



Cabinet
14 October 2019

Report from the Director of Finance

Financing Purchase of Residential Block by i4B or First Wave Housing

Wards Affected:	Toykington
Key or Non-Key Decision:	Key Decision
Open or Part/Fully Exempt: <small>(If exempt, please highlight relevant paragraph of Part 1, Schedule 12A of 1972 Local Government Act)</small>	Open
No. of Appendices:	None
Background Papers:	None
Contact Officer(s): <small>(Name, Title, Contact Details)</small>	Olga Bennet Head of Finance (Commercial and Projects) 020 8937 3337 Olga.bennet@brent.gov.uk

1.0 Purpose of the Report

- 1.1 This report requests Cabinet approval of equity investment in i4B's existing street purchases programme, as agreed in principle by Cabinet when approving i4B's business plan in February 2019.
- 1.2 i4B or First Wave Housing is intending to purchase a block of 153 key worker accommodation apartments in Wembley Park from Quintain. This paper is seeking approval of the Council to fund this transaction by a mix of loan and equity, subject to the negotiation of some outstanding points as detailed in paragraphs 3.15 and 3.16.
- 1.3 There is also a request for the decision on the mix of the loan amount and equity to be delegated to the Director of Finance.

2.0 Recommendations

- 2.1 Cabinet approves an equity investment in the existing i4B street purchases programme by purchasing i4B shares up to a maximum of £21.8m for the first 300 properties, as agreed in principle by Cabinet in February 2019.
- 2.2 Cabinet agrees for new loan facilities of up to £110.5m to be made available to

i4B and First Wave Housing for phase 2 of the PRS purchase programme, including the potential Quintain block purchase.

- 2.3 Cabinet agrees that drawdowns on the loan facility to finance the potential Quintain block E01 02 purchase would be conditional on the negotiation of points as described in paragraphs 3.15 and 3.16 below.
- 2.4 Cabinet delegates to the Director of Finance, in consultation with the Deputy Leader, authority to determine whether the conditions set out in paragraphs 3.15 and 3.16 below have been discharged.
- 2.5 Cabinet agrees for equity investment of up to £22.1m for phase 2 of the PRS purchase programme, including by purchasing i4B shares up to a maximum of £22.1m.
- 2.6 Cabinet agrees to delegate the precise terms and mix of loan and equity funding for phase 2 of the PRS purchase programme to the Director of Finance, such that the total funding for phase 2 of the PRS purchase programme does not exceed £110.5m.
- 2.7 Cabinet notes the new details of the potential block purchase from Quintain, together with the financial and legal implications.

3.0 Detail

i4B Business Plan

- 3.1 In November 2016 Cabinet agreed to establish a wholly owned investment company, i4B Holdings Limited. This company was set up to own and manage private rented sector properties in order to support the Council's homelessness agenda.
- 3.2 Cabinet approved the i4B Business Plan 2019/20 in February 2019. This included:
 - (i) increasing the budget for PRS Phase 1 from £103.5m to £109m;
 - (ii) changing the PRS Phase 2 budget from £116m to £110.5m;
 - (iii) total agreed funding for i4B remaining the same at £254.5m.
- 3.3 The i4B Board proposed that the proportion of properties in Brent and Greater London increased from the initial business plan. The realignment of funding reflected the higher average property cost within Brent compared to the Home Counties.
- 3.4 This paper requests authority to make this funding available to i4B, with additional flexibility to make some of it available to First Wave Housing (FWH) instead. This is because, as a registered provider of social housing, FWH is able to attract grant funding from the Greater London Authority, for example for key worker housing.

- 3.5 Phase 2 includes the potential purchase of a block to be used as key worker housing.

Key Worker Housing

- 3.6 The current Administration has identified as one of its key policy priorities the provision of key worker accommodation. There is an increasing body of evidence that the cost of living in London is acting as a significant barrier to the recruitment of a variety of professional roles in local government and other public sector employers.
- 3.7 One of the five deliverables of the Borough plan is “a future built for everyone, and an economy fit for all.” One of the aspects of this states “we must ensure more affordable high-quality housing, for over 12,000 households currently in need”.
- 3.8 Through the planning process, the Council has already secured 346 Discount Market Rent (DMR) homes that will be prioritised to key workers at no more than 65% of open market rent (inclusive of service charge).
- 3.9 Alongside these DMR homes, the Council has also agreed for 471 homes let at no more than 80% of market rent (inclusive of service charge) to be delivered via a tenure known as London Housing Bank. These homes will convert back to full Private Market Rent after 7 years of completion. Whilst these rents are higher than the 65% DMR London Housing Bank, homes are scheduled to complete between September 2019 and September 2020.

Wembley Park Block E01 02

- 3.10 In addition, the Council has provisionally secured the Discount Market Sale (DMS) affordable housing product for around 250 homes in Wembley Park. Quintain proposes for 153 of these to be in block E01 02.
- 3.11 The existing Section106 agreement with Quintain enables the Council to exercise options to acquire block E01 02 and let them at intermediate market rate. The block contains a mix of 1 and 2 bedroom apartments (63 x 1 bed and 90 x 2 bed).
- 3.12 Originally, these were intended to be used as Discounted Market Sale homes, that is, for Quintain to sell them on the open market at 70-75% of market value, with the Council retaining the 25-30% equity share. DMS units were negotiated at least in part with the intention to improve the social mix in the Wembley area by providing another form of housing product that might be accessible to those on moderate incomes.

The Council now has three broad options:

1. The Council could purchase the block. Under the S106 agreement, the Council has a right to purchase the block for 70% - 75% of open market value for use as Intermediate Dwellings (i.e. not Social Rented).

Alternatively, the Council could negotiate an offer outside of the mechanism detailed in the S106 agreement.

2. If the Council were to forego its right to purchase the dwellings, it would acquire (for free) 25% - 30% of each dwelling. The Council could not realise this asset until individual owners of the flats chose to purchase the remaining equity (known as 'staircasing out').
3. Agree to vary the S106 agreement and allow Quintain to offer a discounted market rate product which prioritises key workers.

Potential Purchase of Block E01 02

- 3.13 Purchasing the block has the potential to give the Council a higher degree of control over the allocation of these properties to key workers, specifically the ability to prioritise Council employees. Officers are exploring whether this could support the Council to recruit and retain officers in specific roles, for example children's social workers. This would contribute to a long term strategy to attracting and retaining key workers in Brent.
- 3.14 In addition, purchasing the block is a potential investment opportunity for i4B/ First Wave Housing, since the block would be acquired at a discount from the open market value. This would fit into i4B's growth and diversification strategy.
- 3.15 The acquisition is subject to negotiations with Quintain lead by the Operational Director of Property and Assets on behalf of i4B and FWH. Negotiations include the timing of payments to Quintain and potential future financial obligations. The loan drawdown will be executed once these terms are agreed.
- 3.16 It is suggested that i4B/ FWH's drawdown of funds to purchase the Quintain E01 02 block is contingent on the usual due diligence relating to block purchases and providing loans. It is recommended delegated authority is given to the Director of Finance to determine when the due diligence is adequately completed. For example, the Director of Finance's considerations would include:
 - (i) the robustness and affordability of operating assumptions relating to the block; and
 - (ii) the adequacy of protection for i4B/ FWH under different scenarios, including contractual default by Quintain.

4.0 Financial Implications

Financial Implications for the Council

- 4.1 The loan and equity investment detailed in section 2 would be financed by Council borrowing in accordance with its debt management strategy. It is anticipated that the interest rate charged to i4B or First Wave Housing would be set in reference to PWLB rates at the time of i4B/ First Wave Housing drawdowns.

- 4.2 If the Council does not exercise its option to purchase the block, it still acquires (for free) a substantial asset. The 25-30% share represented by the option would become the Council's. Quintain have indicated that this would have a face value of circa £17m.
- 4.3 The Council could not realise this asset until individual owners of the flats chose to purchase the remaining equity. The asset is therefore very illiquid. After a few years this would provide a stream of capital receipts to the Council, the value and timing of which would depend on the assumptions made about how quickly owners would choose to staircase out and the change in property values. Such receipts have already flowed to the Council from similar properties in Wembley Park. These receipts will be used to deliver more affordable homes.
- 4.4 It follows that, if the Council exercised its option to purchase the block through i4B or First Wave Housing, and let it out at intermediate rent, it would significantly delay the opportunity to receive these receipts.
- 4.5 The total cost of the block purchase would therefore be the sum of:
- (i) the payment to be made to Quintain;
 - (ii) other purchase costs such as stamp duty;
 - (iii) other costs incurred as a result of the negotiated terms, for example if early payments are made then i4B/ FWH would incur interest payments on the loan prior to practical completion; and
 - (iv) foregone future receipts that the Council would have received (circa £17m)
- 4.6 As lender and investor in i4B and First Wave Housing, the Council is also ultimately affected by financial implications for i4B/ First Wave Housing. These include being exposed to potential financial benefits and risks associated with owning and operating the building. For example, the Council would be impacted by
- (i) any future financial obligations entered into as part of the Heads of Terms with Quintain;
 - (ii) operational profits or losses associated with managing the block;
 - (iii) the block's value increasing or decreasing over time (capital gains or losses).
- 4.7 Special arrangements exist in Local Government to extend the definition of capital expenditure, primarily to recognise that certain expenditure by the Council will have wider, lasting public benefit than is reflected in current accounting rules. This ruling applies to certain loans made to third parties and the proposed loan to i4B/ First Wave Housing for the block purchase is captured by these regulations.
- 4.8 Given this, the 2019-20 capital pipeline/programme and revenue budgets include provision for both the acquisition (initial loan) as well as the resulting MRP and associated capital financing costs over the duration of the scheme.

5.0 Legal Implications

- 5.1 The Recommendations propose equity investment and loans to i4B/FWH. There are potential State Aid implications for both, although with an equity investment there is a potential for the whole equity investment to be regarded as State Aid rather than just the difference between the interest rate applied for a loan and the market rate. The market economy operator principle does provide an exemption to both loan and equity investment falling foul of State Aid and this requires that any investment is made on a similar basis to that a private operator acting under market conditions and in similar circumstances would make. Cabinet is asked to delegate authority to the Director of Finance to determine the precise terms and mix of loan and equity funding and in considering such matters the Director of Finance should have regard to the need to guard against such loan or investment constituting unlawful State Aid.
- 5.2 It is recommended to agree a loan facility for i4B and FWH for phase 2 of the PRS purchase programme, including the potential Quintain block purchase. Business plans for both companies agreed by Cabinet in February 2019 mentioned the wish for closer alignment of both companies. However, i4B and FWH remain separate companies and if it is determined to pursue the purchase of the Quintain block through FWH, Members will need to be satisfied that such purchase falls within the business plan for FWH.

6.0 Equality Implications

- 6.1 The proposals in this report have been subject to screening and officers believe that there are no adverse equality implications.

7.0 Human Resources/Property Implications (if appropriate)

- 7.1 No additional resources are required to deliver this scheme.

10.0 Proposed Consultation with Ward Members and Stakeholders

- 10.1 This paper will be circulated to all ward members.

Report sign off:

MINESH PATEL
Director of Finance