freehold on two properties, which would later play a key role in its strategy for sustainability.

In early 2006, as part of its work on improving enterprise and employment in the West Itchen area, WICT secured funding from the City Council to buy the first of a series of retail incubator units. These units, collectively known as the St Mary Street Business Zone, are designed to assist individuals who are starting their own retail enterprise by providing them with affordable shared retail space and access to a business coach. It proved impossible to obtain the City Council's funding in advance, so the Trust decided to use a £170,000 bridging loan from NatWest to complete the purchase of a 125-year lease of the property by March 2006, and start work on the Business Zone. The Trust used the freehold on its existing properties as a security for the loan, and repaid it four months later, when the public funding came through.

WICT's board is a mix of residents and business people, many of whom are used to dealing with property transactions, and comfortable with the idea of borrowing. This did simplify the process, but Dave Newton, WICT's Managing Director, also acknowledges the importance of the Trust's freehold properties in offering security to all parties involved. For Dave, being clear about the ownership of assets that may have been previously been purchased through a grant programme is critical, as is working with the board to make sure that it is absolutely comfortable with the idea, 'because borrowing is always a risk!'.

The Trust plans to continue its focus on enterprise and employment, and hopes to generate enough surplus from its projects, including the St Mary Street Business Zone, to maintain its programme of coaching, micro-loans and small grants for social enterprise and community groups in West Itchen.

Project:	Purchase and development of retail incubator units
Lender:	NatWest
Amount borrowed:	£170,000 bridging loan
Achievements:	Improving enterprise and employment in West Itchen
Lessons learned:	Clarifying your ownership of assets can make all the difference
Contact:	Dave Newton (Managing Director) d.newton@wict.co.uk

About the Development Trusts Association (DTA)

The DTA was founded in 1993, by people from across the country with experience of setting up and running development trusts. Our mission is 'to achieve a successful development trust in every community that wants one'.

Development trusts are increasingly recognised as an important and viable option for delivering sustainable wealth creation and building social capital in localities that face acute deprivation. This is reflected in the rapid and continuing growth in the DTA's membership – now standing at some 350 full members, with a combined annual income of about £210 million and assets of almost £340 million.

The DTA helps new development trusts get started and helps them grow from strength to strength – not least by encouraging them to learn from each other. The Association also works with a range of partners to get government and other agencies to understand and support the development trusts movement.

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