

REPORT FOR DECISION



DECISION OF:	The Cabinet
DATE:	29 July 2020
SUBJECT:	Next phase modelling of the housing development programme (part A)
REPORT FROM:	Leader and Cabinet Member for Finance and Growth
CONTACT OFFICER:	Vicky Carroll, Director of Housing
TYPE OF DECISION:	Key Decision
FREEDOM OF INFORMATION/STATUS:	For Publication
SUMMARY:	The purpose of this report is to update cabinet on the modelling of the development program and work on likely delivery options.
RECOMMENDATION	<p>The Cabinet is asked to :</p> <ol style="list-style-type: none"> 1) Note the progress towards a business case for c500 new homes development program. 2) Progress to the next stage of planning with a total budget of maximum of £119k taken out of reserves. 3) To come back to cabinet later this year with a full business case for final approval for a delivery model
IMPLICATIONS:	
Corporate Aims/Policy Framework:	Do the proposals accord with the Policy Framework? Yes
Statement by the S151 Officer:	The feasibility work to date indicates that there is merit in proceeding to "full business plan" stage. This report

<p>Financial Implications and Risk Considerations:</p>	<p>only seeks approval for the funding to work up the full business case. No further investments or commitments will be made before a full business case has been approved.</p> <p>There are key risks in any housing development scheme, including variations in interest rates, construction costs, sales and rental values, pace of development, voids, etc. (see section 7 of the main report). Other notable risks include the significant economic uncertainty in the UK at the moment resulting from Covid-19 and Brexit.</p> <p>The feasibility work to date needs to be progressed to a much more detailed level to test whether the proposals are financially viable and what the optimal delivery vehicle would be.</p> <p>It should be noted that the financials in this report do not include assumptions about the significant wider economic benefits to the borough, or other related income streams to the council (e.g. additional council tax receipts).</p> <p>It is proposed that the next stage of planning be funded from corporate reserves.</p>
<p>Equality/Diversity implications:</p>	<p>none</p>
<p>Considered by Monitoring Officer:</p>	<p>Anthony Collins Solicitors have been instructed to advise on the legality of the options available to the council to seek to deliver new housing on council owned sites to meet the shortage of both affordable and specialist accommodation in the borough. They have advised that the Council has a wide range of legal powers to develop its land in this way and there are a number of options available to be considered. A detailed business case will fully explore these options enabling member to make an informed decision on the best way forward.</p>
<p>Wards Affected:</p>	<p>All</p>
<p>Scrutiny Interest:</p>	<p>Overview and Scrutiny</p>

1.0 BACKGROUND

- 1.1 There are related streams of work ongoing in parallel which provide context to and develop the case for a housing development company.
- 1.2 In March and also subsequently in May the Cabinet approved the principal of developing new homes on several council owned sites through direct development. The First Phase program, work has been progressing well and over the last few months officers have identified further sites, which subject to due diligence, could form the basis of a program of c500 new homes.
- 1.3 In April we procured external consultant support from Anthony Collins solicitors and Penningtons to help look at the options for delivery models, including that of a development company (Dec Co), to optimise the potential increased program. Anthony Collins solicitors were commissioned to review the options for legal structure and Penningtons the outline business case financial model. Penningtons ran an internal workshop with senior officers in early June to ascertain the key objectives for accelerating and expanding a development program on council owned sites.
- 1.4 In Spring Arc4 Ltd conducted the Housing Needs and Demand Assessment (HDNA) and Campbell Tickell are working on developing the Housing Strategy. Recent work on the HDNA has identified that Bury has one of the largest affordability gaps in Greater Manchester, the gap between what people earn and what income they would require to comfortably buy or rent in the Borough. The survey work demonstrated that we are also seeing the housing market failing to provide in several of our townships. The emerging HDNA results have fed into the outline business case for a development company.
- 1.5 We are currently developing the Bury 2030 strategy, and supported through work led by the Business and Growth Initiative Directorate, we are developing a strategic place making approach in Bury to regenerate in several areas and link into other key stakeholder investment work. It is known that integral to this work is new build housing development, for instance The Radcliffe Strategic Framework, currently out for public consultation, includes within it several key housing sites which are owned by the Council

2.0 Introduction

- 2.1 The HDNA provides a clear evidence base to increase the numbers of new build housing being delivered in the Borough. In the past the Council has tried to increase housing delivery through working with partners such as Registered Providers and Commercial Developers as well as building directly through the Six Town Housing. Since 2017 the Council have directly developed a small program of new build homes including Mayfair gardens and Radcliffe Times.
- 2.2 There are many different approaches that Bury could adopt to achieve the interventions we want to see. As the smallest GM authority, we do not have a track record of delivering joint ventures for housing sites, previously we have taken more traditional routes of disposing of housing land for others to develop. We have some experience of direct development and we are growing

our expertise in this area. This paper sets out the case for seeking to use our financial capacity to develop directly on our own housing land to retain control of quality, capture profit, attract grant and drive delivery.

- 2.3 The Council currently has a small development program of new build homes and we have Homes England Partnership status. We directly bid and access grant funding from Homes England and fulfil all their regulatory requirements. To help to increase the required supply of new homes we can expand this development program and consider building via a variety of models including that of a Dev Co. This paper sets out the work that has been completed so far and what is required in the next stage.
- 2.4 The Council has identified five brownfield sites in its ownership and these together with others in the Council ownership have the potential to deliver up to 600 new homes, of which c230 are on the brownfield sites.
- 2.5 The Council owns a wholly owned company limited by guarantee, Six Town Housing Ltd (STH) that is an arm's length management organisation responsible for managing the Council's housing stock. Within the Management Agreement, the development of new affordable housing is a function retained by the Council.
- 2.6 The Council envisages the STH will have a role in managing any rental properties. It may also have a role in the development, sale of any for sale properties, including shared ownership.
- 2.7 The Council has Partnership Status with Homes England and can access grant funding.

3.0 Bury Housing Development Program Primary Objectives

- 3.1 An internal workshop run by external consultants with senior executive officers, concluded that primary driver for expanding the housing development program and potentially setting up a Bury Dev Co was to meet strategic housing objectives, profit was a nice to have but not the focus.
- 3.2 The main recommended primary objectives for accelerating and expanding the development program are-
 - To ensure that new housing is built in the Borough
 - Meet identified need for housing in the borough that would otherwise not be addressed by the market
 - Provide a range of housing products and tenures, including specialist accommodation, to help close the Bury affordability gap and increase the number residents in higher quality new homes in the Borough
 - Contribute to meeting the Council's carbon neutral 2030 policy goal
 - Support place shaping regeneration in the town centres and neighbourhoods

The main housing products referenced in the objectives, that can assist our residents, are explained in the table below (along with a description of the current respective roles of the Council and STH with regards each).

Product	What it is	STH	Bury
Shared Ownership	Customer can part buy a property in "tranches", they get a mortgage for each tranche, first tranche sales can be anywhere between 25% - 75% of the property and the customer pays rent on the remaining element. Once living in the property they can stair-case up (buy more shares, up to a full 100% ownership)	Collect the rent element, manage the leaseholder agreement, manage service charges	Apply for grant funding, build and sell the properties raise the building insurance, manage further sales through stair-casing (buying more shares in the property, up to a full 100% ownership)
❖ Rent to Buy	Customer rents a property at below market value then have option to buy after year five.	Collect the rent, manage the tenancy, and manage services and service charges.	Apply for grant funding, build and sell the properties
Affordable Rent	Affordable Rent 80 % of market rent	Collect the rent element, manage the tenancy and services charges	Apply for grant funding, build the properties
❖ Market sale	Properties sold on the open market		Sell the properties

❖ Bury has not yet developed these products

NB All new build homes are built and financed by the Council, we then contract STH to manage the rental properties and elements of the service on sales homes on our behalf.

4.0 Options for delivery

4.1 Anthony Collins Solicitors consider a number of potential options including delivering a housing development program c500 new homes over 5 years.

4.2 Their comprehensive legal report considered the five main options below

Option 1	Do nothing
Option 2	Prepare the Sites – remediation works/infrastructure works and possibly obtain planning permission. Sell the sites to either a private developer or in accordance with Options 4 and 5.
Option 3	Develop the Sites directly: <ul style="list-style-type: none"> • retain the social rent properties (or dispose of to STH or another RP); • dispose of affordable rent properties to STH or another RP; • dispose of the market for sale properties directly (potentially with assistance from STH or a private agency); • dispose of the sub-market for sale properties directly (e.g. if just a direct sale at less than best consideration) or to STH to manage a shared ownership arrangement; • dispose of the private market rental properties (including sub-

	market but not social/affordable rent) to STH or Rent Co.
Option 4	<p>Dev Co develops the Sites:</p> <ul style="list-style-type: none"> • the Council disposes of the Sites to Dev Co; • Dev Co procures the developer and possibly contracts with the Council and/or STH for services to support the development; • the contractor develops the Sites on behalf of Dev Co; • Dev Co sells the social/affordable rent tenure properties and any sub-market sale shared ownership properties to STH; • Dev Co sells the market sale and sub-market non-shared ownership sale properties directly; • Dev Co sells the private market rental units (including where they may be let at sub-market rents but are not social/affordable rent) to Rent Co.
Option 5	<p>A variation on Option 4, the Council sells:</p> <ul style="list-style-type: none"> • the land for private market rental units (including sub-market rents that are not social/affordable rent) to Rent Co; • the land for social rent/affordable rent and sub-market sale shared ownership properties to STH; and • the land for private market sale and sub-market direct sale to Dev Co. <p>STH and Rent Co enter into a development services agreement with Dev Co for the development of their portions of the Site. Dev Co lets a contract for development.</p>

4.3 Options 4 and 5 reference setting up a Dev Co, these have a variety of benefits including, providing a VAT shelter reducing overall costs; enabling agility to move in commercial market conditions; control quality and speed of delivery. When developing on Council owned land they can also assist reducing profit leakage to private commercial developers.

4.4 Currently several LAs in GM and the surrounding areas that have or are exploring setting up Dev Co's to progress their strategic housing ambitions to specifically deliver more new build housing this includes Manchester, Salford, Rochdale, West Lancs, Stockport and Wigan. We have been in touch with them all and have begun early discussions about how we can work together strategically to help deliver, this could be through bespoke procurement framework, sharing market intelligence and even working on joint projects such as specialist housing provision.

5.0 Financial Implications & Risk

5.1 All development schemes carry some risks. In general terms, the risks that we will face can be categorised as follows:

Main Risks	Tactical Risks
<ul style="list-style-type: none"> •Costs of construction (e.g. ground issues, quality, etc) •Price (e.g. sales and/or rental risk; volume and pace of sales) •Market need and demand (i.e. fundamental mistakes in assessing the market) •Costs of operation (e.g. routine maintenance, major works) •Finance (not as much of an issue in or case, borrowing from PWLB) 	<ul style="list-style-type: none"> •Tax •Loss of stock (e.g. Right to Buy, future changes to government legislation, etc.) •Financial modelling (e.g. modelling assumptions materially inaccurate) •Risk transfer failure (e.g. failures in contract, warranty, indemnity, etc.) •Change in building standards (e.g. change in legislation/ government policy such as standards and rent regulations) •Board governance (passing decision making powers to another board/ group of people)

5.2 Risks such as 'price' and 'market need and demand' increase in correlation to profit requirements and/or numbers of sales required to subsidise sub-market rent housing. Risks such as 'cost of construction' can vary significantly from site to site. As we are currently looking at brown field sites, these risks are inherently higher than on clean sites.

5.3 Other risks tend to apply consistently across all scenarios. The mitigation for these risks includes:

- Robust financial assumptions, models and appraisals
- Expert advice (legal, tax, QS, architects, housing market assessment, etc)
- In built flexibility (e.g. ability to transfer "for sale" properties to market rents)
- Use of appropriate partner (e.g. STH) to operate/maintain properties
- Appropriate governance arrangements

These will all need to be covered in detail in the full business case.

5.4 There are inherent risks with developing new homes that we would continue to manage through widely used design and build contracting arrangements and specialist housing frameworks designed to manage and mitigate key risks through the design, development and defects stages.

5.5 Where risk on individual sites is considered high we would retain the ability to do joint ventures with developer partners that may limit the risk in terms of cost of remediation or number of homes for sale.

6.0 Next Steps

6.1 The next phase of the work will procure detailed advice on the accounting treatment and implications for the Council for Dev Co structure options. We will review the recommended proposed company structures for optimum delivery of the project, governance and risk mitigation and get external assurance of the current Council financial model for the proposed development in terms of

assumptions made and proposed phasing for investment and return. We will model the housing development program with a level of sophistication that will allow us to see the relative profitability across several investment measures, including internal rate of return.

6.2 The next phase of work will require a budget as outlined below

Item	Detail	Budget
Financial Services	Advice on the accounting treatment and implications for the Council for the proposed housing company structure options: a. Reviewing the proposed company structure for optimum delivery of the project, governance and risk mitigation, b. Providing advice on the accounting treatment for the Council and any trading companies in terms of balance sheet including borrowing /minimum revenue provision, and c. Initial assurance review of the current Council financial model for the proposed development in terms of assumptions made and proposed phasing for investment and return.	£30-£40k
	Continued financial modelling assurance and programme level management and oversight.	£30-£40k
	Development finance, RICS valuation and market assessment expertise on scheme modelling, due diligence on sites, valuation and market assessments on phase 2 sites if required	£10-£20k
Legal Services	Adjustments to structure as required	£4k
Site Due Diligence	Budget for investigation work if required for phase 2 sites	£15k
Overall Total		£89-119k

7.0 CONCLUSION AND RECOMMENDATIONS

- 7.1 Further work is required on the financial detail of both the delivery models and the capacity to meet the overall ask of the program. To progress we need to procure specialist financial advisors to support the project team. We can use the next few months to further increase the due diligence on sites, by expanding the work on phase one to include sites in a phase two program.
- 7.2 It is recommended to progress this work and to return to Cabinet later in the year with a business case for how to take the development program forward.
- 7.3 A budget of up to £119k has been identified from 2020/21 corporate reserves. It is recommended that this budget is used to procure support and advice for the full business case; and that it be monitored and decisions in its regard be signed off by the Joint CFO and Chief Executive.

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