

## **The provision of services to the private sector by Derby Homes**

### **SUMMARY**

- 1.1 This report seeks the Council's approval for Derby Homes to extend its services into the private sector.
- 1.2 Initially the scheme would build on services already available for leaseholders and other RSLs, offering reliable services at reasonable cost.
- 1.3 Any trading activity that Derby Homes may seek to engage in must relate to activities which the Council can legally do itself, but there must also be some benefit to Derby other than being just an additional provider of a service that is readily available in the private sector.
- 1.4 Subject to any issues raised at the meeting, I support the following recommendations.

### **RECOMMENDATIONS**

- 2.1 That Derby Homes be permitted in principle to provide services to private households in Derby to the extent that provision of such services are within the powers of the Council and do not duplicate existing Council services and that any proposals do not lead to diminution of service provision to the Council and this remains its main business.
- 2.2 That whole contracts for a value of over £250,000 require Cabinet approval, those between £250,000 and £100,000 will require the approval of the Lead Member for Housing and Social Inclusion, and those under £100,000, for the total contract, will be subject to prior written agreement by the Corporate Director of Resources and Housing. Contracts for areas of business that would be contracted individually with the public would be assessed on estimated turnover with approval consistent with the limits as above.
- 2.3 That each contract has an agreed length e.g two or five years, with a clear end date and that the value of the contract in 2.2 above will be the value over the whole contract's life.

- 2.4 That Derby Homes maintain a separate account for each contract within their accounts clarifying in particular taxation issues, along with a business plan for each activity with clear financial targets to be met, to the satisfaction of the Council, and that this be entirely at Derby Homes' risk and expense, with an exit strategy for any business area that fails to meet such targets.
- 2.5 To amend Derby Homes Memorandum of Association as necessary to permit the Company to offer the provision of services to the private sector within the administrative area of Derby City Council.

<b>REASON FOR RECOMMENDATIONS</b>
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- 3.1 Derby Homes Board agreed on 28 April 2005 to develop a scheme to extend its services to private households in Derby. This followed a Council Cabinet decision of 30 November 2004 agreeing a report of the Community Regeneration Commission on Derby Homes' Business Strategy that accepted that Derby Homes needed increased flexibility to seek new business, with certain restrictions.



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### **SUPPORTING INFORMATION**

#### **1. Overview**

##### **1.1 Derby Homes has several reasons for proposing that it be allowed to work in the private sector ...**

- It wishes to support the aims of the Council to meet housing needs by managing properties in the private sector and linking them into the Council's choice based system and so meeting the needs of applicants for rehousing or those who are homeless requiring temporary accommodation. It can also do this by developing new properties for renting.
- Its core service and focus is council housing management and maintenance. In developing new services, Derby Homes will be able to offer similar new services to tenants and leaseholders. For example, carrying out small-scale repairs to what are tenants repairing liabilities and carrying out repairs and gas servicing for leaseholders.
- Any new maintenance work will be placed with existing contractors and discussions have been held with main contractors, such as Commercial Services Department and Vinshires, who are supportive of these initiatives.
- It has now completed its major decent homes programme, which has improved the quality of life of council tenants through home improvements. It now wishes to develop and contribute to the community of Derby and together with the Council, it is exploring the possibility of new build and regeneration schemes. The offering of services in the private sector is part of the organisation's wish to develop the range of its activities.
- Its fee is linked to the number of houses it manages. Right To Buy continues to remove about 150 properties a year from the Council stock and so this will reduce Derby Homes fee by approximately £100,000 a year from 2006-7 onwards. Whilst Derby Homes is downsizing and economising to reflect these trends, it wishes at the same time to make full use of its assets, such as local offices, enquiry centre and staff expertise. The management of services to the private sector is an activity that it has the capacity to undertake and so supplement its fee income. This increased activity will also help to maintain economies of scale.

- Its Board has members with business experience and who are keen for Derby Homes to extend its services into a new markets. Their experience will support this initiative.
- It is aware of the Derby property market and has carried out market research into business opportunities to develop new services and enter new markets. This market research has been used to develop the proposals in this report.
- To date it has developed new services such as consultancy services provided to new ALMOs, and extended its management to over 300 housing association properties in Derby. These have contributed to neighbourhood regeneration in some of the more deprived communities in Derby. At the same time the services provided, have been of benefit to these landlords, who have gained from Derby Homes' skills, accessible service, and local knowledge. This will be one of the strengths of its marketing position.

## 2. **Proposed new service areas**

2.1 It is proposed to focus initially on a menu of housing management and maintenance services, which reflect Derby Homes existing services and experience. This menu will be:

- whole property management, as already provided to two housing associations in the City, to be provided to private sector organisations, landlords and private householders
- lettings services, in partnership with Homefinder, to be provided to private sector organisations and landlords
- specific repairs services to be offered in partnership with Derby Homes' contractor partners to private sector organisations, landlords and private householders, leaseholders and, where appropriate, to council tenants
  - out of hours emergency repairs
  - gas and electricity safety checks and servicing
  - gas central heating installation
  - handyman type repairs, such as replacement internal doors, repair/replace door locks and handles.

2.2 Further services could follow if these initial services are shown to work effectively. The target market will be:

- large private landlord and organisations owning 20 - 200+ properties
- small private landlords with 1 - 20 properties
- private householders interested in having smaller scale maintenance and improvement work carried out to a good quality standard
- council leaseholders who have responsibility for internal decoration, repairs and servicing of gas and electricity
- council tenants who have responsibility for decoration, small scale repairs and non-fair wear and tear repairs.

- 2.3 The main benefits the service will provide to new target customers will be the same as for all existing customers:
- guaranteed high quality service through ISO9001 accredited procedures and IIP trained staff
  - 24 hour service response
  - accountable services through Derby Homes complaints and accountability processes

for private landlords:

- strong links to Council services such as grants and housing benefits
- strong links to the Police and support services to tackle anti social behaviour
- internet Homefinder process in partnership with the Council.

### **3. Market research**

- 3.1 The main findings of recent market research carried out by PCP market research consultants, were that there was reasonable levels of interest and willingness to pay from existing council tenants, right to buy/leaseholders, owner occupiers and private landlords for new services of:

- home decorating and maintenance, including emergency out of hours repairs
- anti crime measures such as watch patrols, security lighting and CCTV
- children services such as crèche, play clubs and after school clubs.

- 3.2 At the same time the survey found a high level of concern from tenants that Derby Homes should concentrate on maintenance and repairs services rather than new services. This is an issue that may be addressed, by ensuring that any new services do not reduce existing resources and services provided to council tenants.

### **4. Potential market for these proposals**

- 4.1 The market research found that these proposals have potential to be successful because they are innovative and will attract customers from the private sector in Derby. The recent market research carried out has shown there is a demand for these services.

- There are 81,100 privately owned properties in Derby, with an estimated 9,400 rented out to private tenants.
- Approximately 1,000 of the rented properties are owned by 40 larger landlords and the rest are owned by 2,000 small landlords who own an average of three properties.
- All properties require maintaining. The supply of skilled labour in the construction and maintenance sector is restricted, and inflation in the maintenance industry has been increasing at three times the normal rate. Recent bad publicity has increased the public awareness of 'cowboy operators' in the house repairs sector. The small landlord typically carries out house repairs by DIY.
- Derby Homes can gain a competitive advantage by building on its strong links with the Council, to provide a publicly accountable service of guaranteed quality.

- Maintenance work out of hours is an area of activity that customers find hard to access.
- Health and safety work such as gas maintenance are services that are attractive to customers because they build on our good reputation.

## 5. **Working with the Council to regenerate the private sector**

5.1 There is a market for whole property management. In particular there are opportunities that Derby Homes feels it is well placed to develop

- The Council has an objective to regenerate the private rented sector in Derby. In particular the Council now has new powers to require poor landlords to improve the management of their properties. The Council can take over the management of those properties that do not respond to these threats. Derby Homes feel well placed to manage such properties on the Council's behalf.
- There are a number of private sector organisations interested in owning rented housing in Derby, who will also be interested in having Derby Homes as their management agent. Discussions have been held with Assetrust Limited who is keen to work with Derby Homes as their management agent.

5.2 There are a variety of competitors in this market ranging from Housing Associations, private landlords, letting agencies and large and small repair and maintenance organisations.

## 6. **The main sources of business risk**

6.1 As the owner of Derby Homes, Derby City Council, and its main customers, the tenants of Derby City Council, may:

- see the need for Derby Homes to concentrate on services to existing council tenants
- see any proposals to extend Derby Homes work into the private sector as too much risk.

6.2 There will be upfront costs of setting up this work, which will not be covered in the first years. Derby Homes must make a surplus or break even across the whole venture or this could be seen to be cross subsidising and paying for these services from rents paid by council tenants. This will require Derby Homes to set aside funding from within its own resources to allow for the predicted losses in the early years plus a contingency amount to allow for the prediction being subject to optimism bias as often occurs at the start up of a new venture. Such funds will need to be agreed with the Council as part of a business plan for each planned activity, and set aside for that purpose until that element of the business is established. This will mean that such funds cannot be used in the meantime on other objectives of Derby Homes.

6.3 There will be the economic risks associated with any trading venture that could result in a loss making operation. This could be the result of insufficient demand, charges being insufficient to cover costs, bad debts and the like.

6.4 Private tenancies are different legal entities to council tenancies and staff will need to be trained in these issues. Staff, who currently devote 100% of their time on council housing issues, may not cope with these changes, and Derby Homes may need to appoint specialist staff.

6.5 Entering into contracts to provide works and services to third parties will expose Derby Homes to greater liability in the form of potential claims for negligence and disputes. It will be important that Derby Homes has in place appropriate liability insurance to meet potential claims.

## **7. The main source where Derby Homes feels that it offers strengths**

7.1 Derby Homes makes the case that its strengths are based on the lead from its Board of 15 members. Derby Homes has successfully managed 14,000 council properties since 2002. Its reputation is well established with a nationally recognised 3 star assessment by the Government's Audit Commission. This can be marketed, together with the close working relationship with the Council that can give reassurance of quality and accountability.

7.2 The senior managers in Derby Homes have an average of 10 years service in Derby housing. All are qualified in their professions of housing management, maintenance and accountancy.

7.3 Derby Homes' 330 staff are well trained and Derby Homes has Investor in People status which reflects the strength of its culture of continuous development. They are based in local offices across the City and able to respond to the need for home visits and inspections. All its staff have mobile phones and access to ICT to ensure they can operate effectively.

7.4 Derby Homes has its headquarters in the city centre, where it has its enquiry centre to respond to phone calls 8.00am to 8.00 pm, five days a week. It has an emergency maintenance service that can respond to repairs 24 hours a day. It has three community watch patrols every evening that are able to visit estates and anti social behaviour complaints, and support tenants and landlords where there are issues.

## **8. Summary**

8.1 In summary, there are many risks associated with allowing Derby Homes to expand its business into new areas, especially the legal and financial ones set out in the relevant considerations sections below.

8.2 Derby Homes' core business remains and must always remain the delivery of high quality services to Derby City Council tenants.

8.3 There is pressure on Derby Homes to expand its business into new areas. Where there is a realistic chance that such business can operate on a self financing or better basis, and that such an operation would have wider benefits for Derby, as well as no detrimental effect on tenants, then the benefits may well outweigh the risks. In such cases, the Council would be able to consider a proposal from Derby Homes to expand its business into a specific area, backed by a business plan for that area.

- 8.4 In order to assure the Council that business ideas have been thought through, it is intended to require each area of business to be subject to a process of business planning to include a critical review of the market evidence and the risk being undertaken by Derby Homes, as detailed in the recommendations.

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**Background papers:** Derby Homes Board 28 April 2005 – The provision of maintenance services to the private sector. Derby Homes Resources Committee 30 June 2005 – Extending Derby Homes Services into the Private Sector. Council Cabinet 30.11.2004 – Derby Homes Business Strategy.

**Appendices:** Appendix 1 – Implications



<b>IMPLICATIONS</b>
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**Financial**

- 1.1 External Audit have been consulted about the potential for a cross-subsidy, and have confirmed that they are happy with proposed arrangements. Items may only be credited or debited to the HRA that comply with the ring-fence provisions in the Local Government and Housing Act 1989.
- 1.2 The Council expects any trading activity to be maintained as a separate sub account for management purposes, around the principles outlined in this report, and to be supervised according to the delegated authority shown in the recommendations at 2.2. Any taxation – for instance corporation tax - and/or VAT issues will need to be clarified as part of the approval process and are undertaken entirely at Derby Homes' risk and expense.
- 1.3 There are clearly additional risks being undertaken in moving into an area of work in competition with the local private sector. While the market research indicates a potential interest from around 10,000 homes, this will be conditional on the price set by Derby Homes for the services offered. There will therefore not be any material surplus from this activity for at least the first few years, possibly more. Losses in the early years will have to be covered by Derby Homes' own funds. Derby Homes will therefore have to set aside specific funding to cover the initial losses expected within their business plan. There may also be a need to set aside further funds within Derby Homes' accounts to allow for the potential additional risk undertaken. There remains a risk to the Council insofar as these funds prove inadequate to meet any potential losses, and as the owner of the business, any surplus or deficit achieved by Derby Homes is part of the Council's group resources. It will therefore be necessary to agree an amount to be set aside within Derby Homes' reserves to allow a reasonable contingency against such a risk.
- 1.4 Each individual area of work will need authorisation from the Council, as set out above in recommendation 2.2, following a detailed plan for its operation, along with a plan to monitor and an exit strategy for any failure to meet expectations.

**Legal**

- 2.1 The Derby Homes Management Agreement already requires the Council's written consent to undertake work for third parties.
- 2.2 Derby Homes Memorandum of Association already allows it to provide services in the private sector within Derby to a certain extent. For instance where this is contributing to regeneration and development of an area as defined in the Housing Grants Construction and Regeneration Act 1996 or involves advice and assistance to Council leaseholders or the provision or management of housing for letting. Any wider provision of services to the private sector will require amendment of the Memorandum. Such amendment will need specific ODPM consent as the original setting up of Derby Homes was approved by ODPM under Section 27 of the Housing Act 1985

- 2.3 There is also a firmly held view that ALMOs, such as Derby Homes, are only able to engage in commercial trading to the extent that their local authority is able to exercise trading powers such as under Section 95 of the Local Government Act 2003. The view being taken is that to allow any wider trading activity by ALMOs would circumvent that provision and the conditions imposed in the related trading order.
- 2.4 The Section 95 power allows the Council to trade commercially in its 'ordinary functions' but only through a separate company. The trading activities of Derby Homes must therefore relate to things which the Council can do itself. For these purposed functions also include the well-being power in the Local Government Act 2000 although that means there must be some benefit to Derby other than being just an additional provider of a service that is readily available in the private sector.
- 2.5 The Section 95 trading power is not available if the local authority has a poor or weak CPA and this would restrict the ALMO likewise.
- 2.6 The Council at this moment in time still needs to pay due regard to Derby Homes entering into any contracts beyond 31 March 2007, when its current agreement with the Council ends, although agreement in principle for a further five years has been agreed by Cabinet.
- 2.7 The proposed contracts will expose Derby Homes to additional risks and liabilities and it is important that they are established and managed on a sound and viable financial basis. Claims and liabilities arising from contracts such as these could potentially detract from the management of the Council's own properties and, in a worst case scenario, threaten the continued existence of Derby Homes. In connection with the Section 95 trading power ODPM has issued formal guidance which covers some of these areas. Regard must be had to the ODPM guidance.
- 2.8 Recent EU case law on procurement has emphasised the importance of ensuring that as a wholly owned company of the Council, the primary role of Derby Homes is the carrying out of housing management functions for the Council. If that role is diluted to any significant extent that could require the current management contract to be subjected to a full public procurement process rather than directly negotiated as at present. The extent of private sector work will therefore need to remain marginal to the overall business or the main management contract would then need to be subjected to public procurement rules.
- 2.9 As a body wholly owned by the Council and set up for public sector purposes, there is a risk of challenge under competition law or the state aid rules. It is important that these commercial activities are kept distinct from public sector activities so as to meet any potential claim that public sector finance is being used to subsidise a private sector activity and which could have the effect of distorting competition in the market. For example, Derby Homes receives many support services from the Council and to the extent that they support the commercial venture then we must ensure that they are not being provided at a subsidised level, that Derby Homes are paying the full cost of those services and those costs are being fully taken into account in setting charges for the commercial venture.

## Personnel

- 3.1 Derby Homes feel that it will be important to measure staff time dedicated to this work, and a time measurement system is being developed.
- 3.2 One additional post within Derby Homes will be required to manage the process of developing these ideas, working closely with the Chief Executive and Directors. The costs of this post will have to be borne by the trading activity accounts.

## Equalities impact

- 4.1 Derby Homes see this initiative as an opportunity to promote local training and employment opportunities for all areas of work.
- 4.2 They also report that in the private housing sector there is a higher proportion of potential customers from BME communities than on our estates. Maintenance services would be available to all, but we will need to carefully consider how these services are marketed and delivered, to ensure that we both reach and meet the needs of all potential customers. Staff and contractors will need to be sensitive to the needs of BME customers of Derby Homes. We will also monitor rates of take up and satisfaction among all sectors of the community.

## Corporate priorities

- 5.1 The proposal comes under the Council's Objectives of **job opportunities strong and positive neighbourhoods protecting and supporting people shops, commercial and leisure activities integrated, cost effective services.**