

Cabinet

10 June 2015

Housing Stock Transfer – Completion Update



Key Decision R&ED/01/15

Report of Corporate Management Team

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Purpose of the Report

- 1 The report updates Cabinet on the completion of the transfer of ownership of the Council's housing stock to the new County Durham Housing Group Ltd (CDHG) and its component housing management organisations; Dale & Valley Homes Ltd, Durham City Homes Ltd and East Durham Homes Ltd on 13 April 2015.
- 2 The report also highlights key issues arising during the final stages prior to completion, and features significant benefits and commitments contained in the final agreement and contract documentation.

Background

- 3 In March 2014, the Council received initial, conditional, approval from the Department for Communities and Local Government (DCLG) of its proposal to transfer its housing stock to a group structure of the existing housing providers.
- 4 The key condition concerned formal consultation with the Council's secure and introductory tenants. Having considered the matter, along with the draft Offer Document for tenants, Cabinet agreed to proceed on 7 May 2014.
- 5 Formal consultation began in June 2014. On 16 July 2014 Cabinet considered a report on the consultation process and representations made by tenants, and approved proceeding to a ballot of tenants in July and August 2014.

- 6 On 10 September 2014 Cabinet received a report highlighting the outcome of the ballot and the clear preference of tenants for transfer to proceed. Over 11,000 tenants (51.2%) took part in the ballot, 9,149 (82%) tenants voted in favour of the transfer.
- 7 Cabinet agreed to proceed with the transfer process in accordance with the positive ballot outcome in September 2014. At the same meeting, Cabinet also approved another report which set out the proposed principles around the transfer negotiations and agreed the appropriate delegations to enable progress towards completing the housing stock transfer within the timetable required by Government.
- 8 Between September 2014 and early 2015, the project made significant progress and on 11 February 2015 Cabinet received a further report outlining progress and issues arising. In particular, the report sought approval to commit to the final stages and submit, by 23 February, the formal applications to Government for Secretary of State's consent to complete the transfer on the projected date of 23 March. This timetabling was especially tight in order to meet the deadline indicated by Government twelve months previously when the initial approval was given.
- 9 When the Council's formal submission was made on 18 February, DCLG indicated firm support for the Council's proposal but advised that the actual transfer completion date should be put back beyond the original deadline in order to enable costs associated with debt premia to be appropriately addressed.

Completion of the Transfer

- 10 In the event, the postponement requested by DCLG amounted to three weeks, including the Easter public holidays. Formal consent documents, including confirmation of the necessary debt write-off, were approved by Ministers and issued by DCLG on 10 April. Completion of the Transfer Agreement duly took place on Monday 13 April 2015.
- 11 Two additional consents were obtained from DCLG, authorising closure of the Housing Revenue Account during 2015/16 following transfer, and retention by appropriation to the General Fund of six non-transferring former Housing land assets.

The Transfer Agreement

- 12 The Transfer Agreement records the complex deal reached between the Council and County Durham Housing Group (CDHG) at the point of transfer. It has legal status and enforceable power as the contract entered into by the parties.
- 13 The Transfer Agreement documents in detail the transfers which have taken place of homes, land, employees, contracts and leases with third

parties, income streams, debts and other assets. These details reflect transfers of rights and ownership.

- 14 The Transfer Agreement also records and requires of the parties duties, obligations and responsibilities, notably the delivery of the Council's promises to tenants outlined in the Offer Document, "Your Home, Your Future, Your Choice" published to inform the choice made by tenants when they were balloted in July and August 2014.
- 15 Further, the Transfer Agreement documents the mutual commitments to maintain support, service and partnership in delivering housing services, new home provision and neighbourhood and community development in County Durham. This includes a schedule of 19 Service Level Agreements (SLAs) through which the Council will support CDHG in its early stages as contractor/partner. The largest of these relate to grounds maintenance and ICT. Use of SLAs will help to ensure maintenance of business and service by the housing company for the benefit and reassurance of tenants and neighbourhoods.
- 16 A copy of a plain language headline summary of the transfer agreement (submitted to DCLG as part of the documentation supporting the Council's application for final consent to transfer) is attached for information as Appendix 2.
- 17 Accompanying Durham's Transfer Agreement are two other contractual documents relating to the transfer of land for potential new housing development; a Development Sites Agreement and an Options Agreement.
- 18 The Development Sites Agreement relates to 23 sites of former Housing Revenue Account land transferred at nil value to facilitate new home building, predominantly for social housing, and in support of the Council's requirement of CDHG to produce 700 new homes in seven years following transfer.
- 19 The Options Agreement relates to 6 General Fund sites and allows CDHG the option, for seven years, to buy these sites, individually, or collectively, for additional development in pursuit of the commitment to create new homes in the county. The agreement includes an annual fee, to cover management and maintenance, payable to the Council until the option is taken up.
- 20 Using simple projections of 35 homes per hectare, the sites covered by the two agreements are capable of comfortably accommodating the prescribed first seven years target of 700 new homes.

Transfer Principles and Key Features of Final Agreement

- 21 The Principles of Transfer (referred to in paragraph 7 above) served all parties extremely well in the lengthy and complex process of identifying

what land should comprise the transferring housing asset and of mapping and addressing the consequent title and conveyancing issues essential to completion of the legal transaction.

- 22 The transferring land relating to the housing stock covered 540 sites and the potential development and option sites added 29 more. Negotiating this with CDHG and preparing the mapping and title documentation was concluded by late February when the provisional proposals were made available for viewing by elected members.
- 23 The only Principle of Transfer which the Council agreed to vary related to land beneath adopted highways. It was originally agreed that this should be retained in Council ownership. However, in making background progress to confirm and document ownership titles, and also as a negotiating point to obtain more favourable detailed terms for the Council, it was decided to transfer the land beneath adopted highways, where the Council is owner, as part of the much larger agreement.
- 24 The reasons for this departure from the principles were:
- The Council had clarified through title searches that it did not own all the land in question.
 - Ownership of sub-soil is not essential to the Council as highway authority in maintaining its statutory obligations or service standards.
 - The limited potential for the Council using sub-soil ownership to control future development of the land is covered by other statutory and contractual controls.
 - Provisionally removing this negotiating obstacle facilitated progress on other, more demanding features of the transfer agreement to the extent that, by transfer day, the overall agreement on offer was such that this concession was considered minor against the major beneficial outcomes to be achieved on other matters.
- 25 On the related matter of un-adopted roads and paths, a mutually beneficial agreement has been reached and accommodated in the Transfer Agreement. Across the transferred estates, 101 sites contain roads and footways which are not formally adopted but are, nonetheless, the liability of the County Council. A significant number of them require repair or improvement to restore amenity and mitigate risk and liability. They are not all immediate priorities for attention using the Council's own resources, although they would require attention in due course. However, as part of the wider transfer negotiations, CDHG has agreed to pay the Council up to £1.8 million to repair and improve these roads and footways over the next seven years. The work will be agreed between the parties annually and, where practicable, will be integrated with CDHG's investment work in respective neighbourhoods. Accordingly the Council will adopt the roads and footpaths in question by the end of the year after their improvement.

Financial Settlement

- 26 The price that CDHG has paid for the housing it acquired through transfer is based on its Tenanted Market Value (TMV). This valuation of housing stock for stock transfer is entirely different to Open Market or Right to Buy values.
- 27 The Transfer Price of the dwellings and associated assets is largely determined by a prescribed formula set by Government and reflects the current value of future income/ expenditure streams of the assets over the next 30 years. In broad terms, the Transfer price is the amount of money which a registered provider purchasing the properties would be able to borrow to buy them and fulfil the Council's transfer promises and then repay the loan by the end of year 30 using all the annual net income streams.
- 28 The Council's attributable housing debt at the point of transfer was £244m which was repaid by a combination of capital receipts proceeds and Government grant. The sale price of the housing stock to CDHG was £114.4m and the DCLG agreed to write off £129.6m. In addition DCLG also financed the early debt redemption premiums of £77million.

Financial Implications for the General Fund

- 29 Previous reports to Cabinet have detailed the financial implications to the Council and the General Fund as a consequence of transferring stock to CDHG. To recap, the cost to the General Fund is £3.550m and this has been accommodated into the MTFP and annual budget for 2015/16.

VAT Shelter

- 30 In normal circumstances, housing associations are not able to reclaim VAT on improvement works to dwellings. A VAT shelter is an arrangement whereby a housing association can reclaim VAT on future improvement works to the transferred stock. This scheme has been devised and implemented in nearly all stock transfers since 2003 and has approval from Her Majesty's Revenue and Customs (HMRC) and the Government.
- 31 A similar arrangement has been agreed for this transfer with any benefits being shared equally on a 50/50 basis between the Council and CDHG. It is forecast that the Council will receive capital income of £29.2m between 2015 and 2030 from the VAT shelter.

Pensions

- 32 Under provisions of TUPE regulations that govern the transfer of a business from one body to another, the pay, terms and conditions of transferred employees are protected – but participation in the Local Government Pension Scheme (LGPS) is not protected. Government

guidance states that when public sector employees are transferred to a new employer in this way the new employer must either:-

- a) Provide a 'Broadly Comparable Pension Scheme' for the transferring employees to join; or
 - b) Apply to join the LGPS as an 'Admitted Body' via an Admission Agreement.
33. In line with practice in previous stock transfers in Durham, the four organisations forming the CDHG secured admission to the LGPS as 'Admitted Bodies' with current staff and new staff continuing to have access to the pension scheme on an 'open scheme' basis. The Council has provided a guarantee to the Pension Fund in respect of the pension liabilities associated with the transferring staff. Pension Liabilities associated with new staff will be monitored on ongoing basis with the council having the option of CDHG providing a Guarantor Bond for these liabilities.
34. The Council has a long term strategy for dealing with pension contributions and liabilities including any deficit. That model, adopted by CDHG, was not familiar to funders and their legal advisers and demanded considerable discussion and negotiation to sustain. Precedents established in earlier transfers, where Councils fully funded deficits at the point of transfer, would not have been feasible in Durham's case. The early notice and attention drawn to the issue and the consistent position maintained throughout by the Council assisted in finalising a viable arrangement.

Warranties and Indemnities

35. As in previous housing transfers across the country, and locally in County Durham, the Council has been required to provide a number of warranties and/or indemnities as a contribution to the apportionment of the risks inherent in running a large social housing company.
36. The three main parties, Durham County Council, County Durham Housing Group and funders all sought to minimise, or even eliminate risk to themselves through placing liability on the other parties, rather than purely relying on their own due diligence, as is standard in other property transactions. This has been a standard feature of all housing stock transfers which has unquestionably made the activity more attractive and reliable to funders who have generally offered comparatively more generous lending rates.
37. All the potential risks in question existed prior to transfer and were entirely the liability of the Council. From the point of transfer, however, the Council ceases to benefit from the housing revenue streams from which financial liabilities could be met and additionally loses, through transfer, the direct control and ability to foresee, mitigate and manage liability as landlord.

- 38 These factors stimulated an assertive negotiation stance by the Council's team in order to achieve the fairest and lowest feasible levels of risk exposure.
- 39 The warranties and indemnities extended across a range of risks including:
- Title (legal ownership rights over transferred land and property)
 - Environmental contamination
 - Asbestos
 - Staff
- 40 In the case of environmental contamination and asbestos, the Council retains large potential risk should extreme circumstances materialise. Considerable due diligence was undertaken to assess likelihood and strong and clear negotiation succeeded in raising the threshold for potential claims (lower risks to be borne by CDHG) and in capping the Council's liability where possible. Additionally insurance has been obtained to cover certain special risks and mitigate exposure further.
- 41 Most warranties apply for 30 years, which is also the term of the initial funding deal obtained by CDHG. Alignment of warranties to this period is considered standard within stock transfer negotiations.

Post Transfer Monitoring of Promises and Performance

- 42 The Transfer Agreement and the original Offer Document contain between them a considerable number of commitments for County Durham Housing Group to fulfil. They range in scale from providing 700 new homes to operational service details. The respective timescales spread from first year specific requirements, through intermediate targets, such as seven years for the key initial delivery of new homes, right through to permanent, continual changes and improvements.
- 43 All these commitments are contractually enforceable through the Transfer Agreement and legal processes, but the relationship between the Council and County Durham Housing Group was never intended to be adversarial. Rather it has been conceived as a genuine partnership based on mutual interest and support.
- 44 Accordingly it is proposed that performance monitoring arrangements will be developed by agreement between the Council and County Durham Housing Group and implemented, reviewed and recorded through the Council's Overview and Scrutiny procedures.

Conclusions

- 45 The stock transfer project is the final Large Scale Voluntary Transfer to be undertaken within County Durham and it was successfully completed on April 13 2015. This was undertaken using the delegated powers Cabinet agreed which enabled the Corporate Director for Regeneration and

Economic Development and the Corporate Director for Resources in consultation with the Cabinet Portfolio Holder for Economic Regeneration and the Cabinet Portfolio Holder for Finance to agree the conclusion of the transfer deal.

- 46 The transfer presents a major opportunity, through a fully funded 30 year business plan to continually maintain decent housing standards, develop new homes and improve neighbourhood amenity across the county.
- 47 A new housing group has been created which has the scale, additional resources, heritage, values and documented commitment to support the Council in the provision, maintenance and development of housing services across County Durham for the foreseeable future.
- 48 Tenants in communities across large parts of the county have shaped the transfer, provided the Council with the mandate to complete the transfer and secured a place at the heart of the new organisations.

Recommendations

- 49 Cabinet is recommended to:
 - a. Note the completion of the transfer of ownership of the Council's housing stock to the new County Durham Housing Group Ltd (CDHG) and its component housing management organisations; Dale & Valley Homes Ltd, Durham City Homes Ltd and East Durham Homes Ltd on 13 April 2015.
 - b. Endorse the delegated decision to transfer sub-soil beneath adopted highways in concluding the Transfer Agreement in the round.
 - c. Agree the outline proposals to monitor performance and delivery against the specific terms of the Transfer Agreement and the Offer Document promises made to transferring tenants.

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Appendix 1: Implications

Finance -

The Council's housing debt has been repaid and written off in conjunction with DCLG's final consent to complete the transfer.

Transfer has been achieved at a cost to the Council. Prior reports identified an annual cost to the General Fund of £3.55m, with provision for this cost built into latest MTFP model which identifies the loss of income from 2015/16 onwards. In addition a number of the Service Level Agreements (SLAs), such as those relating to grounds maintenance, could be subject to change as they become due for renewal or termination at the end of the respective terms in the Transfer Agreement.

Cabinet authorised in September 2014 the offer of a Section 25 loan facility from the council to the County Durham Housing Group to fund necessary start-up costs. An initial loan facility up to the value of £4.5 million was made available by the Council, subject to a commercial rate of interest. This was repaid in full at the point of transfer.

Staffing -

Almost 200 Council employees transferred to the new housing group under TUPE terms. Extensive work was undertaken to manage their transfer, consult with them and keep them informed of developments.

Risk –

N/A

Equality and Diversity / Public Sector Equality Duty -

N/A

Accommodation -

There are no accommodation issues relating to the Councils' requirements resulting from the transfer.

Crime and Disorder -

N/A

Human Rights -

N/A

Consultation -

The Council delivered an extensive formal consultation programme, with all stakeholder groups, as part of its transfer proposal. Extensive dialogue, besides formal negotiations, was also undertaken by officers with representatives from the County Durham Housing Group throughout the process.

Procurement -

N/A

Disability Issues -

N/A

Legal Implications -

The extensive details of the terms of the transfer are documented in the Transfer Agreement and its accompanying documents. They form the record of an enforceable contract with all members of the County Durham Housing Group.

The consents obtained from the Department for Communities and Local Government have given the Council the necessary legal devices and authorities for completing the transfer and managing associated administration tasks.