

Chapter Homes Update

**Report of Ian Thompson, Corporate Director, Regeneration and
Economic Development**

Purpose of the Report

- 1 This report provides the Economy and Enterprise Overview and Scrutiny Committee with background information on the formation of a new company dedicated to the development and management of housing for market rent and sale.
- 2 Cabinet granted prior approval to explore and develop this project on 18 December 2013. Cabinet received a second report on 19 November 2014 which provided updated information on the procurement progress. Delegated authority was granted to the Director of Regeneration and Economic Development and Director of Resources, in consultation with the Portfolio Holder for Housing and Rural Issues and Portfolio Holder for Finance to proceed with the next stages of appointing a building contractor.
- 3 This report sets out the further work undertaken to date. The Business Plan exists to demonstrate the viability of the new company and its development programme.

Background

- 4 The Cabinet report of December 2013 agreed in principle to the establishment of a new 'bespoke' company to develop new housing for market rent and sale. By taking direct responsibility for the development of surplus Council owned land the company will benefit from developer profits and the Council will continue to secure capital receipts from the sale of land.
- 5 Following a competitive tender exercise, specialist legal consultants, Bond Dickinson LLP, were commissioned in January 2014 to give the Council specific legal advice on the advantages and disadvantages of possible company structure options. They also provided some initial high-level advice on the tax implications of possible structures.
- 6 Furthermore, in February 2014 Identity Consult were appointed to act as Technical Advisor for the overall programme following a competitive tender exercise. The Council has ensured a 'break clause' is present at each phase of Identity Consult's contract should there be a need to terminate the contract earlier than anticipated.

- 7 The Council, under its delegated authority provisions (granted in accordance with the recommendations in the report), entered into a Pre Commencement Services Agreement (PCSA) with Gentoo Construction. Building work has commenced on the pilot site at Agnew 5.

Development Land

- 8 The Council has identified four sites in its ownership that would be suitable for the development of market rent and sale housing by the new company, these sites are detailed fully within the Business Plan.
- 9 The sites are chosen because they are immediately available for development and they are each situated in housing markets where demand for both market housing for sale and rent is buoyant. An assessment of market conditions is contained in the Business Plan.
- 10 The sites are located at:
- Agnew 5, Woodham Drive, Newton Aycliffe (125 units)
 - Cobblers Hall Site N, Newton Aycliffe (approx. 60 units)
 - Former Civic Centre site, Chester-le-Street (approx. 53 units)
 - Oakerside Drive, Peterlee (approx. 65 units)
- 11 The site at Agnew 5, Newton Aycliffe is large enough to be sub-divided into 2 phases. The first phase (56 units) has commenced as a pilot phase prior to moving onto phase two.

The New Company

- 12 Following a brand development exercise and associated research the name of the new company has been chosen to be 'Chapter Homes' this reflects our links to Durham City and to the Cathedral.
- 13 The company will take responsibility for both the development of the new housing and the subsequent management of the market rent housing.
- 14 The business of developing and managing housing for market rent and sale is considered to be commercial activity and thus not an activity which the Council could carry out itself.
- 15 The Localism Act 2011, however, permits local authorities to undertake commercial activities through a separate company as long as:
- i. the company's viability can be proven through a Business Plan and the Plan subsequently approved under section 95 of the Local Government Act 2003 .
 - ii. the authority ensures that they are able to recover the cost of supplying any accommodation, goods, services, staff or other things to the new company. (This is intended to avoid any State Aid implications.)

- 16 The company can either be one as defined by section 1(1) of the Companies Act 2006 (a company limited by shares) or one as defined by Co-operative and Community Benefit Societies and Credit Unions Act 1965.
- 17 A company limited by shares is useful when the primary objective is to make and distribute profits to shareholder(s). In this case the shareholder will be the Council and any profits can be used under the local authority's general power of competence.
- 18 A company defined as a 'not for profit' company or a Community Interest Company (CIC) would restrict the distribution of profit.
- 19 It has therefore been determined that the delivery vehicle is a company limited by shares.
- 20 The housing company is a separate entity. Although it is wholly owned by the Council, it has its own identity and its own Board of Directors.
- 21 The draft Articles of Association form part of the Business Plan and they indicate that the Board will comprise up to 7 Directors.
- 22 It should be noted that unlike the Council, the new company will be liable for VAT, Corporation Tax and Stamp Duty.
- 23 VAT is not charged on the main body of costs i.e. the construction works but there will be VAT liability on consultancy and professional fees, although this is limited to the market rent properties only.
- 24 Corporation tax will be levied on company profits – whether this is a capital return or a revenue stream (after taking into account all operating costs).
- 25 Stamp Duty land tax is charged in direct proportion to the value of any land to be purchased and becomes an absolute cost unless relief is available. Bond Dickinson has advised, however, that relief is available between 'connected companies' and they have confirmed that a local authority and a company which is wholly owned by the local authority can be treated as 'connected companies'.

Affordable Housing

- 26 The new company will not be retaining any properties for affordable housing.
- 27 However, planning requirements of the emerging Durham Local Plan (as informed by the Strategic Housing Market Assessment (SHMA)) will necessitate an appropriate percentage of affordable housing (both affordable rented and low cost home ownership).
- 28 In these circumstances, subject to an appropriate financial viability assessment, the new company will seek to transfer the affordable rented and shared ownership housing to a registered housing provider (RP). Those properties identified for Discount Market Sale will be sold directly on the open market by the new company's marketing team.

State Aid

- 29 State aid rules exist (through EU law) to prevent public sector bodies giving preferential commercial treatment to any company including wholly owned subsidiaries operating in a commercial environment. It is therefore crucial that the relationship between the Council and the new company is put on a proper commercial footing. This entails:
- Transferring land at market value
 - Lending money at appropriate (State Aid compliant) commercial rates
 - Charging support costs (especially from Council officers) at the appropriate rate
 - Getting a reasonable return on any share capital injected into the company.
- 30 Having received appropriate legal advice, these matters have all been taken into account in the development of the Business Plan. The Council is therefore confident that its proposals will not contravene the State Aid rules.

Development of Business Plan

- 31 A Business Plan and associated financial appraisals and sensitivity analyses have been concluded to demonstrate that project development proposals are fully viable and that the company can fulfil its role as a profitable wholly owned subsidiary of the Council.
- 32 The viability assessment at Agnew 5 is based on Gentoo's tendered costs and associated master plan submitted as part of the procurement process. These costs have been subsequently refined to take account of the Council's requested changes in house type mix, specification and overall numbers. The costs have now been agreed and form a part of the contract.
- 33 The construction costs for other sites in the programme have also been subject to the tender process but they have not yet been finalised through further negotiations with the building contractor.
- 34 A separate viability exercise has been completed to assess the profitability of the market rented units. This shows that after taking into account management and maintenance costs and loan repayment requirements, a positive revenue income is achievable.
- 35 Funding for the new company is derived exclusively from the Council's resources and is split between borrowing (70% of overall funding) and share capital (30% of funding).
- 36 The current agreed interest rate for borrowing funds to service the longer term ownership of the market rent units is 7.5%.
- 37 Robust loan agreements have been set up between the Council and Chapter Homes.

Edenfield, Newton Aycliffe (Agnew 5) Update

- 38 Work commenced at Eden Field on the 11 January 2016. The initial focus, in line with the programme of works was to establish the site set up, which includes office and welfare facilities and to lay the temporary roads. This was undertaken and the full extent of the site can now be seen.
- 39 The development is split into two phases, this was to ensure the level of demand was in line with expectations, given the demand continues to increase, it is anticipated that approval for phase two will be made in September 2016, providing a consistent delivery programme and clarity to customer who, even at this stage, are looking to purchase properties on phase two of the development.
- 40 The first properties are now almost completed, these include the two show homes, view home and marketing suite.
- 41 At present there has been 110 enquiries and one property has been sold off plan ahead of the marketing suite being available. This level of interest is ahead of expectations and is testament to the design of the scheme.
- 42 A total of 8 affordable properties are to be sold to Livin as part of the terms of the Section106 legal agreement, this provides much needed affordable housing to those who are unable to access the market.
The programme will continue until October 2018 with a sales rate of 2 properties per month being an average target. The contract has been designed to cater for greater or lower demand and the build rate can be accelerated or decelerated accordingly.

Chester Le Street

- 43 Master planning and site design is being undertaken at Chester Le Street. The overall level of sales and rental demand has been assessed and a draft layout has been prepared.
- 44 The initial appraisal concludes that circa 54 units could be located on the site, to ensure profits are maximised, the design has a greater density than that of Eden Field. The housing market in Chester Le Street is strong, which has been evidenced by our dedicated sales agent.

Market Rental

- 45 Chapter Homes aim to deliver circa 30% of properties available for private rent providing a high standard of accommodation within the Private Sector.
- 46 The following properties have initially been identified as potential for rental purposes. These properties will be let on an unfurnished basis however, actual units available could change based on demand for open market sale units:

Plot No's	Property Size and Type	Rent per Calendar Month
26-29	3 Bed Semi-Detached with Garage	£675
49-51	3 Bed end/mid Terrace, No Garage	£650
56	3 Bed Detached with Garage	£675
67-68	3 Bed Semi-Detached with Garage	£675
79-81	3 Bed end/mid terrace with Garage	£650
90-92	3 Bed end/mid terrace with Garage	£650
103-104	2 Bed Terrace, No Garage	£550
106-107	2 Bed Terrace, no Garage	£550
121-123	3 Bed Terrace with Garage	£650

- 47 The pilot site at Agnew 5 phase 1, Newton Aycliffe will generate up to a maximum of 20 units for market rent available for rent of £550-£650 per month in line with the current Rental Market for properties of this size, type and location.
- 48 The properties available for rent will be let and managed by Chapter Homes via a SLA. As a responsible landlord, Chapter Homes will fulfil a range of management responsibilities. To date there has been 13 expressions of interest in the rental product.

Management Functions

- 49 The housing management function will be delivered by Durham County Council Housing Solutions Service via a secondment arrangement to Chapter Homes. The functions will be delivered to a high standard via robust policies and procedures.
- 50 Processes such as Rent Collection, tenancy matters and property lettings will be required to be effective from the handover date. Housing management staff will be clear of the Chapter Homes culture and deliver a higher performing service to that delivered in a traditional Housing Management Service.

Conclusions

- 51 This report continues to set out the progress being made in establishing a new company to develop and manage a programme of market rent and sale housing.
- 52 The new company now has its own robust Business Plan which evidences the overall viability of the project as well as demonstrating the finance, organisation and governance of the company.

Recommendations

- 53 It is recommended that members note the content of this report and progress made to date by the Project Team.
- 54 That the Economy and Enterprise Overview and Scrutiny Committee receive a further update on the progress of Chapter Homes at a future meeting.

Background Papers:

None

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Appendix 1: Implications

Finance – A robust Business Plan and associated financial appraisals and sensitivity analyses has been established and agreed by the Chapter Homes board.

Staffing – In the short term existing staffing arrangements will be utilised to progress the scheme but ultimately dedicated staff may be required for the project. A dedicated staff resource may need to be recruited once workload(s) are established from the detailed Business Plan, for example a Sales Director. Any staffing costs associated with the scheme will be captured as part of the developing Business Plan.

Risk – The appointment of a preferred building contractor will not expose the Council to significant risk should the Council's market housing proposals not proceed.

A 'Pre Construction Services Agreement' (PCSA) has been entered into between the Council and the selected building contractor partner. The Council will contractually only be required to pay a fair and proportionate amount of fees incurred by the building contractor from appointment until the point at which any such agreement ceases.

The design and build building contract will only be entered into should on-going viability be proven immediately prior to tender acceptance and only once planning permission has been obtained.

Equality and Diversity/Public Sector Equality Duty - n/a

Accommodation – n/a

Crime and Disorder – n/a

Human Rights – n/a

Consultation – The Cabinet Portfolio Holder for Housing and Cabinet Portfolio Holder for Finance are routinely updated on progress of the project via the established Project Board for the scheme.

Procurement – Procurement of a preferred building contractor partner is being pursued via the Homes and Community Agency (HCA) Delivery Partner Panel 2 (DPP2) framework.

Joint delegated authority is sought from Cabinet for the Director of Regeneration and Economic Development and Director of Resources, in consultation with the Portfolio Holder for Housing and Rural Issues and Portfolio Holder for Finance, to appoint a preferred building contractor partner in January 2015.

Disability Issues – n/a

Legal Implications – The Council will need to create a suitable company structure to facilitate development and associated housing management proposals for the market rent units. The Council cannot undertake development itself and it cannot be a landlord on this project.