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THE CABINET

**Wednesday, 12th March, 2014 at 8.15 pm in the Conference Room,
Civic Centre, Silver Street, Enfield, EN1 3XA**

AGENDA – PART 1 ADDENDUM

**9. SMALL HOUSING SITES - APPROPRIATION OF LAND FOR PLANNING
PURPOSES (Pages 1 - 8)**

The attached addendum to the report of the Director of Health, Housing and Adult Social Care and Director of Finance, Resources and Customer Services was provided at the Cabinet meeting. **(Key decision – reference number 3780)**

(Report No.206A)

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CABINET REPORT ADDENDUM **206A**

MEETING TITLE AND DATE
Cabinet – 12 March 2014

JOINT REPORT OF

Director of Health, Housing and Adult Social Care and Director of Finance, Resources and Customer Services

Agenda – Part 1	Item: 9
Subject: Small Housing Sites Appropriation Report - Addendum	
Wards: All	
Cabinet Members consulted: Cllrs Oykenor and Stafford	

Contact officer and telephone number: Geoff Richards, 0208 379 2179

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1. EXECUTIVE SUMMARY

- 1.1 This addendum report describes how the Small Housing Sites project will be funded.
- 1.2 The addendum explains that officers have now completed a robust due diligence exercise on the source of funding for this housing project. The outcome of this exercise will result in net cash flow to the Council in excess of £50m.

2. RECOMMENDATIONS

It is recommended that Cabinet:

- 2.1 Agrees to recommend to Council an update to the General Fund Capital Programme in 2014-16 to allocate £17.3m from the Investment in Private Rented Sector Homes to the Small Housing Sites project.
- 2.2 Notes that the appointment of the preferred developer will be subject to a separate Portfolio decision by the Cabinet Members for Housing & Finance and Property, in accordance with the original Cabinet decision in July 2012.
- 2.3 Notes that specific finance and legal comments are included within the main body of the report
- 2.4 Notes that a more comprehensive report, regarding the above funding, will be presented to Full Council on 2nd April 2014.
- 2.5 Agrees to establish a separate Special Purchase Vehicle to take a lease of the 57 private rented properties, the details of which will be presented to Cabinet in June 2014.

3. BACKGROUND

- 3.1 July 2012 (KD 3517) Cabinet approved a report to redevelop seven small sites located across the Borough and delegated authority to the Cabinet members for Housing and Property & Finance to appoint a developer to build the new homes across the sites.
- 3.2 In July 2013 the Council successfully bid for £690,000 funding from the GLA to support the scheme. The grant is subject to the developer starting on site in June 2014.
- 3.3 In November 2013 Planning Committee approved all associated applications subject to conditions and the developer signing the Section 106 Agreement. The planning consent provides 94 new homes including 57 private properties and 37 affordable (20 social rent / 17 shared equity) Council owned homes.
- 3.4 In October 2013 bids were received from three developers. The bids were clarified, evaluated and a preferred bidder identified in December 2013. Following identification of the preferred bidder the Council commissioned a firm of accountants to undertake a thorough due diligence and benchmarking exercise on the private funding proposed by the preferred bidder.
- 3.5 The benchmarking exercise has demonstrated that replacing the private funder with Public Works Loan Board (PWLB) and European Investment Bank (EIB) funding would result in a significantly stronger return to the Council, a shorter repayment period, and greater flexibility over use of 94 homes.
- 3.6 On 27th February 2014 a meeting was held with EIB officials to discuss funding the Small Housing Sites project as part of a larger programme of investment in Enfield capital projects. The positive outcome of the meeting means that the Small Housing Sites project has been provisionally included in the portfolio of projects which the EIB are prepared to fund.
- 3.7 This report sets out the two funding options, and recommends PWLB/EIB as offering a better deal to the Council.

4. DEVELOPMENT FUNDING OPTIONS

Option 1 Private Finance Company

- 4.1 The bid submitted by the developer proposed a lease and lease-back structure. A third party, a private finance company would provide the upfront capital to the developer to build all 94 properties to a specification agreed with the Council. Upon completion of the construction, 37 homes would be handed back to the Council as affordable homes with the remaining 57 let privately.
- 4.2 This arrangement necessitates the Council as freeholder to lease plots of land to the funder with the funder leasing the land occupied by the 57

dwelling back to a Council owned Special Purchase Vehicle (SPV). The lease and lease-back structure provides the private finance company with an interest in the land to secure their investment. The structure also provides a means for the Council to repay the funder for the cost of building the homes.

- 4.3 The lease with the funder would operate for a period of forty one years, including an estimated period of one year for building the new properties. At the end of the lease term, when the amount advanced by the funder has been repaid, the lease structure of all the homes held under the lease to the funder and the lease-back to the SPV would collapse with full unfettered ownership reverting to the Council.
- 4.4 The private finance company proposes repayments of principal and interest to be calculated at 4% + RPI (capped at 5% RPI per annum). The private rents would need to be increased annually throughout the 40 year payback term to keep pace with the RPI linked repayments. If the economy experienced high inflation the Council might not be able to pass on the full rental increase to the private tenants. A divergence between the rate of rent increase and the rate of change in RPI would result in the rental income being less than the payments to the funder. Repayment of interest and principal equates to a cost of finance which exceeds 12%.

Option 2 PWLB/EIB Finance

- 4.5 Under the PWLB/EIB structure, the Council will be responsible for borrowing the £17.3m construction cost. The Council will lease the developer short leases for the affordable housing plots and long leases for the private rented plots. Once the SPV has been established the long leases will be assigned to the SPV and the long leases will be used as the mechanism for the SPV to repay the loan to the Council.
- 4.6 Once the 37 affordable homes have all been constructed the short leases will be terminated and the affordable homes will be held in the HRA.
- 4.7 The total cost of the construction will be funded through council borrowing over 40 years. In practice there would be sufficient rental income generated from the 57 private rented homes to repay the EIB element of the loan after 25 years and the PWLB element after 29 years. A full 11 years sooner than would be the case if the scheme was financed privately.
- 4.8 The appended graph highlights the marked difference in the net cash flows into the General Fund between the public and private options. The difference between the options is particularly notable after Year 25, when the EIB element of the public loan option has been repaid. The PWLB/EIB option improves the net cash flow to the General Fund by £59m over a 40 year period. This is based on an annual RPI increase of 5%.
- 4.9 This option provides the Council with greater flexibility to repay the loan in full or sell the properties at any point in time. The Council would also own all 94 homes throughout the duration of the loan being repaid (the SPV would be wholly owned by the Council), whereas under the privately funded model the

Council would not own the 57 private homes until collapse of the lease structure at Year 41.

- 4.10 An SPV is required for this option because legal advice recommends against holding housing assets in the General Fund unless they are held in a SPV. Holding homes in an SPV also removes the risk of tenants seeking the Right to Buy. The SPV will be the subject of a separate report to Cabinet in June 2014 and further information about the composition of the company will be provided at that stage.
- 4.11 The Council will arrange the borrowing from PWLB/EIB and lend on to the SPV at a rate which is the greater of either the Council's cost of borrowing or the EU reference rate (to mitigate the risk of the SPV being caught by State Aid legislation – the EU reference rate is currently 4.88%). The SPV will be expected to repay both principle and interest on a 6 monthly basis which equates to an effective cost of finance of 5.9%.
- 4.12 The structure of the loan to the SPV will allow interest and principal payments to be capitalised in the early years of the loan and large repayments been made by the SPV in the later years when cash flows are more secure.
- 4.13 The Director of Finance, Resources & Customer Services will make the final decision on funding the loan to the SPV.

5 ALTERNATIVE OPTIONS CONSIDERED

- 5.1 The alternative option considered was to progress a lease and lease-back option with another third party funder. Public Works Loans Board (PWLB) / European Investment Bank (EIB) borrowing is cheaper than an income strip from other private funders.

6 REASONS FOR RECOMMENDATIONS

- 6.1 Council officers in their commitment to achieve best value to the Council, commissioned a reputable consultancy firm to undertake further modelling on the different funding options. The result revealing a net cash flow of £59m between the two funding options.
- 6.2 The £59m positive difference is a compelling reason alone to recommend the PWLB/EIB option over the private alternative. However, the PWLB/EIB option also results in a shorter repayment term and means that all 94 homes, not just the 37 homes, remain in the Council's ownership throughout the loan repayment period further underlining the superiority of this option.

7. COMMENTS OF THE DIRECTOR OF FINANCE, RESOURCES & CUSTOMER SERVICES AND OTHER DEPARTMENTS

7.1 Financial Implications

7.2 This report recommends allocating financial resources already approved under the capital programme to generate a net cash flow of £63m from the alternative of using private funding. This allocation of funds will enable the project to start on site in June; the timeframe set by the GLA and the date by which the developer has agreed to hold their prices.

7.3 Securing PWLB/EIB funding to invest in this project demonstrates the Council's commitment to bringing forward 94 new homes that the Council will own from day 1; maximise grant opportunities to deliver disability compliant properties and sheltered housing for working Londoners; contribute to the Council's key objectives to promote economic growth, environmental improvements and social benefits; and help to decant tenants/leaseholders from other major regeneration projects.

7.4 There are no additional costs to the Council from the recommendation to reallocate £17.3m from the Investment in Private Rented Sector Homes to the Small Housing Sites project. This borrowing has already been factored into the Council borrowing requirement.

7.5 The Financial Regulations contained within the Constitution state that:

7.6 "The allocation of additional Council resources to schemes in the approved programme, or to new schemes, is subject to the following process:

7.7 Schemes which are not part of a rolling annual block allocation – for increases above £500k, a Council decision following a Cabinet recommendation"

7.8 In order to comply with this requirement Cabinet is being asked to recommend the addition of this scheme on the Capital Programme to Council, on the basis set out in the report.

7.9 Legal Implications

7.10 The allocation of the finances is in accordance with the Financial Regulations contained within the Constitution.

7.11 The establishment of the company will be in accordance with section 95 of the Local Government Act 2003 and Section 1 of the Localism Act 2011 (the general power of competence). Full legal implications will be included in the report to Cabinet of 25th June and are also contained within the original report.

7.12 Property Implications

7.13 There are no direct property implications with this addendum. Property implications will be considered in subsequent reports to be presented in June.

8 KEY RISKS

8.1 The key risk in relation to this project is a start on site is not made by the end of June 2014 and the GLA subsequently withdraw the grant funding.

9 IMPACT ON COUNCIL PRIORITIES

9.1 Fairness for All

9.1.1 The proposals for the Small Housing Sites ensure fairness for all members of the local community by consulting with residents on redevelopment proposals in their area, and taking on board the views of all sections of the community, prior to the Council taking a decision on the future of the housing stock in the opportunity area.

9.2 Growth and Sustainability

9.2.1 Growth and sustainability are central to the proposals for the Small Housing Sites. The final proposal will boost growth in terms of increasing the supply of quality residential housing in the area. Furthermore, all options will prioritise environmental sustainability, including improving the energy efficiency of the residential buildings and promoting recycling and sustainable transport.

9.3 Strong Communities

9.3.1 The proposals involve the community in the decisions that will shape their area and foster a greater sense of community cohesion in the area.

10. EQUALITIES IMPACT IMPLICATIONS

10.1 A full equalities impact assessment has been prepared for the project.

11. PERFORMANCE MANAGEMENT IMPLICATIONS

11.1 N/A

12. HEALTH AND SAFETY IMPLICATIONS

12.1 The preferred bidder passed the mandatory health and safety evaluation.

13. HR IMPLICATIONS

- 13.1 Delivering the Small Housing Sites project coupled to other regeneration projects represents a significant undertaking for the Council. The Development and Estate Renewal Team has had to expand to ensure that the complex needs of residents are being met.
- 13.2 As the project evolves so the need for different skills to adequately resource the demands of the project will need to evolve so the team will need to maintain a flexible approach.

14. PUBLIC HEALTH IMPLICATIONS

- 14.1 There are a number of public health implications that arise as a result of redeveloping the Small Housing Sites. Issues arising during the demolition and construction phases will be closely monitored and contractors will be required to work in accordance with the Considerate Constructors Scheme.

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