



Cabinet
10 November 2014

**Report from the Director of
Regeneration and Growth**

For Action

Wards affected:
Barnhill, Wembley Central
Brondesbury Park
Willesden, Kenton, Stonebridge

Housing PFI Project Agreement Revisions

1.0 Summary

- 1.1 As a result of a number of external factors the Council's Housing Private Finance Initiative (PFI) project currently faces considerable financial challenges and a projected deficit which falls on the Local Authority.
- 1.2 This report proposes a number of contractual revisions to provide the Council with flexibility in order to improve the financial performance of the project and substantially reduce the prospective deficit. These have been arrived at following a period of negotiation with the Council's PFI contract partner, Brent Co-Efficient (BCE) and following consultation with the Homes and Communities Agency (HCA) the Department for Communities and Local Government (DCLG).

2.0 Recommendations

Cabinet is asked to:

- 2.1 Note and approve the proposed revisions to the Project Agreement (and related documents) as set out in paragraphs 4.1 to 4.15 of this report and to delegate agreement of the final terms of revision to the Project Agreement (and related documents) contract to the Strategic Director for Regeneration and Growth in consultation with the Chief Finance Officer and the Borough Solicitor.

- 2.2 Delegate authority to the Strategic Director for Regeneration and Growth, in consultation with the Chief Finance Officer and the Borough Solicitor, to agree the variation to the PFI Project Agreement and all other related documents, in order to enable the contract revisions to be properly documented.
- 2.4 Authorise the Borough Solicitor, or authorised delegate on her behalf, to execute all of the legal agreements, contracts and other documents on behalf of the council and such other legal agreements and documentation which may be necessary to give full effect to the variation to the PFI Project Agreement, subject to her receiving confirmation of continuing credit approval from the Department for Communities and Local Government, through the Homes and Communities Agency (HCA) or, executing such contracts and other documentation with a pre-condition that they shall only come into full effect upon the issuing of such PFI credit approval by the HCA/DCLG.
- 2.5 Agree that the Chief Finance Officer can issue, on behalf of the council, such certificate or certificates under the Local Government (Contracts) Act 1997 to:
- a. Brent Co-Efficient in respect of the Deed of Amendment (or such other document) to give effect to the variations to the PFI Project Agreement;
 - b. Brent Co-Efficient's funders in respect of any the Direct Agreement Amendment Deed (or such other document) to give effect to the variations to the Direct Agreement entered into between the council, such the funders and Brent Co-Efficient; and
 - c. Hyde Housing Association and the Brent Co-Efficient's funders in respect of a the Residual Value Amendment Deed (or such other document) to give effect to the revised Residual Value Deed to be entered into between the council, Hyde Housing Association and the funders.
- 2.6 Agree that the Chief Finance Officer will be fully indemnified by the council in the event of any claim against him arising from the provision of any Certificate he may issue in accordance with recommendations/decisions in 2.5 above.

3.0 Background

- 3.1 The PFI contract was entered into between the Council and Brent Coefficient Limited (BCE), a subsidiary of Hyde Housing Group (Hyde), on 19 December 2008 for Phase 1 which was extended in July 2010 to include Phase 2 and the contract ends on 18 December 2028. The project provided for the construction between 2010 and 2012 of 364 units of accommodation by BCE, and an additional 20 units of residential care accommodation which are owned by the Council. All units have been constructed and the project is in its service operational phase.
- 3.2 The 364 units are intended to be available for use as Temporary Accommodation by Brent in order to assist in meeting its statutory interim duty to provide temporary accommodation to homeless households. The contract

also requires that a proportion of these units convert to Social Rented properties over the course of the contract: a minimum of 72 units in 2013 rising to 98 units in 2023.

- 3.3 At the end of the contract a minimum of 158 of the units are to be provided thereafter by Hyde as social rented housing, with this number potentially being increased if the overall value of the units (reflecting market values at that time) exceeds the debt repayment due to the project lenders.
- 3.4 As a result of the welfare reforms introduced by Government, in particular the housing benefit subsidy limitations for temporary accommodation, rental income to fund the required payments to BCE has not risen as assumed in the contractual financial model and over the remaining course of the contract is projected to fall substantially short. The contract had assumed that the housing benefit rates for temporary accommodation would rise by RPI+0.5 % per annum over the course of the contract. In practice, since 2010, housing benefit rates for temporary accommodation have been frozen and on the introduction of Universal Credit expected in 2018, are expected to be re-based to a lower level and to then rise by CPI only. (CPI inflation has on average been 0.7% lower than RPI inflation over the last twenty years.)
- 3.5 As a result under the current contract the Council is expected to incur an annual and increasing deficit over the remaining contract term. Financial modelling, based upon reasonable forward assumptions, indicates this deficit will cumulatively rise to c.£17.4m (before adding interest costs arising from servicing this deficit) by the end of the contract in 2028. The actual financial performance of the contract will depend on a number of variables that can only be reasonably estimated in advance. These include CPI and RPI inflation levels, uprating of Local Housing Allowance (Housing Benefit) rates and housing market rental inflation.
- 3.6 In order to remedy the position negotiations have been undertaken with BCE and Hyde over recent months on revisions to the contract that have the potential to optimise the project's financial performance and minimise the prospective deficit. The proposed revisions, set out below, have been agreed in principle by these parties, and the HCA and DCLG have indicated their support, which is required for any contractual changes. If approved by Cabinet the required contractual changes will be legally drafted with a revised contract expected to be entered into in December 2014.
- 3.7 The proposed contractual revisions have been designed to provide the Council with the flexibility to respond to the developing financial position over the remainder of the contract term, rather than prescribe a specific solution that may then prove ineffective as underlying assumptions are overtaken by changing circumstances.
- 3.8 The revisions will provide the Council with flexibility over the way in which the 364 units are used and the corresponding rents that can appropriately be charged. It will allow the Council to make judgements each year about the appropriate mix of housing benefit-supported temporary accommodation,

intermediate and Affordable Rented units, within certain limits, in order to optimise financial performance while contributing to meeting housing need.

- 3.9 The most significant change is the introduction of a contingency to utilise the PFI units to provide discounted market rent, or intermediate rent housing. This product is recognised by the HCA and GLA as being part of the mix of affordable housing products and aligns with the objectives of the project.
- 3.10 It is recognised, however, that if units are let at intermediate rents they will need to be used to provide temporary accommodation or otherwise meet housing needs in a more targeted way, primarily for those in employment, and will not be available to meet the broad range of temporary accommodation needs they currently do. This may have a resulting impact on other temporary accommodation pressures and costs.
- 3.11 The Council will be able to determine the way in which the units (to a maximum of one third of the units in any year) are used on an annual basis. It is proposed that annual decision on this be reserved to the Cabinet, and be included in the annual Housing Supply and Demand report, and be informed by a full understanding of the financial and other implications of this.
- 3.12 The existing commitment to provide a minimum of 158 affordable homes from the end of the contract is maintained and the number realised may be increased through the proposed changes.
- 3.13 On the basis of current assumptions the proposed revisions would reduce the final deficit to c.£5.6 and £6.2m by 2028. The majority of this deficit arises over the latter part of the contract and current assumptions about the future position during that period are necessarily uncertain. Over the next five years, by end 2019/20, the cumulative deficit would be reduced from c.£3.6m to c.£1.7m.
- 3.14 The PFI units are currently occupied by households to whom the Council owes an interim duty to provide temporary accommodation. These households are eligible to bid under the Council Allocation scheme for an affordable social housing property.
- 3.15 Where units are converted to Affordable Rent existing residents will if appropriate under the Allocation scheme be offered fixed-term Affordable Rent tenancies of their existing properties or they will be provided with alternative temporary accommodation. If units are in the future let at intermediate rents an assessment will be made of whether this is affordable to the existing household and if not alternative temporary accommodation will be provided.

4. Contractual Revisions

- 4.1 The proposed revisions to the terms of the project agreement have been agreed in principle by BCE and Hyde, They have also been considered by the DCLG who have indicated that they are supportive in principle of the proposed changes. The proposed revisions and their implications, are set out below:

Revision 1

- 4.2 It is proposed to remove the requirement to convert a specified number of units during the contract term from Temporary Accommodation use to Social Rented units. If the conversions were to proceed they would worsen the financial position.
- 4.3 The DCLG is currently considering this revision alongside the alternative of revising the requirement to convert 92 units during the contract term from Temporary Accommodation use to Social Rented units to a requirement to convert a minimum of 72 units from Temporary Accommodation to Affordable Rent equivalent units no later than 2015 and for a period of no less than 5 years. This would limit the adverse impact of conversions and provide the council with flexibility to partially recover the position later by converting the units back, on expiry of fixed-term tenancies, to temporary accommodation or intermediate rent if the financial position required it. Decision by the DCLG between these alternatives will be provided in November and these alternatives are reflected in the financial implications set out in this report.

Revision 2

- 4.4 To provide the option for the Temporary Accommodation units to be let at 'intermediate rents', i.e. at rents of up to 80% of prevailing market rents.
- 4.5 Intermediate rented housing is a form of affordable housing (and one promoted through the HCA and GLA) but differs from Affordable Rented housing in that rents are not limited by Local Housing Allowance rates but may be charged at up to 80% of market rents.
- 4.6 This change would increase rental income to the project and reduce the projected deficit. The deployment of the units at intermediate rents would represent a more targeted approach to the use of these units to meet housing need than is the current position. The units would be used to meet the needs of those to whom the Council owes a duty to provide temporary accommodation, other homeless households or those in need of housing assistance. Affordability will be a fundamental consideration. The units will be targeted primarily at those in employment and either not in receipt or in partial receipt of housing benefit and for whom rents at up to 80% of market rent would be affordable. In nominating a household to these units the council would continue to ensure that the rent could be afforded as is required under the current Project Agreement.
- 4.7 The Council has around 3,300 households in temporary accommodation. As a result in part of the welfare reforms the proportion in employment has risen significantly and approximately 20% of households are currently in paid work. The size of the Council's temporary accommodation provision could enable the Council to use the PFI units in a differentiated way, to meet the temporary accommodation needs of those in employment for whom the rents are affordable and to meet the housing needs of others in need who approach the council for assistance.

- 4.8 Intermediate rents would be introduced gradually over an extended period in order to minimise any impact on households currently housed in these units who are not in employment at the relevant time and who are not able to afford the intermediate rents. There would be early engagement with these households to assess their circumstances and to discuss their options. If discounted market rents are not affordable the household would be accommodated in other temporary accommodation available to the Council in accordance with the Council's statutory duty, or where appropriate through the offer of a social housing unit or a suitable private rented sector discharge as appropriate to their circumstances.

Revision 3

- 4.9 For conversion to be to Affordable Rent rather than Social Rent, both during the contract period (if any) and at the end of the contract.
- 4.10 Government policy is now to support Affordable Rent provision as the main form of affordable tenure, replacing social rent. In accord with this it is proposed that the existing requirement to provide a minimum number of Social Rented units at contract-end is replaced with an equivalent requirement to provide Affordable Rent units instead. The effect of this change will be positive in that the value of these units will be higher and this will potentially enable a larger number of the PFI units to be converted to affordable housing at the end of the contract.

Revision 4

- 4.11 For rent collection overage provisions to be amended to maximise income to the project.
- 4.12 In order to maximise rental income available to the Council to meet its payment obligations it is also proposed to amend the existing provisions in relation to rent collection overage (and underage). Currently, if target rent collection levels are exceeded (or not reached) 50% of the excess is retained (or shortfall, paid) by Hyde. In practice rent collection levels are significantly higher than the target levels. It is therefore proposed to reduce the degree of Hyde's share in any upside (or downside) to 10% within the existing range in order to maximise income to the project and to reduce the deficit.

Revision 5

- 4.13 At the end of the contract for the Council to be able to recover up to £2m of any deficit from 50% of the increase in value that results from the 158 affordable units being secured as Affordable Rented instead of Social Rented units.
- 4.14 This provision provides the Council with a limited amount of contingency if a deficit remains at the end of the contract term. This facility depends upon the overall value of the 364 units being sufficient to meet BCE's debt repayment

requirement at that time. Modelling indicates a reasonable likelihood that this will be achieved.

4.15 In summary, the proposed revisions to the contract agreement have been designed as far as possible to accord with the existing objectives of the project to provide accommodation to meet housing need and provide a permanent legacy of affordable housing while assisting in recovering the project's financial position and reducing the projected deficit to which the council is exposed. They have the potential, together, to put the project back on a more sustainable financial footing whilst maintaining the rationale and purpose of the project.

5.0 Financial Implications

5.1 The current contract is not affordable to the Council. As a result of previous changes and reasonable projections of future policy in relation to housing benefit subsidy levels for temporary accommodation it is projected that a deficit of c.17.4m will result by contract end.

5.2 The proposed revisions will significantly reduce the Council's deficit but they are unlikely to eliminate it entirely. It is projected that through these revisions the deficit at contract-end could be reduced to between £7.6 and £8.2m (in out-turn cash terms).

5.3 If, as projected, a deficit accumulates by contract end the Council may be able to recover up to £2m of this deficit from 50% of the increase in value that results from the 158 affordable units being secured as Affordable Rented instead of Social Rented units. This increase in value is estimated at c.£5m but the actual figure will be determined at the end of the contract and depend on then prevailing Social and Affordable Rent levels. This provision reduces the eventual projected deficit to between £5.6m and £7.2m.

5.4 The projected impact of the proposed revisions are summarised cumulatively in the table below.

Proposed Revision (All figures are out-turn)	Financial Impact on baseline (£m)	Projected Deficit at end-contract (£m)
Current baseline position	-	17.4
Revised rent collection provisions	1.0	16.4
No conversions to Social Rent during contract	4.4	12.0
*Deployment at Intermediate Rents (changeover between 2015-18)	4.4	7.6
(OR Min. 72 conversions to Affordable Rent in 2015 and deployment of remainder at Intermediate Rents between	(0.6)	(8.2)

Proposed Revision (All figures are out-turn)	Financial Impact on baseline (£m)	Projected Deficit at end-contract (£m)
2015-18)		
Deficit recovery from Affordable Rent value increase at contract-end	2.0	5.6 (OR 6.2)

*For the purposes of this financial illustration it has been assumed that the units would be moved to intermediate rents over a three-year period from 2015-18.

- 5.5 The Temporary Accommodation earmarked reserve (£5.7m at March 2014) will be reclassified so that it can also be used to fund any shortfall on this PFI contract. The Council will be required to meet any deficit in-year and this will be reflected in its annual budgets. The Council's Medium-term Financial Strategy will also take account of the extent of the proposed deficit that needs to be funded over that term.

6.0 Legal Implications

- 6.1 The effect of a Contract Act Certificate under the Local Government (Contracts) Act 1997 is to provide comfort to the other party to the contract (and its funders) that even if the contract is declared void or ultra vires then a certificate issued under the Local Government (Contracts) Act 1997 will have the effect of rendering such contract intra vires. It is likely to be necessary for the Council (as is recommended in paragraph 2.6 of the report) that the Chief Finance Officer certify the agreements referred to in paragraph 2.5 of the report. These certificates are given in the Chief Finance Officer's personal capacity and as such it is also recommended that he be indemnified (as he was in respect of the Phase 1 and Phase 2 certificates) for any losses arising as a result of giving such certificates. The Director of Finance at the time has previously signed such Contract Act certificates in respect of the legal documentation when the original Project Agreement for Phase 1 of the PFI project was entered into in December 2008 and when the Phase 2 PFI variation was entered into in July 2010.
- 6.2 When considering the proposed amendments, and in particular the financial implication arising from those changes and also the financial implication to the Council of not agreeing the changes to the Project Agreement and related documents, the Council needs to consider the fiduciary duty which is owed to council tax and ratepayers within the borough which obliges the council, when exercising its functions and thus when considering the recommendations in this report, to make proper arrangements for securing the economic efficient and effective use of the local authority's resources.
- 6.3 The Council has a number of powers which enable it to procure the accommodation and services envisaged within the current PFI contract namely:
- a) Part VII of the Housing Act 1996 ("HA 1996") places various duties on a local housing authority to secure that accommodation is available for persons who are homeless or threatened with homelessness including, (i) section 188 HA

1996 which requires that the local authority shall secure that accommodation is available for a person's occupation if it believes, pending enquiries into the applicant's homelessness application, that the applicant maybe homeless, eligible for assistance and have a priority need and (ii) section 193 HA 1996 where, unless the local authority can refer the applicant to another local housing authority, it shall secure that accommodation is available for occupation by an applicant where it is satisfied that an applicant is homeless, eligible for assistance and has a priority need and is not satisfied that he become homeless intentionally;

- b) Section 21 of the National Assistance Act 1948 provides that a local authority may with the approval of the Secretary of State and to such extent as he may direct, make arrangements for providing residential accommodation to persons aged 18 or over who by reasons of age, illness, disability or any other circumstances are in need of care and attention which is not otherwise available to them;
- c) Section 1 of the Local Government (Contracts) Act 1997 provides that a statutory provision conferring or imposing a function on a local authority confers power on the local authority to enter into a contract with another person for the provision or making available of assets or services, or both, (whether or not together with goods) for the purposes of, or in connection with, the discharge of the function by the local authority .

7.0 Diversity Implications

- 7.1 A full EIA was undertaken in relation to the Council's Tenancy Strategy which was agreed in 2013. This addressed the implications of future social housing provision being at Affordable rather than Social Rents. The policy requires that such Affordable Rents are set at different percentages of market rent for different bed-sizes in order to support their affordability, and this policy will be applied to any PFI units converted to Affordable Rent.
- 7.2 If the PFI units are let at intermediate rents at a future point this will impact on households then accommodated in them, either by increasing the rents payable or in requiring them to move to other temporary accommodation.
- 7.3 An initial Equalities Analysis has been undertaken which includes an action plan. This requires that decision on any future let of the PFI units on Intermediate Rents is supported by an Equality Analysis in order to assess the impact of the proposed change on the households accommodated in the relevant units at that time and on the characteristics of those requiring temporary accommodation generally at that time, with identification and assessment of appropriate measures to mitigate any adverse impacts.

8.0 Staffing/Accommodation Implications (if appropriate)

- 8.1 There are no immediate staffing or accommodation issues arising from this report.

Background Papers

Appendix 1 – Heads of Terms
Appendix 2 – Financial Modelling Results Summary
Appendix 3 – Further Legal Comments - Not for Publication
Appendix 4 – Equalities Analysis

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