

NOT FOR PUBLICATION

Appendices of this report contain exempt information as defined in Paragraph 3 of Part 1 of Schedule 12A to the Local Government Act 1972 (information relating to the financial and business affairs of the Council)

Report to: **COUNCIL**

Date: **25th November 2021**

Title: **St Anns Chapel Housing Project**

Portfolio Area: **Cllr J Pearce – Housing**

Next steps to be undertaken: **N/A**

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RECOMMENDATION:

It is RECOMMENDED that Council:

- 1. Approves construction of the project to deliver 8 Affordable Homes, 3 Open Market Units and 2 serviced plots at St Anns Chapel Affordable Housing Scheme (“the Project”).**
- 2. Agrees that the total project cost of £4.2 million of the project is to be funded as follows:**
 - 2.1 Long-term funding of up to £2.2m from a combination of internal and external borrowing (from the Public Works Loan Board);**
 - 2.2 Funding of up to £250,000 from the Affordable Housing Earmarked Reserve (in addition to the £100,000 approved previously);**
 - 2.3 £1.4m from the disposal of the 3 Open Market Units;**
 - 2.4 A Homes England grant of not less than £110,000; and**
 - 2.5 £162,000 from Section 106 contributions (previously approved)**

- 3. Approves the short-term borrowing costs of approximately £3.6million over a two-year period (before the three Open Market Units are disposed of for £1.4million)**
- 4. Delegates the borrowing strategy for the internal and external borrowing approved above to the Section 151 Officer in accordance with normal treasury management activities.**
- 5. Delegates to the Head of Assets the power to dispose of the 2 Serviced Plots as consideration for the land purchase and the 3 Open Market Units.**
- 6. Authorises the Head of Assets to make an application to Homes England for grant funding of at least £110,000 to support the delivery of the Project.**
- 7. Authorises the Head of Assets in consultation with the Head of Housing to increase the number of Affordable Rental Units up to 8 within the proposed Affordable Housing Scheme.**
- 8. Authorises the Head of Assets to make the contract awards necessary for the delivery of the Project.**
- 9. Notes that upon completion of the Affordable Homes, it is intended to transfer them on long-leases to the Community Benefit Society being formed by the Council, subject to the Director of Place and Enterprise in consultation with the Section 151 Officer, undertaking due diligence to identify the associated legal, financial and accounting implications of doing so.**

1. Executive summary

- 1.1. This report provides an update and makes recommendations with respect to the St Anns Chapel Community Housing Project, following previous approvals in April 2020 [Minute CM88/19, Council 30th April 2020] and September 2020 [Minute CM22/20, Council 24th September 2020].
- 1.2. Despite best efforts of officers, the project has not concluded the construction phase due to a supply chain failure, with the principle contractor.
- 1.3. Brexit and the pandemic have all impacted the cost of construction and the delivery of housing and inflated the housing market in that time (reported to be in the order of 20%).
- 1.4. On 23rd September 2021, the Council declared a housing crisis. One of the key reasons for this was the acute shortage of affordable rented accommodation throughout the District, particularly in coastal areas such as St Anns Chapel.
- 1.5. Previously, it was proposed the Affordable Housing Scheme would be largely discount purchase units for ownership with 1 affordable rental unit. It is now proposed up to all 8 units be delivered as affordable rental units. The development could therefore deliver 8 much needed rented houses. A further 3 open market sale properties to cross-subsidise the development and 2 serviced plots for the landowner will be constructed.
- 1.6. The housing need survey supports provision of rental accommodation in the locality (parish and immediate neighbouring parishes) and identifies a need for the following affordable housing: 4 x 1 bed, 10 x 2 bed and 2 x 3 bed rental units.
- 1.7. In the past 3 years, just 20 new affordable rented properties have been delivered by the market across the South Hams AONB. The St Anns Chapel scheme, could add 40% more rental units to that total.
- 1.8. The Section 106 Agreement details the requirements for any Low Cost Market Dwelling or Affordable Rented Dwelling but the Affordable Housing Scheme is yet to be agreed and subsequently approved.
- 1.9. A further procurement exercise has been completed and the supply chain secured. A construction contract is available to enter, subject to Council approval.

- 1.10. The cost of delivery and building the units is £4.2 million. The impact of sales of open market units and secured funding results in approval being sought for long term Public Works Loans Board (PWLB) borrowing over 50 years of up to £2.2m. This long term borrowing is required to allow the retention of up to 8 affordable rent properties.
- 1.11. The business case set out in the report is based on 8 rental units with rent set at published Local Housing Allowance (LHA) for the relevant property type within the Administrative Area (Plymouth).
- 1.12. The business case is based on a "worst case" assumptions and may be improved upon – see Risks and Opportunities sections. It includes the proposed use of £250k of funding from the Affordable Housing Earmarked Reserve, which has a current balance of £470k, to assist in the delivery of affordable rented properties.
- 1.13. If approved, delivery will commence in spring 2022 with completion anticipated for late 2023.
- 1.14. The properties will be highly efficient, high quality homes and will be low cost to heat and run. Air source heat pumps and low water use fittings all form part of the design specification. Furthermore, the concept of Fabric First¹ has been utilised throughout which prioritises energy efficiency within the building envelope.
- 1.15. It is envisaged the properties will be managed by Seamoor Lettings. The Council is continuing the process to set up a Community Benefit Society with Registered Provider status and the homes will remain the property of the Council in perpetuity, continuing to meet housing need. The business case supports setting aside up to 25% of all rental income for management and maintenance.

2. Background

- 2.1. Previous Council approvals gave the Head of Assets, in consultation with the Head of Paid Service, the s151 officer and the Lead Member for Assets, delegated authority to approve expenditure of up to £8.5m from a combination of internal borrowing and external borrowing to fund the construction of the first four community housing projects in accordance with business cases being South Brent, St Ann's Chapel, Brixton and Kingsbridge.
- 2.2. These developments, in line with the Community Housing Strategy were to be developed to support the delivery of homes accessible to those with local connections where market housing, either to purchase or rent is beyond reach. In turn supporting the vitality and sustainability of local communities.

¹ Maximising the performance of the components and materials to make the building as energy efficient as possible.

- 2.3. Following this decision, the Council worked in collaboration with Bigbury Parish Council to develop an affordable housing scheme in St Ann's Chapel based on a mix of 8 discount purchase and affordable rented units plus 3 open market units to be sold to cross subsidise the scheme.
- 2.4. Following receipt of recommendations for approval of the planning applications for each scheme from the respective authorities planning committees, the completion of pre-construction technical and environmental assessment work and a competitive tender process, in September 2020 an Executive report recommended the signing of construction contracts (JCT) to complete the St Anns Chapel (13 Units) and South Brent (17 Units) Developments with expenditure of up to £5.8m.
- 2.5. In December 2020, a Letter of Intent (LOI) was issued to the successful contractor, with a view to entering the full construction contract. At that stage, the contract was for the delivery of the St Anns Chapel element only, albeit the intention was to enter contract with the same contractor (as per the tender), once the South Brent scheme was in a position to proceed.
- 2.6. However, the successful tenderer had concerns in relation to labour supply chain issues particularly the availability of ground workers, drainage challenges at St Anns and the impact of the period between tender and award.
- 2.7. The Council provided opportunities for the contractor to continue to secure the works and revise the tender price based on inflationary costs, the revised drainage scheme and costs which may have been reasonably incurred. Despite this, the contractor pursued a route to secure payment under the Letter of Intent solely, instead of securing the contract. The contract therefore was not completed.
- 2.8. Section 4.1 sets out details of the new supply chain that is now in place.

3. The Affordable Housing Scheme

Housing Need Survey

- 3.1. Establishing housing need is key principle of any housing project and this has been established at St Anns.
- 3.2. The housing need formed part of the planning report and this scheme will deliver on some of the established need. It is therefore not necessary to conduct an updated housing need survey.

- 3.3. There is however a need to carry out community engagement work to ensure the community are aware of the proposed changes to increase the affordable rented accommodation up to all 8 units. The Council will ensure the opportunity and ability to access these homes is widely publicised and the community is kept apprised of the progress of the scheme.

Affordable Rental Dwelling

- 3.4. A benefit of the project having not yet commenced is the ability to adjust the tenure of the properties away from discount sale into affordable rent.
- 3.5. The proposed Affordable Rented Dwellings will be made available for rent at the Plymouth Local Housing Allowance (LHA) for the relevant property type within the Administrative Area. This rate is significantly lower than the South Hams LHA rate. On this basis, the rent will be £134.63 per week (£583/month) for a 2 Bedroom house and £159.95 per week (£693/month) for a 3 bedroom house.
- 3.6. Combined with low running costs of the new energy efficient housing and high open market rents in the area, the rent is significantly affordable.
- 3.7. Comparable evidence in the locality (limited availability), suggests a similar 2 bedroom property would rent for circa £900/month and a 3 bedroom property in excess of £1200/month. The rent proposed is therefore circa 60% of the open market rental value. Added to this the low running costs, it is considered these properties will be affordable and accessible for local people. Generally, social rents are considered to be around 60% of open market rent in the area.

Planning Position

- 3.8. Strategic and DM planning policy issues have been considered through the development of this project and as demonstrated by the planning approval, seen to be in line with both.
- 3.9. The Section 106 Agreement requires the provision of affordable dwellings in accordance with an Approved Affordable Housing Scheme. This includes the numbers, types and tenures of the Affordable Dwellings and must be agreed before occupation.
- 3.10. The Approved Affordable Housing Scheme will be supported by housing need evidence. If the proposed tenure provision of up to 8 affordable rent units is approved, the Affordable Housing Scheme will be developed on this basis. In this case, approval must be sought from Devon County Council as South Hams District Council is the landowner and cannot covenant with itself.

- 3.11. The development proposal has been given planning permission on the basis of it being a rural exception site, as an affordable housing-led scheme responding to identified housing needs in the area.
- 3.12. The market challenges of bringing forward rural exception sites are well understood and as such there are few proposals that reach the planning application stage once the viability challenges of this type of development are known. Policy TTV27 allows for up to 40% of open market housing to be delivered onsite in order to cross-subsidise the affordable housing element of a proposal. This scheme does not fully utilise this.
- 3.13. The tenure split being offered onsite reflects the adopted policy position across the JLP Councils, which is to be flexible and responsive to the specific housing needs in the local area. The split between affordable rent and social rent in this instance reflects what is known about housing need in this area at the point when the development is going to be delivered.
- 3.14. Research undertaken to inform the Housing Emergency declaration highlights an ongoing shortage of rented homes in our area, particularly at an affordable rent. There are a number of reasons for this, and the Council is being proactive in bringing forward housing tenures that meet known short term gaps in housing provision. This issue is particularly acute in the coastal belt villages, where the provision of rented accommodation lost to the holiday accommodation market has led to a severe restriction in housing choice for local people.

4. Business Case

Contract Tender

- 4.1. The original procurement exercise was run in summer 2019. The market has seen significant impacts from the Covid-19 Pandemic and Brexit which have caused supply chain delays and material cost increases. It is estimated contract costs are now in the region of 20% higher than pre-pandemic. Furthermore, this impacts the contractor's treatment of risk within any tender.
- 4.2. Following the breakdown of the supply chain through the existing tender, a retender exercise commenced in June 2021. Further to this, we now have a preferred contractor and an associated contract price. This is circa 20% higher than the previous contract tender price.

Financing of the £4.2million scheme in the long term

The total build cost is £4.2million would be financed as below:

- Long term borrowing of £2.2million over the asset life of 50 years (a mixture of external Public Works Loan Board borrowing and internal borrowing)
- Sale proceeds from three open market units of £1.4million
- Approval is sought in this report for further funding from the Affordable Housing Earmarked Reserve of £250,000
- Homes England grant funding (minimum contribution of £110,000)
- Section 106 funding of £162,000 (£97,700.91 from the contribution from the former Old Chapel and £65,193.00 from the contributions from the Hollywell Stores developments)
- Affordable Housing Earmarked Reserve £100,000 (already approved at Council 30th April 2020)

Financing of the £4.2million scheme over the first two years

- 4.3. There would be short term borrowing costs of approximately £3.6million over a two year period (before the three open market units are disposed of for £1.4million). It is recommended that the borrowing strategy is delegated to the Section 151 Officer, in accordance with normal treasury management activities.

Homes England Funding

- 4.5 The St Anns Chapel project was originally intended to provide intermediate housing to be sold into the market as discount purchase sales at 65% of open market value. The business case previously did not require Homes England funding to breakeven. However if this had changed, discount purchase properties did attract Homes England funding at that time.
- 4.6 In the new Affordable Homes Programme (2021-2026) this is no longer the case and Homes England funding is only obtainable on shared ownership or affordable rent properties.
- 4.7 We have a pending application on the Homes England application system for the scheme. We cannot yet confirm how much Homes England funding we may secure to support the scheme. However, following discussions with Homes England we anticipate a successful application on at least two units with associated funding of £110,000.

Development Value

- 4.8 An open market value appraisal was completed in August 2021 and placed a total development value of £3,980,000, of which around £1,400,000 relates to the open market units. These will be sold to cross-subsidise the affordable rental units and reduce the required long term borrowing.
- 4.9 In simple terms, this means the assets will have a book value of nearly £4m and are anticipated to appreciate in value.
- 4.10 The value of the rental units will be retained within the Council.

Proposed Funding arrangements

- 4.11 There are three distinct funding stages in the Council's project development programme:
- **Development Costs** – all pre-construction costs incurred including detailed design, planning consent, legal fees, land assembly & acquisition and tender preparation & award. This stage is initially funded through the Community Housing Fund grant with costs incurred being reimbursed at the point of entering into construction contract, such that these costs can be reinvested in subsequent projects thus providing revolving funding to enable the programme to continue.
 - **Short Term Finance (£3.6million)** – finance required over the construction term
 - **Long Term Finance (£2.2 million)** – finance required to enable the rental units to be retained by the Council. The required repayments (capital & interest) to be covered by the net rental return of the affordable units.
- 4.12 The development and feasibility costs have been paid out of the original £1.88million Community Housing grant and the spend on the St Anns scheme currently totals £318k. This revenue cost will be capitalised and funded by borrowing (therefore these revenue costs will be recyclable) as the scheme proceeds to fruition. These costs of £318k can then be reinvested in future housing pipeline projects to address the housing crisis.
- 4.13 In order to facilitate the construction of the project, it is proposed the required finance will be drawn down from the PWLB and internal borrowing as appropriate. The figure of £3.6 million is required in short-term borrowing to facilitate the construction phase of the development.
- 4.14 Once the scheme is completed and the sale of the open market units, along with known costs for contingency, finance costs etc and any further secured funding, will equate to the required figure to be borrowed from PWLB over a period of 50 years will be £2.2 million as shown in 4.2.

5 Funding

A cash-flow forecast is included as Appendix 1 within the Business Case.

Opportunities

Homes England Funding

- 5.1 There is a pending application on the Homes England application system for the scheme. The amount of Homes England funding that may be available cannot be confirmed, however further to discussions with Homes England it is anticipated at least £110k in funding will be available. We are continuing to work with Homes England to maximise funding for this project.

Community Benefit Society

- 5.2 It is the intention of the Council to retain ownership of these eight properties, leasing them through a community benefit society. Retaining ownership ensures the properties are protected for future generations and further safeguarded through robust local connection criteria. These properties will be the first Council Houses South Hams District Council has built in a generation.

6 Risks

Supply Chain

- 6.1 There are current market wide, global challenges impacting the construction industry which are leading to supply chain and material availability challenges.

Pre-Commencement Conditions

- 6.2 The current design allows for onsite drainage through a soakaway system. However, in order to complete the required monitoring period, we must wait until the end of March 2022 for the groundwater monitoring to have complete a full cycle. It will only be known on completion whether onsite drainage is possible.
- 6.3 There is an option to go to offsite drainage, however this requires access over third party land and the installation of infrastructure outside of the development boundary. There is an extra cost which has been costed within the existing tender and included within the contract cost currently reported in the business case.

Revision of Affordable Dwelling Tenure

- 6.4 Whilst the Section 106 Agreement is not prescriptive as to the mix of affordable rented or low cost housing, it may be we are unable to agree an increase of all eight units as affordable rent.
- 6.5 We will be carrying out community engagement work to ensure the community are aware and supportive of the proposed changes to increase the affordable rented accommodation. The Council will ensure the opportunity and ability to access these homes is widely publicised and the community is kept appraised of the progress of the scheme.

7 Summary

- 7.1 The St Anns Chapel Housing project presents an opportunity to develop an affordable scheme that meets the local housing need and addresses the wider South Hams housing crisis.
- 7.2 It is proposed up to a total of £350k of the Council's reserves in the Affordable Housing Earmarked Reserve will be utilised to bring the project to fruition but this would also reimburse the Community Housing Fund with £318k of development costs spent to date, equating to a modest investment with respect to the Council's own funding.

- 7.3 The long-term financial position therefore is positive and after the 50-year term of the PWLB borrowing, the council will wholly own the rental properties. It should also be noted, at an annual growth of 1% in value, against current value of 8 rental units, the properties would appreciate in capital value by circa £1.7 million.
- 7.4 The Section 151 Officer has reviewed the business case and the associated costs, income and borrowing position of the Council and supports the recommendations set out in the report.

8 Way Forward

- 8.1 The Council approve the recommendations in this report to ensure this scheme can move into the delivery phase.
- 8.2 If approval is given, the Council will be able to deliver up to 8 affordable rented houses in response to the housing crisis, to be agreed in the Approved Affordable Housing Scheme.

9 Implications

Implications	Relevant to proposals Y/N	Details and proposed measures to address
Legal/ Governance	Y	<p>The Council has power under the Housing Act 1985 to provide housing accommodation by either building on land acquired for that purpose or acquiring houses.</p> <p>The contract for the delivery of the Project has been procured in accordance with the Council's Contract Procedure Rules.</p>
Financial	Y	<p>It is proposed that the Council will fund up to £4.2million initially for scheme development and up to £2.2 million as long term finance from a combination of internal borrowing and external borrowing (from the Public Works Loan Board) to build the St Ann's Chapel (13 units) housing scheme. Other sources of funding will be from any capital receipts yielded from open market sales and s106 affordable housing contributions and the Council's affordable housing reserve as detailed in Section 4 'the business case'. Specialist treasury management advice has been taken and will be further sought nearer to the time that the scheme starts on site.</p> <p>The Council legally does not have the ability to borrow in advance of need. It is therefore not possible to guarantee the interest rate that will be achieved. Any borrowing decision will be in</p>

		line with the Council's adopted Treasury Management Strategy and Affordable Borrowing Limits.	
Risks	Y	<u>Risk</u> Project cost escalation Shortfall in proceeds from sale of market, discount or rented units Interest rate rise	<u>Mitigation</u> Project supervision contract with supervising engineers. The economic model allows a 7% contingency sum. Binding contractual protections will be put in place which include liquidated damages to prevent overrun (excluding COVID related delay). Additional cost mitigation through re-evaluation of construction costs upon completion of contract. Renewed valuations by external agents undertaken to confirm values within economic model. Conservative estimates applied to inflation and property value increases. PWLB rates fixed at the point of drawdown, such that the economic model will be fully verified based on the rate of borrowing at the time. Internal borrowing reduces the overall interest cost of the scheme.

Comprehensive Impact Assessment Implications		
Equality and Diversity	N	N/A
Safeguarding	N	N/A
Community Safety, Crime and Disorder	N	N/A
Health, Safety and Wellbeing	N	N/A
Other implications	N	N/A

Appendices:

EXEMPT

Appendix 1: St Anns Chapel Development Business Case