



Housing Private Finance Initiative Project: Outline Business Case

RECOMMENDATIONS

- 1.1 To submit the Outline Business Case – OBC – for the Council’s Housing Private Finance Initiative – PFI – Project, to the Office of the Deputy Prime Minister – ODPM.
- 1.2 To consider a report on the outcomes of that submission at a future meeting of Council Cabinet.
- 1.3 To authorise officers to proceed with the development of the Project during the period between submission and the final response from ODPM.
- 1.4 To confirm that the Council’s expected total contribution to this scheme is expected to be around £935,000, funded from the existing housing capital programme.

REASON FOR RECOMMENDATIONS

- 2.1 The Project Board approved the OBC for the Housing PFI Project – the Project - its meeting on 20 April 2005.
- 2.2 The ODPM has made it clear that the OBC must be submitted by the end of April 2005 if the Project is to be considered for approval in the current bidding round.
- 2.3 Approval of the OBC will trigger the next stages of the Project, involving the need for renewed commitment on the part of the Council to agree the resources necessary to implement those stages.
- 2.4 In order to keep the Project Plan and Timetable on track, development work must continue in order to make sure that the next stages can be implemented as soon as ODPM approval is given.

SUPPORTING INFORMATION

- 3.1 The Project will provide:
 - a minimum of 175 affordable rented homes built/refurbished to Decent Homes standards across the city
 - management and maintenance of the homes for twenty five years by a Registered Social Landlord – RSL
 - Council-nominated tenancies

- financial penalties for poor performance by the Preferred Bidder
- a form of safeguard for tenants at the end of the 25 years
- homes in the ownership of the RSL at the end of 25 years.

- 3.2 The OBC is based on the Council's proposals to contract with a private sector partner to achieve the delivery of a minimum of 175 new affordable rented homes. Outside the core PFI, we may explore including a small number of affordable shared ownership properties, properties for outright sale, and a number of refurbished homes. Should it prove unworkable or inappropriate to include these mixed tenure arrangements, these will be considered within the context of the Project but outside its primary scope. The new and refurbished affordable rented homes will be provided by the PFI Provider to agreed output specification standards. These homes will be let to Council nominees with a Registered Social Landlord – RSL – as landlord, and subsequently managed and maintained to agreed standards.
- 3.3 Approval of the OBC has the effect of confirming the provisional allocation of PFI credits to the Project – currently requested at some £17.2m. The ODPM has made it clear that for approval to be given within the current bidding round, the OBC must be submitted to ODPM by the end of April, if the Project is to be delivered within the envisaged time frame.
- 3.4 The approval process involves submission to the ODPM by the end of April in order to allow sufficient time for consideration by ODPM and Partnerships UK – PUK – and time for any subsequent discussions between those organisations and the Council to amend the OBC before consideration and final approval by the governments Project Review Group – PRG – at its meeting on 16 August 2005.
- 3.5 Although this period of some three and a half months may seem excessive, it provides the opportunity for the Council to maximise the robustness of the OBC, and thereby the likelihood of final approval by PRG. In addition, this period will allow the Project Team to develop the procedures and documentation needed for those stages of the Project following PRG approval, in order that those stages can be implemented without delay.
- 3.6 The Expression of Interest – EoI – for this scheme, submitted in December 2003, included a proposed commitment from the Council of £935,000. It is proposed that this be formally adopted as the contribution to the Project, comprising set up fees and a cash contribution to the Project. The current capital programme has a total of £835,000 spread over a number of years from 2004/05 to 2007/08 and beyond that currently total £835,000. There is therefore a need for a virement of £100,000 within the existing Council Capital Programme from the Housing Facilitation Fund to the PFI Project.

OTHER OPTIONS CONSIDERED

4. The options considered are set out in section 5 of Appendix 2 to this report.

For more information contact:	Mike Melluish Tel 255533 e-mail: mike.melluish@derby.gov.uk
Background papers:	None
List of appendices:	Appendix 1 – Implications Appendix 2 – Summary of the Outline Business Case – OBC Appendix 3 – Confidential report

IMPLICATIONS

Financial

- 1.1 The cost to the Council of this scheme is anticipated to be £935,000. This cost represents an element for one-off project management and other development costs of up to £750k, together with a capital contribution of around £185k to improve the revenue affordability of the Project. The benefit of this cash injection will be spread over a number of years and funded from the existing Housing Capital Programme. £750k is the ODPM estimate of expected development costs. The Council expects that the Project can be implemented at a lower cost. However, a report will be presented to the Cabinet detailing the expected development costs once approval has been given for the project to proceed.
- 1.2 In addition to this, the Council will be making available, through the use of Section 106 agreements, land at below market cost levels to the successful partner. This is a significant factor in making the Project more affordable than it would otherwise be. This is at no direct cost to the Council, being negotiated with developers as part of the planning process.
- 1.3 The Project as currently drafted has a PFI credit requirement of around £17.2m. This is a significant increase from the EoI figure of £4.4m and is mainly explained by reference to:
- increases in the cost of land and construction
 - increased number of dwellings from 150 to a minimum of 175
 - reduction in the value realised at the end of the contract, known as the residual value or RV. This reduction follows discussion with ODPM and RSLs and it is this issue that has markedly increased the net cost of the Project in terms of PFI credits.
- 1.4 The OBC is cautious in its land strategy, which assumes at this point that land sufficient to provide only 35 units will be available at the cheaper Section 106 rate. It is hoped that more sites will become available over the next few months. Should this happen, the Project would have additional funds available which could be deployed to increase the units available or to increase the length of the contract. At present, such sites are not guaranteed and it would be too great a risk to include any more than is currently proposed.
- 1.5 The stock will remain with the Provider at the end of the contract period, and that the intention is to negotiate a longer term deal for the tenants beyond that period, funded by an overage agreement.
- 1.6 The sites currently under consideration are referred to in section 8 of Appendix 2, and in Appendix 3 to this report for consideration in the private part of the Cabinet meeting.

Legal

- 2.1 Approval of the OBC by PRG will allow the Council to seek expressions of interest in the Project from potential bidders through the Official Journal of the European Union – OJEU Notice.
- 2.2 In addition, we will need to undertake some preparatory work on the legal elements of the ITN, in particular the Project Agreement, in advance of PRG approval in mid-August.
- 2.3 The Project Agreement developed by the ODPM and the 4Ps includes, at Appendix 1D to the Agreement, the required drafting to regulate the Home Ownership Protocol – Right to Buy.

Personnel

3. None arising directly.

Equalities impact

- 4.1 The main thrust of the OBC is to increase the availability and quality of affordable housing across the city to those in need.
- 4.2 Issues of access to, and use by disabled people will form part of the Council's specification for the new homes.

Corporate objectives and priorities

- 5.1 The Project falls within the Council's objectives of **a shared commitment to regenerating our communities, healthy, safe and independent communities, and a diverse, attractive and healthy environment.**
- 5.2 The Project will further the priority of **improving customer service through a customer-focused culture, using new technology and investing in our buildings.**

Derby City Council Housing PFI Project Summary of the Outline Business Case – OBC

- 1 Derby City Council is seeking to use PFI, for non-Housing Revenue Account housing provision and improvement. This proposal has therefore been developed to meet its objectives to:
 - provide additional affordable housing
 - provide secure well managed housing
 - create sustainable and mixed communities
 - accelerate efforts to address non-decency in the private sector
 - tackle blight from empty homes
 - generate employment.
- 2 The Council intends to contract with a private sector partner to achieve the delivery of a minimum of 175 new affordable rented homes, which may include a small number of affordable shared ownership properties and properties for outright sale, and a number of refurbished homes.
- 3 The new and refurbished affordable rented homes will be provided by the PFI Provider to agreed output specification standards. These homes will be let to Council nominees with a Registered Social Landlord – RSL – as landlord, and subsequently managed and maintained to agreed standards.
- 4 The Council's existing non-HRA housing PFI Project has been extremely successful and has returned 150 empty properties back into use as well as providing much needed affordable rented homes. With the recent completion of this programme, the Council considers it imperative to pursue additional programmes which will maximise the number of new affordable homes being delivered in Derby. The Council is also experiencing increased demand for affordable housing owing to a number of social and economic factors such as increase in house prices, family breakdown, inward migration of asylum seekers/refugees and low incomes. The Council's Housing Register at February 2005 identifies 8,986 households in need waiting for suitable properties, of which 22% have been waiting for suitable accommodation for more than two years.
- 5 The Council has considered the following delivery mechanisms for the Project:
 - do nothing
 - delivery through Derby Homes
 - delivery through Housing Grant to RSL
 - private sector leasing
 - PFI.

- 5.1 The Council has discounted the 'do nothing' option, as the need for the new homes is clear. This option would neglect its responsibilities towards households in housing need, leaving them to live in unsatisfactory accommodation, with detriment to their health, life-chances and general well-being.
- 5.2 Derby Homes is the Council's Arms Length Management Organisation – ALMO, currently responsible for managing and maintaining the Council's HRA stock in accordance with the Council's Business Plan. While Derby Homes are fully capable of undertaking the procurement and future management of the stock required, there is currently no financially viable mechanism through which this could be achieved.
- 5.3 Local Authority Social Housing Grant – LASHG – is the 'traditional' way of increasing the provision of affordable homes. It uses grant, from either the Housing Corporation or the Council, to constrain rents to affordable levels. The Housing Corporation's clearly stated priority for this Region is to focus the development of affordable homes on the Milton Keynes/South Midlands area. Consequently, while some Housing Corporation Social Housing Grant – SHG – is available to RSLs providing affordable housing within the city, this is limited and already earmarked.
- 5.4 Without grant aid, RSLs might enter into short term leasing arrangements with private sector landlords in order to provide temporary accommodation. Experience of short term leasing in other areas suggests that the quality of the properties is likely to be poor. Additionally, without grant aid, the rents would of necessity be at or around market level, creating a poverty trap for those households in housing need. This would be contrary to the Council's and the Government's policies of promoting economic activity on the part of those able to undertake it, and supporting households into employment.
- 5.5 The Council already has experience of using PFI to provide affordable housing, having entered into a 30-year contract with Home Housing Group in 2000 to provide 150 social rented homes through acquisition. This contract is operating satisfactorily from both the Council's and the RSL's perspectives, and is providing well-managed homes to the Council's nominees, and assisting with inner city regeneration in accordance with the project objectives.
- 5.6 Initial soft market testing has indicated that even with the more rigorous financial regime now in place for such schemes, bringing with it the need for the Provider to take residual value risk, there is some appetite for this approach. In addition, the assessment of Value for Money – VfM – and affordability, indicate that PFI provides VfM against the Public Sector Comparator – PSC – and supported by the level of PFI credits as proposed in the OBC, a PFI Project would be affordable to the Council.

- 6 The Council's experience of its existing Housing PFI scheme, financial assessments and soft market testing with RSLs has confirmed that, for procurement to proceed quickly and efficiently, it will need to have 'site certainty' at or around issue of the Invitation to Negotiate – ITN. The Council has considered in detail the possible sources of sites:
 - land secured through Section 106 - S106 - 'planning gain' negotiations
 - land brought forward by the contracting RSL or developer
 - land for housing held by the Council.
- 7 The Council's overall vision for the Project is for new/refurbished homes to be provided in those parts of the city experiencing the highest levels of aspirational housing need, and where traditionally there have been low levels of social housing provision. The Council has no sites in such areas available for the Project, and soft market testing with RSLs and developers/house builders indicates that, while a few have some land holdings in Derby, most do not. In practice, therefore, Project developments in such areas may be restricted to Section 106 sites.
- 8 The Council's Project Team has spent a considerable amount of time exploring the availability and characteristics of appropriate sites, and has now agreed a prioritised list of six sites to underpin the development and implementation of the Project. The sites have been prioritised in a way broadly consistent with the vision underpinning the Project and, as such, reflect the strategy the Council will adopt in delivering the new homes. That strategy will seek to protect the concept of affordable housing in areas experiencing the highest levels of aspirational need. But, should any insurmountable issues arise as the sites are considered in priority order, the overriding priority will be the provision of new homes, regardless of area.
- 9 With the six prioritised sites as the starting point, the Preferred Bidder may be expected to acquire one or more sites sufficient to provide the balance of new homes proposed, should any deficiencies arise within the six identified.
- 10 This possibility was raised with potential bidders at the Bidders Open Day held on 17 March 2005 and, depending on the progress made with the sites concerned, will be reiterated as part of the Invitation to Submit Outline Proposals – ISOP – process, with a view to 'site certainty' being clear within the ITN documentation.
- 11 The exact number of affordable homes to be provided has yet to be finalised but, as reflected elsewhere in the OBC, will be in the region of 175 upwards. The exact balance between tenures will be for negotiation between the Council and the Preferred Bidder, but we envisage a mix of rented, together with shared equity and market sale homes – which should contribute to offsetting costs – will form a characteristic of the Project.

- 12 The main features of the financial parameters of the Project are set out at Appendix 1.
- 13 The general principle to be followed is that the Council will expect high standards of design, layout and landscaping for all new affordable housing schemes developed. The objective is to provide a balanced and mixed scheme with no noticeable difference in the quality of the residential environment between the private market housing and the affordable element. The design and materials used for the affordable housing units should be characteristic of the remainder of the development, so that they are visually indistinguishable from their private counterparts.
- 14 The Council will expect that the affordable properties delivered will be able to accommodate the number of people set out below, unless there are constraints on the overall proposed development. In these instances, the number of persons that individual properties will be able to accommodate will need to be agreed on a site by site basis.
- 1 bed flats, 2 people
 - 2 bed flats, 4 people
 - 2 bed houses, 4 people
 - 3 bed houses, 5 people
 - 4 bed houses, 7/8 people.

Size	1B 2P flats	2B 4P flats	2B 4P houses	3B 5P houses	4B 7/8P houses	Total
Social rented	20	30	40	65	20	175

- 15 The Council will expect that the standards of management of the properties, access and tenants rights will as a minimum match the current standards that apply to housing associations funded under the Housing Corporation's Approved Development Programme. We will therefore be looking, among other things, for:
- a housing management service that is provided by a housing association;
 - equality of outcome for residents;
 - careful risk management;
 - support for the creation of long-term and sustainable communities
 - well-managed housing that:
 - helps vulnerable residents to maintain their tenancies
 - ensures equality of access and service to minorities
 - experience and competence in social housing management including:
 - nominations agreement
 - tenancy and property management
 - an equal opportunities framework

- assistance to the Council in their duty towards the homeless, and people in housing need
 - an appropriate relationship with local stakeholders, such as the Council.
- 16 The Council will aim to develop a Payment and Performance Mechanism that:
- encourages the contractor to meet the Output Specification in full, with financial penalties where this is not achieved
 - is not unduly onerous, avoiding unnecessary and costly performance standards
 - encourages the development of partnership working over the contract term.
- 17 The Provider will be paid the Unitary Charge for the service provided that the full Output Specification is met and that service standards do not fall below target levels. Deductions will be made from the Unitary Charge where either of the conditions is not met.
- 18 Operating within the framework set out in the Council's Constitution, the Project Board is responsible on behalf of the Council for the oversight and strategic direction of the Project. Membership of the Board is:

Councillor Philip Hickson	Derby City Council Cabinet Member for Performance Management, Economic Development and Housing - Chair
Mark Menzies	Assistant Director, Housing and Advice Services - Vice Chair
Paul Dransfield	Director of Finance
Sue Glithero	Director of Policy
David Enticott	Head of Technical Finance
Ian Fullagar	Housing Strategy and Performance Manager
John Brittain	Co-opted member

- 19 The Council has established an experienced and representative Project Team, with its forward programme of meetings forming an integral part of the Plan and Timetable. Membership of the Team is as follows:

Mike Melliush	PFI Programme Manager
Rachael Wright	PFI Programme Support Officer
Karen Cadman	PFI Admin Support
Mark Menzies	Assistant Director, Housing and Advice Services
Ian Fullagar	Housing Strategy and Performance Management
Martin Laidler	Housing Development Manager
Graham Moody	External Adviser
Phil Helm	Group Accountant
Peter Morris	Group Accountant
Manisha Patel	Senior Accountant
David Enticott	Head of Technical Finance
Stuart Leslie	Chief Legal Officer
Jim Olford	Chief Valuer
Rosie Heath	Senior Planning Officer

- 20 The ITN will include a draft Project Agreement and Direct Agreement. The Project Agreement will set out the risk that the Council wishes to transfer to the Private Sector and the risks it is prepared to retain and/or share. The Project Agreement will be based upon the model contract within the Housing PFI Procurement Pack, and will also incorporate the most recent Standardisation of PFI Contracts – SOPC – terms issued by the HM Treasury and the latest 4Ps guidance. The Council expects to sign a Project Agreement, which closely mirrors 4Ps guidance, and is totally compliant with SOPC.
- 21 The Council will amend the draft Project Agreement and Direct Agreement that it issues as part of the ITN to accord with any further guidance issued by the ODPM, HM Treasury or the 4Ps. In particular, the Council will reserve the right, in the ITN, or subsequently, to amend the Project Agreement and, if necessary, the Direct Agreement to take account of any changes that are required as a result of the publication of revisions to SOPC drafting.