

QUERCUS HOUSING - INCREASING THE DELIVERY OF AFFORDABLE HOUSING IN THE SEVENOAKS DISTRICT

Finance & Investment Advisory Committee - 4 November 2021

Report of: Sarah Robson, Deputy Chief Executive, Chief Officer People & Places

Status: For Decision

Also considered by:

- Cabinet - 11 November 2021
- Council - 16 November 2021
- Housing & Health Advisory Committee - 20 October 2021

Key Decision: No

Executive Summary: Reliable access to decent housing is fundamental to improving life chances and reducing dependency on wider social support systems. In Sevenoaks District there is a shortfall between the demand for and supply of new affordable homes. This report sets out a proposal to amend the Quercus Housing Business Plan to enable prudential borrowing to take forward the purchase of Abbey Court in West Kingsdown in order to increase the supply of new affordable homes delivered by Quercus Housing, the Council's affordable housing trading company.

This report supports the Key Aim of: the Council's Housing and Health Strategy.

Portfolio Holder: Cllr. Kevin Maskell

Contact Officer(s): Sarah Robson, Ext 7129

Recommendation to Housing and Health Advisory Committee, and Finance & Investment Advisory Committee:

That comments on recommendations (a) to (d) below are passed to Cabinet.

Recommendation to Cabinet:

That recommendations (a) to (d) below are recommended to Council.

Recommendation to Council:

- a) To approve a revised 2021/22 Capital Programme (Appendix C) that excludes the Property Investment Strategy scheme which will give SDC access to Public Works Loan Board (PWLB) borrowing to enable this scheme to progress.
- b) To approve the draw down of a loan from prudential borrowing (for example, through PWLB) for up to £1,050,000, which it then loans to Quercus Housing (as the Trading company) in order to progress the capital purchase and refurbishment of Abbey Court (West Kingsdown), subject to due diligence, to support the delivery of affordable housing in the district.
- c) To approve for the terms of the loan to be determined at the point of draw down by the Deputy Chief Executive, Chief Officer - Finance and Trading.

Introduction and Background

- 1 Sevenoaks District Council is taking a pro-active approach to ensure and influence the supply of new homes in a sustainable way that protects the character of and improves the fabric and public realm of the district.
- 2 However, there remains a shortfall between the demand and supply of new affordable homes in Sevenoaks District, both in absolute terms as viability issues result in below policy delivery, and in specific specialist tenures especially in the provision of affordable rental housing, older people's housing, specialist accessible housing and social rented housing for large families.
- 3 The lack of affordable housing has contributed to the rise of homelessness and, as the Council has a statutory responsibility to assist homeless residents, this has created a greater financial burden upon the budget.
- 4 Delivery of affordable homes historically has been a planning led approach with the reliance on Planning Obligations, also known as Section 106 (s106) agreements to deliver affordable homes in the district.
- 5 The Council recognises the importance of Rural Exception Sites in providing affordable housing to areas that need them and continues to promote the opportunities they will bring in providing affordable housing to rural areas.
- 6 The Council is already looking at how it can use its own land assets more effectively to deliver additional housing to assist the Council in satisfying the housing demand caused by the failure of the market to deliver in these areas, whilst at the same time retaining asset value and providing greater control of what is built.
- 7 The high cost of land in the District makes it difficult for our Registered Provider (RP) partners to acquire land for building new affordable housing

themselves. To make the most cost effective use of s106 commuted sums, the Council has subsidised new developments that could not proceed without some assistance, for example, we are currently working with West Kent Housing Association to subsidise the delivery of 7 new supported housing flats for rough sleepers, using commuted sums of £200,000 at Vine Court Road. Supporting this proposal through the use of s106 commuted sums is an appropriate use of the funding, particularly as this type of supported housing would not otherwise be delivered by our RP partners.

- 8 Intervening in the housing market through direct delivery also offers opportunities to deliver a wider housing offer in areas and tenures that reduces demand elsewhere on the Council's service provision.
- 9 In 2019, the Council established Quercus Housing, a Local Authority Trading Company, to support the delivery of affordable homes in the district.
- 10 £6 million in s106 commuted sums for affordable housing was allocated to support the delivery of the Quercus Housing Business Plan. The funding has been provided by developers where affordable housing could not be delivered onsite. The funding is used to deliver affordable housing in the district.
- 11 In 2019, Quercus Housing purchased Gladedale House in Westerham. 5 units conform to the new 'genuinely affordable' definition in that they are within the Local Housing Allowance rate and the remaining 4 units are 'intermediate rent', in that they are 80% of market rent and offered to local essential workers. Five of the units have been leased to Quercus 7 for market rent. The total cost of the project was £3.771m, with £2.481m funded from S106 affordable housing contributions and the remainder of the cost, paid for by Quercus 7, for its leasehold properties.
- 12 Quercus Housing has recently completed the final contract stages with a developer at 11-13 High Street, Swanley to purchase the freehold for 15 flats for £3,600,000. The property comprises 12 two bed flats and 3 one bed flats. The development has provided a good opportunity to invest the s106 monies available, assisting affordable housing requirements in a single block investment in an area which is popular with renters.
- 13 Quercus Housing is currently in the negotiation stage to purchase the former nursing home Abbey Court, West Kingsdown, which could be converted into self-contained units at affordable rent, which would be split between Local Housing Allowance and 80% of market rent.
- 14 The Council's Housing team would use Abbey Court to provide suitable move on accommodation at affordable rent for households currently placed in temporary accommodation, but would develop its Local Lettings Plan in consultation with local councillors and the parish council to support residents with a local connection and housing need in West Kingsdown.
- 15 The property is subject to a covenant in terms of its use. The building requires refurbishment and alterations to provide the right mix of shared

accommodation. In planning terms, the use would be a house in multiple occupation (HMO) requiring a change of use.

- 16 An offer of £700,000 has been submitted by Quercus Housing to the agent. Quercus Housing's offer was not the highest, but is considered the most deliverable. There is restrictive covenant for release by separate negotiation to allow for use as an HMO. Solicitors for the Rochester Diocese has agreed a payment of £35,000, plus fees, for a modification to be made to the covenant on the property, which would allow a HMO on the site. Solicitors have been instructed to undertake due diligence in order to properly evaluate the investment property, understand the property's potential and any risks involved in the purchase.
- 17 However, the estimated costs of refurbishment is close to £875,000, plus contingency and fees, which may bring the figure closer to over £1 million. There is currently insufficient s106 funding to support the refurbishment of the property.
- 18 Quercus Housing is attempting to find a way forward and in a realistic timeframe given there is financing, planning and refurbishment required. A financial appraisal has been completed (Appendix B). The appraisal includes an outline of cash-flow, including debt (interest and capital repayment) based on projected income and expenditure from Abbey Court. It should be noted that the floor plans have been updated to offer 19 self-contained units at affordable rent, including a mix of within Local Housing Allowance and 80% of market rent, which suggest a rental income of approximately £150,000 per annum in Year 1 if fully occupied, with an annual rent increase.
- 19 Although Quercus Housing makes a small operating profit, the acquisition of 11-13 High Street, Swanley will be instrumental in supporting any future loan, as it will be fully income producing within 6 months of practical completion. Based on attached cash-flow, both Gladedale House and 11-13 High Street, would need to produce identifiable net positive cash-flow to cover around £60,000 per annum of interest and capital repayments for a £1,050,000 loan over a 20 year period. The effect of different interest rates and loan periods would need to be tested.
- 20 It should be noted that provision has been made for service charges in the appraisal in order to mitigate any risk if a tenant does not pay and the debt is not recovered. However, service charges should not impact the cash flow of the Quercus Housing, as the tenant will be responsible for service charge payments, which will be collected by Leaders Letting and Estate Agents, who also manage the tenant rent accounts.
- 21 At present, Quercus Housing's business model is reliant on receiving s106 commuted sums for affordable housing, which impacts its ongoing financial scope to provide an annual programme of affordable housing delivery in line with its Business Plan.

- 22 At its meeting on 16 September 2021, the Quercus Housing Guarantor Board approved amendments to its Business Plan to enable the company to undertake prudential borrowing via the Council. Any borrowing would be subject to the usual approval mechanisms, including the review of the financial compliance aspects and scheme viability in consultation with the Quercus Housing Guarantor Board.
- 23 Most local authorities opt to borrow from the PWLB at below market rates and then on-lend to their subsidiary companies. There is an exemption from State Aid compliance for non-commercial purposes, thus in the case of Quercus Housing, below market rate lending is possible.
- 24 For example, the Council would draw down a loan from the PWLB, which it then loans to Quercus Housing (as the Trading company) in order to build/establish new affordable housing for rent. Quercus Housing is then responsible for providing this housing to the customers/tenants and recovering rents and service charges. The loan is then repaid to the Council with interest.
- 25 The Quercus Housing Guarantor Board expressed its support to progress Abbey Court and seek alternative funding or borrowing avenues, at its meeting on 8 July 2021, agreeing that although Abbey Court is not straightforward, it does present a rare opportunity to meet a hard to fulfil housing need in the district.

Prudential Borrowing

- 26 The Prudential Borrowing Capital Finance system was introduced in 2004, allowing councils to borrow without Government consent. A council can invest in "any purpose relevant to its functions under any enactment, or for the purposes of the prudent management of its financial affairs". There are Government and CIPFA guidelines which councils must follow and they must adopt an investment strategy on an annual basis. Councils are also required to set aside a minimum revenue provision against any investment. As local authority borrowing contributes to the public sector debt, its overall level of borrowing and future constraints on such have to be considered.
- 27 Note that Prudential Borrowing Guidance is currently being updated to include additional restrictions but it is not anticipated that the changes will impact this scheme.
- 28 Therefore in principle the Council can use prudential borrowing to support affordable housing development. The great advantage is that the Council is able to borrow from Public Works Loans Board (PWLB) at very competitive rates. For the Council, affordable housing can represent a safe return on investment and it can take security over the properties acquired or developed. The Council has to consider the amount it can lend and what bodies it can lend to within the context of its investment strategy and prudential limits.

Other Options Considered and/or Rejected

- 29 The Council could chose not to approve amendments to the Business Plan to include the ability to undertake prudential borrowing. However, this would significantly restrict Quercus Housing’s ability to deliver affordable housing in the district and limit its reliance on s106.

Key Implications

Resource (non financial)

None. Utilising existing staff resources.

Financial

New Public Works Loan Board (PWLB) guidance issued in August 2021 specifically mentions that it can be used for housing schemes including on-lending to a wholly owned housing company. The guidance goes on to state: “Housing can include all spending on delivering new homes, maintaining or improving existing homes, and purchasing built homes to deliver housing services. This is the case irrespective of the financial arrangements of the housing project or housing delivery. However, the government expects that the location and value of any housing expenditure be appropriate to meet the local authority’s housing needs.”

However, due to the ‘Property Investment Strategy’ scheme currently being included in the capital programme, which is classed as an ‘invest for yield’ scheme, the Council is unable to borrow from the PWLB for any scheme. Therefore, to enable access to PWLB funding, the 2021/22 capital programme will have to be revised by removing the ‘Property Investment Strategy’ scheme.

At present, the financial appraisal (Appendix B) assumes Council borrowing at 2%. However, Finance will advise on the PWLB annuity rate over an agreed period in due course.

Finance will advise whether Minimum Revenue Provision may need to be considered to help facilitate the loan.

This borrowing would then be forwarded to Quercus Housing who would repay the Council from the rental income received.

Legal Implications and Risk Assessment Statement

The Quercus Housing Business Plan has been updated and approved by Guarantor Board. The company’s Risk Management Strategy and Assessment will continue to be reviewed and updated to incorporate any future risks and mitigation of borrowing. Detailed budget monitoring is completed on a monthly basis where all variances are explained.

Having successfully negotiated the partial release of the Covenant, Abbey Court provides a future property asset to the Council.

Equality Assessment

The decisions recommended through this paper have a remote or low relevance to the substance of the Equality Act. There is no perceived impact on end users.

Conclusion

Abbey Court presents a rare opportunity to meet a hard to fulfil housing need and presents as a great opportunity for Quercus Housing to deliver additional affordable rented accommodation in the district. The footprint of Abbey Court is substantial and with the agreed release of the Covenant, would provide the Council with a future asset.

The revised 2021/22 Capital Programme excludes the Property Investment Strategy scheme which will give SDC access to Public Loan Works Board (PWLB) borrowing to enable this scheme to progress.

To approve the draw- down of a loan from prudential borrowing (for example, through PWLB) for up to £1,050,000, which it then loans to Quercus Housing (as the Trading company) in order to progress the capital purchase and refurbishment of Abbey Court (West Kingsdown), subject to due diligence, to support the delivery of affordable housing in the district.

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Appendices

Appendix A - Abbey Court - draft floor plan

Appendix B - Abbey Court - financial appraisal - EXEMPT

Appendix C - Revised 2021/22 Capital Programme

Background paper

None