

FLINTSHIRE COUNTY COUNCIL

REPORT TO: **CABINET**

DATE: **TUESDAY, 16 JULY 2013**

REPORT BY: **DIRECTOR OF COMMUNITY SERVICES**

SUBJECT: **DELIVERING HOUSING DEVELOPMENT IN
FLINTSHIRE WITHOUT THE REQUIREMENT FOR
PUBLIC GRANT SUBSIDY**

1.00 PURPOSE OF REPORT

- 1.01 To outline to Cabinet the range of optional financial models available to the Council to facilitate housing development in Flintshire without the requirement for public grant subsidy.
- 1.02 To assist Cabinet to make informed choices when considering housing development opportunities across Flintshire to meet the needs identified within the agreed Local Housing Strategy.

2.00 BACKGROUND

- 2.01 A contraction in the amount of capital funding available, alongside the fall of house prices has required the Council to rethink its approach to housing development. This is as a direct consequence of the considerable shift in the economic environment in which housing delivery operates. Previously viable schemes are now unviable, volume house builders are taking a much more cautious approach to delivery, Social Housing Grant availability has been reduced and the traditional routes to deliver housing and affordable housing are fragile.
- 2.02 The Council needs to ensure that the right types of housing offer in the right locations are delivered to meet the needs of existing households and to attract economically active households into Flintshire and must therefore consider new delivery models, seek out alternative forms of funding and consider different tenures and housing products.
- 2.03 The Council, with support, is looking to develop strategic financial appraisals to make best use of its assets and propose procurement arrangements to create viable propositions and deliver sites cost effectively. The Council recognises the need to deliver a balanced housing offer that creates diverse housing options, offering a range of tenures that include rental and ownership solutions for the full range of income groups.

- 2.04 The focus to date has been on how individual/package sites can be brought forward and developed to deliver affordable homes for rent or sale and how to meet the growing needs of the newly emerging 'middle market' that are unable to access home ownership because of increasingly complex barriers to purchase, such as the lack of sufficient deposit. These groups are economically active and underpin the economic aspirations of Flintshire to support a growing economy and a range of high quality homes for rent and assisted purchase are needed in a range of locations to meet this need. In addition there is a need for development of a significant number of 1 and 2 bedroom homes to meet the needs of those affected by Welfare Reform.
- 2.05 It is recognised that this thinking is new and introduces different risk profiles for the Council. It will require further detailed work before decisions can be made about specific schemes or sites. This report provides the outcomes of initial work for Cabinet consideration. The report begins by considering the national context for Welsh housing and reviews the current housing market in Flintshire.

3.00 CONSIDERATIONS

3.01 National Agenda

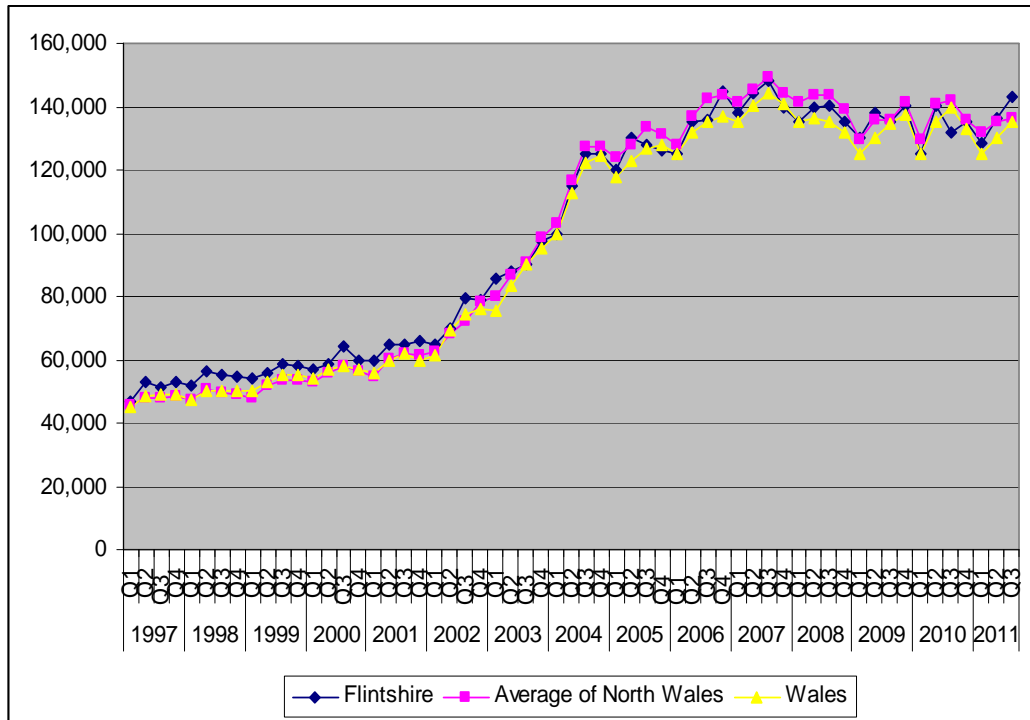
- The increased delivery of new homes is central to the White Paper 'Better Lives and Communities' which was published for consultation in May 2012. The paper supported a range of measures that would help to support this objective include:
- The use of a range of innovative funding mechanisms;
- A new scheme to provide 95 per cent mortgages for first-time buyers of new-build homes- a Welsh mortgage guarantee scheme;
- Delivering a Welsh Housing Bond;
- Enabling a new co-operative housing tenure; and
- Revisions to the planning system.

- 3.02 The White Paper remains committed to the principles of social housing, but places greater emphasis on the use of private rented accommodation, particularly intermediate rental housing, which is seen as part of the solution to the shortage of homes. The White Paper plans to give more flexibility to local authorities, housing associations, and private landlords to operate in different local rental markets and to meet the housing needs of people in different circumstances, as well as working with local authorities to enhance their potential to build new homes.

3.03 The Local Context

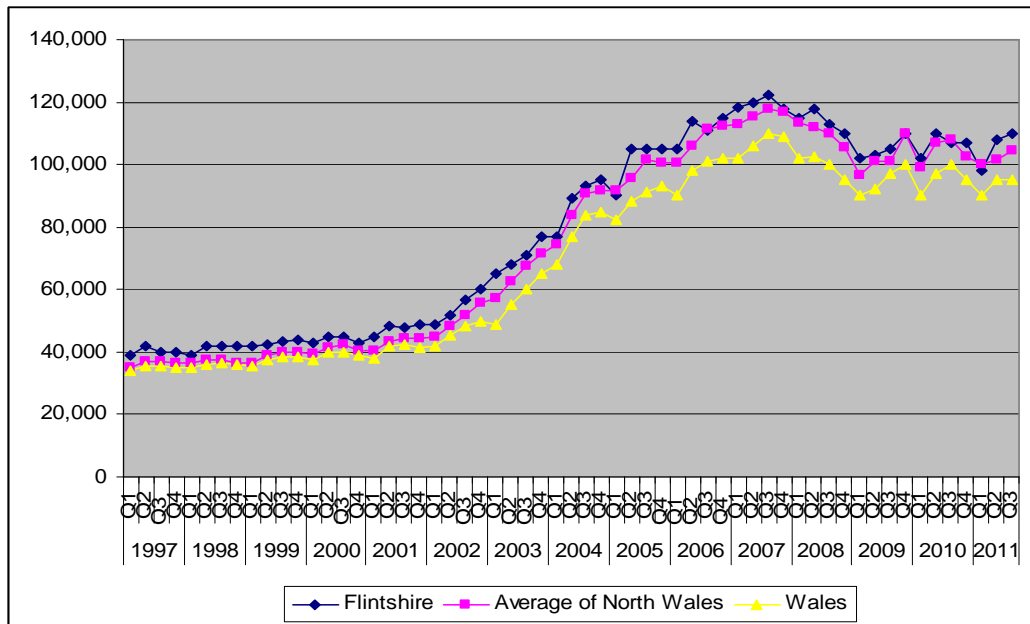
Graph 1 illustrates the median value of housing in Flintshire compared to North Wales and Wales. Generally, the median house prices are slightly higher than the Wales median and very similar to the North Wales Median, peaking at £148k in Q3 of 2007. During the down turn prices have remained relatively stable and were around £143k at the start of 2012.

3.04 Chart 1: Median house prices 1997 - 2001



3.05 Chart 2 overleaf illustrates the Lower Quartile house prices. These are the prices that a first time buyer in the market would expect to buy at. The chart shows that Lower Quartile property prices are slightly lower in Flintshire than North Wales and higher than Wales overall. The average lower quartile price in Flintshire was £100k at the start of 2012, whilst for North Wales this figure was closer to £106k and £95k for Wales as a whole.

3.06 **Chart 2: Lower Quartile house prices 1997-2001**



3.07 In terms of transactions, in line with housing markets generally, Flintshire has experienced significant reductions. At the height of the market in 2007 quarterly transactions reached 700 whilst at the end of 2011 this figure had reduced to just less than 400.

3.08 The Local Housing Market Assessment update for Flintshire has recently been published. The update recommends the provision of an additional 2,885 dwellings over the 2012 to 2017 period. 40% of this should be for affordable housing and 60% open market housing.

Feedback from local lettings agents and developers

3.09 Discussions have been held with 5 local estate and letting agents to establish the current housing market in Flintshire. The agents confirmed that prices have dropped by about 15% since 2007, but that the market is now quite buoyant. There are a number of buy to let investors back in the market and demand for private market rent is high.

3.10 For property sales, 2-3 bedroom terraced properties are very popular and sell for between £90-150k, sometimes more. Agents felt that providing additional 2-3 bed homes would be popular and whilst semi detached was the preferred property type, a modern terraced town house would also be popular. There is little demand for flats on the owner occupation market, but these property types would be popular to rent. The agents reported how difficult it was for purchasers to buy and were very interested to see more home ownership products developed such as shared equity and rent to purchase. Any products that supported purchasers to raise the deposit would be popular and help developers to de-risk sales.

- 3.11 The market rented sector is growing and properties are let quickly. A rental value for a 2-3 bed terraced property would be £500-550 per calendar month and up to £595 for a 3 bed semi detached property. Rental growth is healthy and expected to remain so.

Delivery

- 3.12 As stated above there are a variety of different models and actions that the Council could take in delivering housing schemes. The current economic circumstances clearly present a number of challenges to the delivery of the Council's housing sites (both Council Fund and HRA) and in particular to the delivery of affordable housing. The principle effects of the down turn in relation to the delivery of new homes have been: -

- A significant reduction in property prices, which has meant that creating viable schemes is becoming increasingly difficult;
- Developers are finding it increasingly difficult to access affordable credit;
- Developers are more risk averse/selective and developing in challenging regeneration areas is much less attractive; and
- A severe contraction in the availability of credit, leading to reduced mortgage lending. Often if purchasers can access mortgage lending many are choosing not to; put off by because of concerns around long term employment security and sluggish house prices.

- 3.13 The outcomes of this are that housing delivery has reduced and with it the number of affordable homes being delivered and a new and significant priority group that has emerged who can sustain home ownership but require support to access homeownership or long term intermediate/sub market rented homes. This excluded middle market is not a priority for social rented homes because of their incomes, but equally they are excluded from homeownership given the complexities around lending criteria and affordability.

- 3.14 This is a target group that the Council should attract into Flintshire; they bring skills and prosperity to an area and support economic growth. If the Council wishes to retain and attract this target group, it will need to ensure that it delivers the right housing offer for them. This group will want to buy homes or rent them over a longer time period.

Existing Methods of Delivery

- 3.15 **Section 106** - The Council has a proven track record of using Section 106 agreements to facilitate provision of affordable housing. Section 106 allows Local Authorities to require a developer to make a contribution to the Council which can then be used to fund public realm development or affordable housing. In Flintshire there is currently a requirement that 30% of all housing on new build schemes to be affordable.

- 3.16 Whilst the Council must ensure provision of enough affordable housing units, the requirement for a Section 106 agreement is often seen as increasing the number of unviable housing schemes. Many developers have access to land bought before the economic downturn, which has lost value. In addition house prices have fallen as stated above. This means that provision of affordable housing on these sites could result in a loss for the developer and many are holding on to these sites in the assumption that house prices will eventually rise again.
- 3.17 The Council has been creative in the use of Section 106 agreements to secure both development and affordable housing, including the acceptance of shared equity properties and gifted units. Whilst the council is securing 30% of the value of the affordable housing provision on these developments in challenging times, due to the reduction of social housing grant and the housing associations financial capacity, it may be appropriate to achieve this in alternative ways
- 3.18 An example of this would be on a recent development at Wood Lane Farm. Traditionally through section 106 the Council would have required 66 units of accommodation to be provided to meet the 30% UDP policy allocation. The option originally considered was to provide the properties on a shared equity basis. However, having made reference to both the Local Housing Market Assessment and the affordable housing register it would have been impossible to sell this number of properties using this tenure model. Therefore the Council worked with the developer to provide a mix of gifted houses, shared equity and a financial contribution of £240K, which ultimately achieved the same value and allowed the development to proceed. This creativity is assisting in meeting the Council's objectives, however, it will not provide the number of affordable housing properties required and is likely to further stymie development of housing built for rent and for open market sale until house prices begin to rise again.
- 3.19 As evidence of the above, the number of affordable houses delivered via section 106 contributions in 2012-2013 was 55 through Shared Equity, which are now built and occupied. However, the number of affordable rental properties delivered through a section 106 contribution was only 1.
- 3.20 **Social Housing Grant** - In order to overcome some of the traditional barriers to development, Social Housing Grant funding is provided by Welsh government to Local Authorities. This funding is allocated on a 3 year cycle to Registered Social Landlords to facilitate housing development. The main purpose of Social Housing Grant is to ensure the construction of high quality social housing, supporting schemes that would otherwise be unviable due to the reasons outlined above
- 3.21 However, the use of Social Housing Grant is also failing to provide the number of affordable units required. Flintshire's current Social Housing Grant programme, covering the period up to 2015/2016 is oversubscribed and this funding, along with all other public capital funding is declining.

The funding for 2011/2012 was £1,826,662, funding for 2012/2013 was £1,758,032 however, the funding for 2013/2014 and 2014/2015 is £1,557,749, a decline of approximately 15%. This reduction in funding is directly impacting on the number of social housing units built by the RSLs and will continue to do so over the medium to long term.

- 3.22 SHG funding also comes with a number of conditions, in addition to the requirement to build housing at social rents. All properties must be built to Development Quality Requirement (DQR) standards. This increases the build cost of units. In anticipation of further reductions of SHG funding some RSLs are seeking to build accommodation at affordable rents as opposed to social rents. This would increase the viability of certain schemes, as it allows units to be built to a slightly lower standard, reducing upfront cost, it also allows for higher rental yields. However, the three main housing associations operating in Flintshire have yet to take up this opportunity and it will probably be some time before they are in a position to do so. Therefore, Social Housing Grant will not be in a position to provide the required units of affordable accommodation. Further information is contained within **Appendix 1 – Social Housing Grant Template**.

New Methods of Delivery Prudential Borrowing

- 3.23 Some Councils across England and Wales are planning to or have already used prudential borrowing to develop new homes to meet the needs for smaller units of social housing, or to meet unmet housing need through estate redesign or new development. Any capacity available however, is limited through borrowing limits set by Government and would not meet all needs identified over the longer term. **Appendix 2 – Prudential Borrowing Template**.

New Opportunities for Section 106 developments

- 3.24 In the Section 106 model of delivery a developer would usually deliver the sales units and a housing association takes the affordable units, The Council may also choose to take on the housing association role and manage the affordable and market rent units themselves. Whilst there are many differences between managing social units and delivering a service for market rent, the Council and the housing associations are equipped with the skills and expertise to undertake this role
- 3.25 However, there may be a number of issues with this model that would require the Council to provide support in different ways and a number of these are detailed below:
- affordable credit for the developer may be difficult and the Council could support (if funding was available), the provision of a low interest loan to reduce the borrowing requirements of developers or the cost of doing so. This can have a further positive impact on viability and enable delivery to move forward.

- the developer is unlikely to be able to fund shared equity products on the market sales stock given the already low values. The Council could fund the loan products to enable a product to be put in place and recoup the funding when the properties are sold (by purchasers). This would de-risk sales for the developer and retain the owner occupation units; much needed to diversify the housing stock in many areas.
 - the Housing Association partner may wish to share the risk of taking on long term market rent units with the Council.
- 3.26 Delivery of this model would require Flintshire to provide capital funding, either from the core capital programme or through prudential borrowing. In addition, any homes that are developed for rent or sale other than social rented homes would need to be “held” in an arms length company wholly owned by the Council but separate.
- 3.27 The Council has a number of Capital Assets in the form of land which would reduce the cost of development while it has significant pressure on its revenue resources therefore the financial models below provide the Council with opportunities to increase affordable housing delivery and supply by utilising assets with limited or no financial contributions

The Local Authority/Registered Social Landlord/Developer Partner model of Delivery

- 3.28 This model involves the creation of a joint venture or legal partnership at arms length to the Council. The development risk will be shared amongst all partners. The joint venture would appoint a contractor to undertake the build. The joint venture would fund the scheme, sell units on the open market, and retain and manage the affordable and market rent units. This model along with all new financial models requires the Council to consider disposing of its land asset at nil value, effectively providing its investment in the scheme, without the need to provide capital funding.
- 3.29 These partnerships are very flexible and there are a growing number led by local authorities. The models can be established to work within the local authority’s requirements and may involve institutional investors having a role in funding delivery, or in purchasing completed units for investment. There is no ‘fixed’ approach to these arrangements and the Council may:
- Provide land assets for free, or under a deferred payment system, with value being realised after a longer time frame or
 - Share the build costs with a contractor partner or housing association and share sales risk.
- 3.30 Whilst further work is required this model would provide a sound delivery basis on which to proceed potentially utilising a Limited Liability Partnership. Further information is contained within **Appendix 3 – Joint Venture with Developer/Housing Association Template**

3.31 **Leasing finance/institutional investment**

3.32 There is a growing trend and offer from contractors/developers to provide the funding for the up front build cost and then recoup it over a period of time by leasing the units to a managing agent; in this case the Council (or housing association partner). These models are growing in popularity and there are a number of established models available on the market which the Council may choose from. The models offered by different investors/developers will have their own financial assumptions and the Council will need to consider these individually. A series of meetings have taken place with developers and their funders in order to fully understand the models. The primary benefit is that the Council does not have to front fund any development

3.33 In some models, investors provide the necessary funding, whilst the Council would appoint a contractor/developer to deliver the schemes. The investor owns the properties but leases them to the Council to rent out and repay the initial costs plus a rate of return. Alternatively a number of developers are front funding schemes themselves, building the sites out and then leasing the properties to the Council or partner housing association.

3.34 In most models after the end of the term of the lease, the properties will move into the Council /housing association ownership. These models can work for both sale and rent, providing the sale value achieved gives an adequate rate of return. However, they are likely to be offered within an affordable rented tenure model, (rather than social). Further information is contained within **Appendix 4 – Leasing Template**.

A deferred purchase model/institutional investment

3.35 In the current housing market where purchasers find it difficult to buy a home, but retain an aspiration to purchase a property in the future, a rent to purchase model may provide a practical solution. The product allows a household to initially rent a (new) property, but on the clear (legal) understanding that they can purchase it in the future under pre-determined terms. Rent levels can either be “open market” or sub market. The landlord can reserve the right to terminate the tenancy after an agreed number of years, if the tenant has not chosen to purchase. The purchase terms can include such features as a fixed price (for the first 3 years of tenancy, typically 3 or 5), often on a shared equity or shared ownership basis, and with purchase incentives such as partial rebate of rent, or discount if no/minimal repairs have been requested. Further information is contained within **Appendix 5 & 6 Forward Funding & Deferred Purchase Model (Rent to Buy) Template**.

Housing Co-operatives

3.36 The Welsh Government is keen to support a co-operative delivery model

and also supports Community Land Trust models. In Homes for Wales: A White Paper for Better Lives and Communities the Government wants co-operatives to become a much more significant part of the housing system and plans to aid the development of co-operative housing as a housing choice. Housing co-ops are groups of people who live in and collectively manage their accommodation. This can involve taking responsibility for arranging repairs, making decisions about rent and who joins or leaves the co-operative. Living in a housing co-operative can be a good way to get affordable housing and may give you more control over where you live.

- 3.37 Co-operatives use limited equity models and are a form of “mutual home ownership” or rented or market co-operatives. Co-operatives result in democratic community membership, standards at least equivalent to those for social new build housing, and will be suitable for people on a range of incomes. Community Land Trusts are likely to facilitate such developments.
- 3.38 The Government is considering the need for a new form of co-operative tenancy. The purpose would be to permit a member’s right of occupancy to create an equitable interest in a co-operative’s property, which can then be used as security for loans to buy a ‘limited equity’ stake in their home.
- 3.39 The Government is committed to delivering 500 new homes through Co-operatives and so this is unlikely to be a model that delivers all of the new homes being proposed and is unlikely to assist in improving financial viability. However, as a model for re-provision of affordable housing and in improving stakeholder interest in the area it is a model worth further investigation

Risk Analysis

- 3.40 Each of the options outlined in this report provides key considerations depending on the site identified, tenure mix needed and financial resources available. Each site will require appraisal on an individual basis. Each of the delivery options exposes the Council and its partners to new risk areas and each has a number of advantages and disadvantages.

Conclusions

- 3.41 Delivering new housing will be very challenging in the current housing market; there is an increasing demand for housing as new household projections increase and the Welsh government are prioritising an increasing supply of homes as a key political objective. The housing market remains challenging, prices have reduced, as have the number of sales. The successful delivery of schemes will require a range of tenure models and new delivery arrangements. Although more detailed financial modelling will determine final scheme property mix and tenure, the financial modelling and discussions with local agents and developers has illustrated that financial viability and delivery are likely to be more

successful if:

- The number of homes for market rent is increased and replaces a proportion of market / affordable sale on schemes. This supports a growing demand for private rented accommodation which is supported by local agents, it also means that developments have less 'sales risk' because the units would be sold or leased to either the Council or partner housing association.
- Affordable rent replaces some social rent units. The additional rental income will have a positive financial impact on the viability of schemes. The affordable rent level at 80% of market rents is an acceptable tenancy option for the Welsh Government, although further work would be required to test its affordability locally.
- Lower numbers of affordable housing units are considered on some sites. Market rent deliver the optimum financial viability and the Council will need to consider the proportion of affordable housing that is required within schemes.
- A rent to purchase product is introduced. The Council can take advantage of a buoyant rental market in the early years and benefit from rising property prices in later years¹.

3.42 Whilst it has been demonstrated that alternative tenure models do improve economic viability and provide flexibility to the Council, the Council needs to consider the Welsh Government requirements to ensure that any housing that is retained in ownership by the Council would need to take account of the current guideline rent regime and any changes that may apply in the future. This would make it difficult for the Council to retain ownership of properties for market rent for example. However, it is possible to enter into an agreement with Welsh Government under Section 83 of the Local Government and Housing Act 1989 to exclude certain houses which may be owned by the Council from the HRA calculation; early discussions with Welsh Government are recommended.

3.43 There are a number of delivery models available to the Council which have briefly been reviewed in this report. These require further work but legal advice obtained to date confirms that these models are all deliverable.

4.00 RECOMMENDATIONS

4.01 That Cabinet note the variety of financial models available to the Council to facilitate housing development in Flintshire without the requirement for public grant subsidy and draw upon this framework for making future decisions for specific schemes to meet its housing objectives.

5.00 FINANCIAL IMPLICATIONS

5.01 There are no financial implications at this stage.

6.00 ANTI POVERTY IMPACT

6.01 Each of the models will provide additional affordable housing and would therefore have a positive anti poverty impact.

7.00 ENVIRONMENTAL IMPACT

7.01 All new affordable housing arising out of these financial models will be built to high standards which would provide a positive environmental impact.

8.00 EQUALITIES IMPACT

8.01 There are no equality implications arising out of this report.

9.00 PERSONNEL IMPLICATIONS

9.01 There are no personnel implications arising out of this report

10.00 CONSULTATION REQUIRED

10.01 Consultation with Members will be required to secure support for the chosen financial model to deliver each scheme.

11.00 CONSULTATION UNDERTAKEN

11.01 Senior Members and Member stakeholders have received a presentation on each of the financial models with an opportunity to evaluate the risks and benefits of each.

12.00 APPENDICES

12.01 Social Housing Grant

12.02 Prudential Borrowing

12.03 Joint venture

12.04 Leaseback

12.05 Institutional Investment (Forward Funding)

12.06 Deferred Purchase

LOCAL GOVERNMENT (ACCESS TO INFORMATION ACT) 1985 BACKGROUND DOCUMENTS

None

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