



Cabinet
20 January 2016

**Report from the Strategic Director,
Community Well-being**

For Action

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

Housing Tenancy Conversions

1.0 Summary

- 1.1. The Council's Housing Private Finance Initiative (PFI) project provides 364 units of Temporary Accommodation (TA) for homeless households and 20 units of residential care accommodation through contractual arrangements running until 2028. It was originally intended that a rising proportion of the TA units would be converted to Social Rented properties over the course of the contract (temporary to permanent conversions), in order to provide settled accommodation for at least 158 households by the end of the contract.
- 1.2. However, the financial viability of the project has been affected adversely by a number of external factors including the Government's welfare reforms. In particular Housing Benefit subsidy limitations mean that the rental income is less than that required to service the cost of operating the project. In November 2014 Cabinet was advised of a projected £17.4m deficit over the remaining contract term and the Council has made provision of £5.7m to meet part of this deficit, reducing it to £11.7m.
- 1.3. In order to further reduce the shortfall Cabinet agreed to make a number of changes to the PFI contract and the revised agreement was entered into in April 2015. The 158 temporary to permanent conversions will now be to Affordable Rented units instead of Social Rent. This change aligns the project with the Government's preferred tenure type and has a positive financial impact on the value of the homes at the end of the contract.
- 1.4. The contractual changes also provide greater flexibility over the future use of the 364 TA units during the contract period, in order to meet housing need while assisting with deficit reduction by generating increased rental income.

Up to one third of the units can now be converted to either Affordable Rent or Discounted Market Rent (a form of intermediate rent) tenures or back to TA during any year.

- 1.5 The proposal in this report is to convert the maximum allowable 122 TA units to Discounted Market Rent during the current year. Should this be agreed, and assuming that the remaining 242 TA units are also converted to Discounted Market Rent as soon as the contract allows, the projected deficit will be reduced to £3.4m. A sharing arrangement in respect of the increased value of the 158 Affordable Rent units at the end of the contract is expected to further reduce the deficit to £1.4m, which the Council will be required to meet from its resources.
- 1.6 It was always intended to convert a proportion of the PFI homes to different tenancy types in order to provide more settled accommodation for current tenants. The proposal in this report represents an acceleration of this approach and the expectation is that the majority of the 122 households in the first tranche of conversions will transfer from TA to Discounted Market Rent tenancies, remaining in their current homes.
- 1.7 Prior to the offer of a Discounted Market Rent tenancy being made officers will assess the suitability of the proposed offer, including the affordability of the property to the tenant. There are safeguards contained within the PFI contract and homelessness legislation if either the Council's PFI partner or the tenant considers the offer of a Discounted Market Rent tenancy to be unsuitable.
- 1.8 While the offer of more settled accommodation is a positive opportunity for current tenants it is recognised that tenancy conversions may lead to affordability issues emerging over a period of time and the Council may need to use the Discounted Market Rent units to meet housing needs in a more targeted way. However, this challenge is not unique to the PFI project, as a result of the changing affordable housing and social welfare landscape.
- 1.9 Officers will work closely with Hyde colleagues and residents to ensure the implementation process for tenancy conversions is communicated well and completed smoothly.
- 1.10 Some of the households affected by the above proposal will have Protected Characteristics in respect of the Equality Act 2008, as set out in the accompanying Equality Assessment. For some of these households the impact will be positive, for some negative and others broadly neutral. However, the proposal is needed in order to ensure that the Council meets its fiduciary duty, to reduce the projected deficit.

2.0 Recommendations

Cabinet is asked to:

- 2.1 Note that the revised Project Agreement was entered into in April 2015.

- 2.2 Note that the projected financial deficit at the end of the contract, without exercising the option to convert PFI units to alternative tenures, has increased due to the impact of external factors since the last Cabinet report.
- 2.3 Agree to convert up to 122 units of Temporary Accommodation to Discounted Market Rent units, as set out in the report, and to delegate authority to the Strategic Director Community Well-being, in consultation with the Chief Finance Officer and the Chief Legal Officer, to issue to Brent Coefficient Limited a schedule setting out the units to be allocated as Discounted Market Rent units in accordance with the Project Agreement.

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), in December 2008 for Phase 1, which was extended in July 2010 to include Phase 2 and the contract ends in 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 were originally intended to be available for use as Temporary Accommodation (TA) by Brent in order to assist in meeting its statutory interim duty to provide TA to homeless households. The contract originally required that a rising proportion of these units convert to Social Rented properties over the course of the contract and that, from the end of the contract, 158 units be provided thereafter by Hyde as Social Rented housing, with this number potentially being increased if the overall value of the units exceeds the debt repayment due to the project lenders.
- 3.3 In November 2014 Cabinet was advised of a projected deficit over the remaining contract term, arising as a result of the Government's welfare reforms. In particular the Housing Benefit subsidy limitations for TA mean that 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, this is projected to fall substantially short. At the time the Council was expected to incur a cumulative deficit of £17.4m (before adding interest costs arising from servicing this deficit) by the end of the contract in 2028. The Council has made provision of £5.7m to meet part of this deficit, reducing it to £11.7m.
- 3.4 In order to remedy the position Cabinet agreed to make a number of changes to the PFI contract (Project Agreement) that had been negotiated with BCE and Hyde, and which were supported by the Homes and Communities Agency (HCA) and the Department for Communities and Local Government. The revised contract was entered into in April 2015 and the final revisions relevant to this report are summarised below:

Revision 1

- 3.5 The Council is entitled to propose changes to the tenure of up to a maximum of 122 PFI units in any contract year and to allocate each 'converted' unit as either an Affordable Rent equivalent unit or a Discounted Market Rent unit, or to convert it back to TA. This provides the Council with flexibility over the way in which the 364 units are used and the rents that can be charged, in order to optimise the financial performance of the project while contributing to meeting housing need.

Revision 2

- 3.6 The requirement to convert a specified number of units during the contract term from TA use to Social Rented units has been changed. The Council is now required to convert a minimum of 72 units from TA to Affordable Rent equivalent units no later than 2018, for a period of not less than 5 years.
- 3.7 Rents may be charged at up to 80% of local market rents for these units, limited contractually by Local Housing Allowance (LHA) rates. This change accords with government policy to support Affordable Rent as the main form of affordable housing tenure, replacing Social Rent. The scope to convert TA units to Affordable Rent is discussed in section 5, below.

Revision 3

- 3.8 The revised contract provides the option for TA units to be let at Discounted Market Rent i.e. at rents of up to 80% of prevailing market rents, not limited contractually by LHA. Discounted Market Rent is similar to intermediate rent housing, which is a form of affordable housing promoted through the HCA and the Greater London Authority (GLA). The scope to convert TA units to Discounted Market Rent is discussed in section 6, below.

Revision 4

- 3.9 The minimum number of 158 units of TA, which were previously required to be converted to Social Rent at the end of the contract, will now become Affordable Rent equivalent units at contract expiry. The effect of this change should be positive in that the value of these units is expected to be higher than Social Rent units and this should enable a larger number of the PFI units to be converted to affordable housing at the end of the contract.

Revision 5

- 3.10 Brent now retains 90% of the rental income collected by Hyde in excess of contractual target rent collection levels, in order to maximise income to the project and to reduce the deficit. If target rent collection levels are not achieved the Council will be required to meet 90% of the shortfall. In practice actual rent collection levels have been higher than target levels.

Revision 6

- 3.11 At the end of the contract the Council will be able to recover up to £2.0m of any deficit from 50% of the increase in value resulting from the 158 affordable

units being secured as Affordable Rented units instead of Social Rented units. 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.

- 3.12 In summary, the above revisions to the Project Agreement accord, as far as possible, 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.

4.0 Current Financial Position

- 4.1 The current baseline financial position reflects the 72 TA units which are required to be changed to Affordable Rent units by April 2018. Since the November 2014 report the financial viability of these Affordable Rent units has been affected by changes to LHA, which is now expected to increase by 1% annually (rather than 2.5% as assumed in the previous modelling) after a four year freeze from 2016/17. The projected deficit at the end of the contract has increased slightly from £11.7m to £12.6m (after the £5.7m provision), as set out in Appendix 1.

5.0 Temporary Accommodation to Affordable Rent equivalent Conversions

- 5.1 The Council is required to convert a minimum number of 72 units to Affordable Rent by 2018, for not less than five years, and for at least 158 units to become Affordable Rent units at contract expiry (contract revisions 2 and 4). External legal advice confirms that PFI units are currently exempt from the Rent Standard and are anticipated to be excluded from the 1% rent reduction. The financial viability of the Affordable Rent units will, however, be impacted by the LHA freeze and reduced indexation thereafter.
- 5.2 Brent's Tenancy Strategy requires that Affordable Rents are set at different percentages of market rent for different bed-sizes in order to support their affordability. For 1 bedroom properties the PFI contractual position aligns with council policy i.e. Affordable Rents to be set at 80% of market rent, whereas for larger units a lower percentage (70% or 50%) would need to be applied in order to be consistent with the policy. It is, therefore, proposed to prioritise the 1 bedroom units for conversion to Affordable Rent.
- 5.3 While Affordable Rent units will still have an overall positive impact on the financial performance of the project compared to Social Rent properties, there is no incentive in terms of deficit reduction to bring forward the timing of these conversions or to increase the number of units converted to Affordable Rent prior to the end of the contract.
- 5.4 It is not proposed to exercise the contractual TA to Affordable Rent equivalent conversion option at the present time. This position will be reviewed in time for the next cycle of tenancy conversions.

6.0 Temporary Accommodation to Discounted Market Rent Conversions

- 6.1 It was recognised, in the November 2014 Cabinet report, that if units were let at Discounted Market Rents they may need to be used to meet housing needs in a more targeted way, primarily for those in employment. This would involve moving current residents to alternative accommodation.
- 6.2 However, external legal advice confirms that the Discounted Market Rent units would fall within the definition of “Social Housing” and would, therefore, be currently exempt from LHA caps in respect of Housing Benefit. This is positive in that it provides an opportunity to offer more settled accommodation to those current residents of the TA that are in receipt of Housing Benefit and for the Council to discharge its homelessness duty, where applicable. This will reduce the need to move households into alternative accommodation in order to effect the proposed tenure changes.
- 6.3 Households will, however, still be affected by the overall benefit cap (currently £26,000 a year for couples with children or single parents) unless they are exempt from the cap and this will be taken into account in considering the units to convert. Working families are exempt from the cap.
- 6.4 Members may be aware that, in his Autumn Statement, the Chancellor of the Exchequer announced proposals to extend the application of LHA caps to Social Housing. Based on current information this would affect all new tenancies granted after 31 March 2016, with Housing Benefit entitlement changing from 1 April 2018 onwards.
- 6.5 It would be advantageous, both financially and in terms of meeting the objectives of the project, to maximise the number of TA units converted to Discounted Market Rent before 1 April 2016. Early discussions with our PFI partners indicate that BCE/Hyde would be supportive of this approach, which would minimise the need to move households in the future because they are unable to meet the cost of the new rent.
- 6.6 Any properties converted after the above date would still attract Housing Benefit above LHA level until 31 March 2018, after which the caps would apply, unless PFI properties are exempted from the LHA caps. At that point in time an assessment will be made as to whether the rent remains affordable to the existing household and, if not, alternative accommodation will be provided.
- 6.7 However, once any Housing Benefit claimants move on to Universal Credit, the housing element within Universal Credit will be based on the LHA rate. This will be implemented as part of managed migration of existing claims from 2018 to 2021 or sooner if the claimant needs to make a new claim. The proposed conversion of PFI units to Discounted Market Rent Social Housing is, therefore, an appropriate short to medium term strategy to reduce the projected deficit while maximising affordability.
- 6.8 Based on the above assessment it is proposed to convert 122 TA units to Discounted Market Rent as soon as is practicably possible. It is also anticipated that all remaining units (except for the 72 units which must be let at Affordable Rents for five years from April 2018) will be converted to

Discounted Market Rent over the following two years, but this will be for separate approval by Cabinet at future dates.

6.9 It is proposed to prioritise the first 122 properties to be converted to Discounted Market Rent on the following basis (in priority order), prioritising those households that are exempt from or less likely to be affected by the overall benefit cap. This excludes 1 bedroom units as the majority of these are intended to be converted to Affordable Rent from 2018:

- Working households
- Other households exempt from the benefit cap including ASC nominees
- Smaller properties by earliest date of homelessness acceptance

6.10 Assuming that the first 122 conversions can be achieved by 31 March 2016, and further conversions are undertaken in future years as set out in the preceding paragraphs the estimated impact is to reduce the projected deficit at contract expiry by £9.2m to £3.4m (after the £5.7m provision), as set out in Appendix 1. 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.

6.11 The financial modelling is sensitive to the basis for calculating market rent, from which both Affordable and Discounted Market Rents are derived (by applying the 80% factor). The financial outputs summarised in this report are based on market rents taken from GLA rent map data for September 2015, using median rent figures by postcode.

7.0 Supported Housing

7.1 Of the 364 TA units approximately 26 properties are let currently to Adult Social Care (ASC) clients. The PFI accommodation (by virtue of it being purpose-built, and well located for local services and public transport) is suited to ASC clients with low level support needs, who are able and want to live independently in general needs housing.

7.2 Where service users are 'stepping down' from more managed settings, such as supported housing or residential care, there may be flexibility for Housing Benefit to support higher rent levels for the PFI units, in order to assist with deficit reduction. There would be quality of life benefits for clients living more independently and revenue savings arising to the Council from using less costly specialist accommodation.

7.3 Officers will explore the potential to allocate a proportion of Discounted Market Rent units that become vacant in the future to ASC nominees. All nominees are subject to agreement with BCE/Hyde under the terms of the PFI contract.

8.0 Impact on Current Tenants

8.1 The PFI project faces financial challenges, arising from a number of external factors, resulting in a projected deficit. The April 2015 contract changes provide greater flexibility over the future use of the TA units. In considering

the implementation of these changes officers have been mindful of the need to minimise the impact on current residents, while recognising the Council's fiduciary duty to reduce the deficit.

- 8.2 It was always intended to convert a proportion of the PFI homes to different tenancy types in order to provide more settled accommodation for current tenants and for the Council to discharge its homelessness duty accordingly. The proposal in this report represents an acceleration of this approach, which is generally positive. The expectation is that the majority of the 122 households in the first tranche of conversions will transfer from TA to Discounted Market Rent tenancies, remaining in their current homes with no disruption to their education or employment arrangements.
- 8.3 Prior to the offer of a Discounted Market Rent tenancy being made officers will assess the suitability of the proposed offer, including the affordability of the property to the tenant. There are safeguards contained within the PFI contract and homelessness legislation if either BCE or the tenant considers the offer of a Discounted Market Rent tenancy to be unsuitable. The tenant will be able to request a statutory review of any decision that an offer of accommodation is suitable.
- 8.4 If the outcome of the assessment process is that a property is not suitable to be offered as a Discounted Market Rent unit, for example if it is unaffordable to the current tenant, the Council will work with that household to provide alternative accommodation. Ultimately, in the event of a tenant refusing a suitable offer, either of a Discounted Market Rent tenancy or alternative accommodation, they would be required to make their own arrangements for housing.
- 8.5 Discounted Market Rent is similar to intermediate rent housing, which is a form of affordable housing, and households will be offered an Assured Shorthold Tenancy. The starting rents (80% of local market rents) will be broadly similar to the current rents charged for the TA units. However, unlike the TA rents, Discounted Market Rents will increase in line with market rents.
- 8.6 It is recognised that this may, not immediately but over a period of time, lead to affordability issues and the Council may need to use the Discounted Market Rent units to meet housing needs in a more targeted way, primarily for those in employment. This is reflected in the logic of prioritising working families and other households that are exempt from the overall benefit cap in the first tranche of conversions.
- 8.7 However, it is important to note that the impact of changes to the affordable housing and social welfare landscape is not exclusive to the PFI project. The Government's intention is to end lifetime tenancies, with fixed-term tenancies becoming the norm. Changes to the Housing Benefit system, including the implementation of Universal Credit, will have implications for households in a range of project and accommodation types.
- 8.8 Officers will work closely with Hyde colleagues to ensure the implementation process for tenancy conversions is completed smoothly. This will include

clear communications with residents and one to one discussions, where necessary. Residents will have the opportunity to remain in their home while any review or appeal of the suitability of a Discounted Market Rent offer is underway.

9.0 Financial Implications

- 9.1 The revised projected deficit at the end of the contract has increased from an estimated £11.7m to £12.6m. The increase is mainly due to the impact of changes to the Local Housing Allowance (LHA) announced by the Government in 2012 for implementation in 2014/15 onwards, an increase of 1% annually rather than 2.5% assumed in the previous modelling.
- 9.2 To minimise the impact of the deficit, this report proposes to convert 122 TA units, which is the maximum allowed within the contract in any contract year, to Discounted Market Rent by 31 March 2016. It is also anticipated that all remaining units (except for the 72 units which must be let at Affordable Rents for five years from April 2018) will be converted to Discounted Market Rent over the following two years.
- 9.3 This proposal will generate an additional £9.2m income which will reduce the projected deficit to £3.4m. At the end of the contract, the Council will also be able to recover up to £2.0m or 50% of the increase in value resulting from the 158 affordable units being secured as Affordable Rented instead of Social Rented units. It is anticipated that this will further reduce the overall deficit to an estimated £1.4m by 2028.
- 9.4 The Council has previously made provision of £5.7m to meet part of the projected deficit and will be required to meet the estimated balance of £1.4m from its resources as part of the Council's Medium-term Financial Strategy. This projection is dependent on a number of volatile factors including future market rent, rent collection rate and interest rates, a financial risk that should be noted.
- 9.5 The PFI units are currently exempt from the Rent Standard. This provides the Council with the ability to ensure that Discounted Market Rents are indexed in line with changes to local market rents. In the event that actual rent inflation exceeds RPI+0.5%, as assumed in the financial model, this will further contribute to deficit reduction.

10.0 Legal Implications

- 10.1 Under the terms of the revised PFI contract the Council is entitled to allocate a dwelling as either an Affordable Rent Equivalent Dwelling, A Discounted Market Rent Dwelling and/or as Temporary Housing. The Council is only entitled to propose a maximum of 122 changes to tenure in any contract year, which is why the report proposes that 122 dwellings are converted from Temporary Housing to Discounted Market Rent Dwellings.
- 10.2 The revised PFI contract also provides that the Council shall notify the Contractor by 1 December of each year with a schedule of the number of

dwellings to be allocated as Discounted Market Rent Dwellings (amongst other things). This deadline has passed, but it is understood that the Contractor has accepted that the Council can provide this schedule of conversions later than required by the contract.

- 10.3 Dwellings are regarded as "Social Housing" if they fall within the definition of "Social Housing" in the Housing and Regeneration Act 2008. Essentially, for rented dwellings, this requires two tests to be satisfied, namely (i) that the rent is below market rent and (ii) that the property is made available for letting in accordance with rules designed to ensure that it is made available to people whose needs are not adequately served by the commercial housing market.
- 10.4 The Dwellings let under this PFI contract are all let by Hyde Housing Association as landlord. As a Registered Provider, Hyde is bound by the terms of the Rent Standard for all Social Housing. Even if the PFI dwellings are regarded as Social Housing they are, nonetheless, currently exempt from the Rent Standard.
- 10.5 The social housing rent reduction referred to in this report is contained in the Welfare Reform and Work Bill. Although it is not possible to provide absolute legal certainty until the Bill becomes an Act of Parliament and the regulations that underpin it are made available, it is anticipated to exclude from its operation the same properties which are presently exempted from the Rent Standard – so the PFI dwellings should also be exempted from the requirement to reduce rents by 1%.

11.0 Diversity Implications

- 11.1 A full Equalities Impact Assessment 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.
- 11.2 The revised PFI contract provides for all Affordable Rents to be set at 80% of market rent, regardless of unit bed-size. The assumption in this report is that the 72 units to be converted to Affordable Rent will be all one bedroom units, for which the Council's policy rent is 80% of market rent. The policy requirement at 11.1 will, therefore, be met.
- 11.3 Where TA units are converted to Discounted Market Rents this will impact on the current tenants, either by increasing the rents payable over a period of time or, if the rents are considered to be unaffordable, in requiring them to move to other accommodation, which may be permanent or temporary accommodation. Some of these households will have Protected Characteristics in respect of the Equality Act 2008. For some households the impact will be positive, for some negative and others broadly neutral.
- 11.4 There is the potential for households with protected characteristics to be disproportionality affected by these changes as an unintentional consequence

of the way in which units are selected for conversion to Discounted Market Rent. However, with the exception of the 72 units proposed at 11.2 to be converted to Affordable Rent, all remaining units are likely to be converted to Discounted Market Rent over a three year period.

- 11.5 However, this proposal is needed in order to ensure that the Council meets its fiduciary duty in respect of the PFI contract, to reduce the projected deficit. It is important to note that the intention was always to convert a proportion of the TA units to provide more settled accommodation for current tenants. What has changed is the nature of the tenancies to be offered.
- 11.6 Furthermore all current TA tenants are being encouraged to bid for permanent accommodation elsewhere in the Council or housing association stock, with 80% of lettings this year designated for homeless households. This provides a significant opportunity for affected households to bid for alternative accommodation, should they so wish.
- 11.7 An Equality Analysis has been undertaken, which accompanies this report (Appendix 2) and which includes an action plan to obtain more detailed and up to date data on affected households and to mitigate the impact of PFI tenancy conversions on protected characteristic groups.

12.0 Staffing/Accommodation Implications

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

Background Papers

Appendix 1 – Financial Modelling Results Summary

Appendix 2 – Equality Analysis

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