

31 January 2018		ITEM: 14
Council		
Thurrock Regeneration Ltd – Proposed Development of Belmont Road Site, Grays		
Wards and communities affected: Grays Riverside		Key Decision: Key
Report of: Leader - Cllr Rob Gledhill; Portfolio Holder for Regeneration - Cllr Mark Coxshall		
Accountable Assistant Director: Detlev Munster - Assistant Director, Property & Development		
Accountable Director: Lyn Carpenter, Chief Executive		
This report is Public		

Executive Summary

Thurrock Regeneration Limited (TRL - formerly, Gloriana Thurrock Ltd) was originally anticipated to develop between 350 and 500 properties when it was set up in 2013. The objective of Gloriana was to intervene, strategically, in the housing market, developing housing on key sites in the borough. It was to act as a catalyst for private sector investment, where stalled sites and low market confidence was a real block to delivering Thurrock's vision.

It is proposed that TRL look to establish an increasing development pipeline of homes which will take the company beyond its initial 350-500 home target. Consideration will be given to ensure an optimum level for a functioning, compelling business plan that effectively balances the competing issues of development/financial risk, delivery capacity and commercial returns whilst achieving its main aim of supporting the house building market.

This report provides details of TRL's proposals to develop the Belmont Road site in Grays with the recommendation that the Council agrees to lend the funds to TRL to deliver the scheme.

This is the final Gateway stage in the pre-construction process. The scheme proposed for the Belmont Road site, has received full planning approval. TRL is working towards a start on site with enabling works as soon as possible and a full site commission by the proposed developer by June 2018.

Officers have worked with the scheme employer's agent and financial consultants to produce a best possible final cost estimate for the scheme, including contingency,

which will be finalised through the contractor procurement process. The use of Right to Buy receipts is also discussed as an option for the HRA to help purchase Belmont Road affordable units which will result in 28 new council homes for those on the Council's waiting list.

It is proposed that delegated authority be given to the S151 Officer, in consultation, with the Chief Executive, the Portfolio Holder for Finance and the Leader, to approve the scheme funding to TRL and related amendment to the Council's finances. This delegated authority will be subject to the scheme meeting key financial parameters.

Recommendation(s)

That Council:

- 1.1 Agrees that Thurrock Regeneration Ltd develop the Belmont Road, Grays site in accordance with the consented planning application.**
- 1.2 Agrees that authority be delegated to the S151 Officer, in consultation, with the Chief Executive, the Portfolio Holder for Finance and the Leader, to agree the final funding to TRL, and to enter into legal agreements as required, subject to the financial parameters as set out in the report.**
- 2. Information and Background**
 - 2.1 The scheme consists of 80 terraced and semi-detached houses, following the existing street line with a courtyard of bungalows at the centre of the development. There are three pocket parks incorporated within the proposed scheme, one of which will host children's play facilities. Natural surveillance is achieved throughout the development making the scheme feel secure. Thus the scheme proposed will remove the existing untidy and unmaintained land at the end of the Belmont Road cul de sacs, provide much needed, quality homes which will improve the street scape and deliver usable open space which can be enjoyed by all. There are ten, 2 bedroom bungalows with the rest of the development predominantly 2 and 3 bedroom houses.
 - 2.2 The proposed tenure mix is planning policy compliant with 35% affordable housing, a mix of affordable rented and shared ownership with the remaining housing being for the private market.
 - 2.3 A final fixed price tender is expected in April 2018 and enabling works will start as soon as possible with a full start on site by the proposed contractor by June 2018.
 - 2.4 Assuming Full Council approval is forthcoming, the next step is that the Land Transfer, Management and Funding Agreements between the Council and TRL are entered into and TRL enters into a construction contract.

3. Issues, Options and Analysis of Options

- 3.1 The development scheme received planning permission on 28th September 2017. The alternative options for the Council to consider are to sell off the land with planning permission to a private developer, or the possibility of the HRA investing in or building out the site. Summary of key risks and opportunities:

Option	Opportunities	Risks
Transfer the land to TRL to develop	<ul style="list-style-type: none">• Articulating the vision• Control of design and place making• Long term investment• Generation of returns / pursuit of mutual objectives• Revenue receipts• Dividend at the end of the development• Cross subsidy for affordable housing• Certainty in the delivery of homes• Potential opportunity for Council to own affordable units	<ul style="list-style-type: none">• Market uncertainty• Competing demands (company vs corporate)
Disposal to a private developer	<ul style="list-style-type: none">• Up front capital receipt	<ul style="list-style-type: none">• Risk of different scheme coming forward due to viability• Uncertainty of delivery• Less control over the development
HRA	<ul style="list-style-type: none">• Increased Council housing units	<ul style="list-style-type: none">• No Borrowing capacity in the HRA and therefore not a current option

- 3.2 Provision could be put in place in a disposal to a private developer (with regards to the contract) to restrict the development to the conditions set out in the planning permission. However, as the financial modelling suggested, it is unlikely to be attractive to other developers due to viability. Therefore, there could be a delay in building out the scheme or at the worst case scenario not at all.

- 3.3 Agreement to the recommended option for TRL to gain the funding and land transfer would provide the Council with a revenue stream via the repayment of interest on the loan over several years as well a dividend at the end of the business term.
- 3.4 Members are aware that increasing stock within the Housing Revenue Account (HRA) is limited due to the current debt cap regulations. Government announced in the 2017 Autumn Budget its intention to put in place a process for the HRA debt cap to be lifted in high demand areas from 2019/2020. However, despite the ring-fence that separates the HRA from the General Fund (GF), it is possible to use GF capital receipts to pay for HRA capital expenditure.
- 3.5 This offers a further benefit that Thurrock Regeneration Ltd (TRL) can bring. Whilst receipts from the St Chads development needs to be used to repay TRL debt back to the council, all forecasts result in a dividend in excess of £3m by the project end after all debt liability has been repaid. With a receipt due from the disposal of the affordable housing units, this allows for an amount equivalent to that dividend to be freed up now that can then be part matched against the one to one receipts the council already holds.
- 3.6 The Government introduced a new Right to Buy (RTB) policy in March 2012 “Reinvigorating RTB”. As part of this policy Councils could retain all surplus RTB receipts (rather than just 25% as previously) if the receipts were used for one-to-one replacement. In order to retain these surplus RTB receipts, Thurrock Council entered into a RTB Agreement with the Government. However, the RTB receipts can fund no more than 30% of the total scheme cost of new affordable rented housing. The receipts must also be spent within three years or there are returned to the Government with interest.
- 3.7 Therefore, assuming an excess in the region of £3.2m, a budget to the HRA of £4.8m becomes available with the one to one receipts policy (that is an additional 30% of total scheme cost of affordable rented housing). This could be used to purchase Belmont Road affordable units. By capitalising the receipts from the St Chads site and using the one to one receipts from RTB TRL will be able to build 28 new council homes for the HRA for those on the Council’s waiting list which should become available in late 2019. This can be achieved without lifting the HRA borrowing cap.

Risk Assessment

- 3.8 The risk register approved by Cabinet at FBC stage has been kept under review. All site related risks will be dealt with, now the scheme has gained planning approval. The key risks at this stage are financial viability and state aid compliance due to a worsened financial situation since Gateway 2. Full site investigations have taken place to test ground conditions.
- 3.9 The financial position is discussed in more detail below.

- 3.10 The state aid regulations are complex and intrinsically related to the financial viability. However, whilst the financial position is less favourable than that projected at gateway 2 this does not preclude meeting state aid requirements. The Council's legal officers are taking expert advice and the scheme will not proceed unless the scheme is state aid compliant. Initial indications are that this should not be an issue.

Financial Projections

- 3.11 The Council's financial advisers have developed a financial model to assess whether TRL and its developments can be established on a viable basis. This model considers the cashflow, tax and accounting implications of TRL's proposed developments and also considers the cashflow and accounting entries impacting the General Fund. It can be used for each scheme on a stand-alone basis to examine whether the viability tests are met.
- 3.12 The model has been refined since the report, TRL is now receiving income that could potentially finance development activity, which could reduce the loan requirement from the Council. As a result, TRL now has a robust model capable of being updated on a regular basis, with current data, as the Belmont Road site is developed out. This will enable up to date progress and financial reports to be produced for TRL and the Council as required.
- 3.13 The inputs and assumptions for Belmont Road have been reviewed and will be subject to continuing review as construction progresses. Key changes are as follows:
- Overall development costs for the Belmont Road scheme have increased since the previous report reflecting continuing price increases in the construction sector.
 - Scenarios with regards to sales and market rent have been tested to ensure the most financially viable option. Prudent assumptions throughout the modelling have been used.
 - Borrowing costs have fallen reflecting current interest rates and interest rate projections.

3.14 Sales Assumptions and Affordable Housing

The financial model currently assumes the market housing will be, initially, rented out for a period of three years to ensure the sales will benefit from house price inflation (a 2.5% increase is assumed per annum). The model then assumes that private units are sold off at approximately four units a month. The sales rate and spread will be monitored to ensure the optimum rate and return for TRL is realised. The model will be kept under review during the construction period to keep other options open, such as the immediate sale of private units.

A narrative summary of the current position is set out below:

Input	Commentary
Tenure Mix	65% of the development will be for market rent/private sale. 35% will be affordable housing a mix of affordable rent (let at 80% of market rent) and shared ownership. No sales are assumed initially.
Construction Programme	1st June 2018 to 1st February 2020.
Land Cost	Independent valuation prior to land transfer.
Construction Costs	Based on employer agent's latest cost estimates and include planning and design costs. Costs have increased since the last report reflecting demand in the construction sector continuing to outstrip supply.
Sales Profile	Over time it is assumed that all market rent properties are sold.
Sales Values & Overall Sales Income	Sales values are based on recent market information and will be uplifted by house price inflation to the sale date.
Rental Income	Rents are based on recent market information. Affordable rents, of which there are 28 units, are set at 80% of current market rents and are in all cases within current Local Housing Allowance figures. They will be uplifted by inflation (CPI – see below) plus 1%, in line with government policy for affordable rents, until the final sale date.
Operating Costs	Management and operating costs reflect the cost of the services provided by the Council to TRL on a full commercial basis. Therefore this arrangement should lead to a small net income within the General Fund resulting from the margin charged on top of direct costs to TRL. Maintenance and lifecycle costs reflect industry norms.
Bad Debts & Void Losses	This reflects a prudent allowance and is informed by the Council's experience of managing its own stock and experience of other providers.
Central running	An annual sum is included to cover accounting, insurance, IT and other central support costs which will

costs	be payable to third parties.
Inflation	Factors general inflation (CPI) and other inflation factors including house price inflation assumptions are based on relevant independent data.
Interest Rates	The interest rate which the Council is assumed to pay on its borrowing reflects the rate that the Council will be borrowing at. Funds on-lent to TRL will attract a margin which is based on current prescribed margins for state aid compliancy.

Financial Parameters

3.15 In looking at the results of the financial modelling, the following underlying principles and parameters were agreed at FBC stage:

- **Impact on General Fund.** Interest payable in the General Fund, as a result of the PWLB loans taken out to provide loans and equity finance to TRL, should be covered by interest receivable from the loans to TRL.
- **Council equity return.** From a commercial perspective the Council needs to be satisfied that best value is generated by investing cash and land within TRL and that the return reflects a position that does not involve the provision of unlawful state aid.
- **TRL financial viability.** TRL will be consolidated into the Council's group accounts and, therefore, the Council must be satisfied of TRL's overall financial position and ability to repay its loans.

3.16 At this position, the financial implications are as follows, taking each parameter in turn:

- The financial model shows that the interest payable by the Council, in respect of loans taken out to fund TRL, will be met from interest payable by TRL to the Council. In summary, this parameter is met.
- The returns which the Belmont Road site can be expected to generate are at the lower end of the acceptable range, reflecting the high cost of developing given the market conditions. However, this is not out of line with market trends. The current development estimates, with an element of contingency included, does meet this parameter. When TRL receives the final tender for the scheme the projected return must meet state aid requirements and this will be a key parameter in relation to approval to proceed.
- The latest projections confirm TRL's financial viability and also that it will be able to operate as a going concern and repay its loan from the Council

based on current known information and assumptions utilised within the model. The final parameter is therefore met.

- 3.17 In summary, when the final financial position is known following receipt of the construction tender, the above three parameters will be re-assessed and all three will need to be satisfied for the scheme to proceed.

4. Reasons for Recommendations

- 4.1 Development of the Belmont Road site will provide quality housing to meet housing needs and improve the lives of Thurrock residents. The development will also contribute to place making and enhancing Grays town centre regeneration. The recommendation in this report is designed to allow there to be no delay to the scheme start.
- 4.2 It is proposed that Council give delegated authority to the S151 Officer, in consultation with the Chief Executive, the Portfolio Holder for Finance and the Leader, to agree the final financial position when the construction tender is submitted but subject to meeting the financial parameters set out in this report.
- 4.3 The estimated cost of construction and thus the level of borrowing that the Council will have to undertake has been analysed and the final figures will be shared as part of the delegated authority process for approval.
- 4.4 TRL will provide an income return to the Council which can support regeneration projects which can meet the aspirations and desires of local people.

5. Consultation (including Overview and Scrutiny, if applicable)

- 5.1 The General Services Committee (cross party) as representatives of the Council (the shareholders) have been kept informed of the progress through the General Meetings of the Company. Planning Committee has granted permission for the scheme following consultation. Resident community consultation has taken place on the site proposals and Property Board has been kept updated as the scheme progressed.

6. Impact on corporate policies, priorities, performance and community impact

- 6.1 TRL will support the Council's place shaping agenda and will help deliver a range of housing tenures and other projects. By enabling TRL to develop quality housing on land that it owns the Council will provide an alternative route to private sector led regeneration which may otherwise be constrained by market conditions. Such housing will contribute to improving, and creating great places where community pride, good health and wellbeing and economic prosperity will thrive.

7. Implications

7.1 Financial

Implications verified by: **Sean Clark**
Director of Finance and IT (S 151 Officer)

The financial model needs to demonstrate any development is both viable for the Company and the Council. It is critical that any authority delegated by Council requires the scheme to meet the financial parameters set out in this report. At its budget meeting in February 2014 the Council agreed that approval for any financial borrowing for the purpose of providing funding for TRL should also be sought at the time of scheme approval and this recommendation has been included in this report. There is also pressure to capitalise the HRA's RTB receipts. The receipts must be spent within three years or they are returned to the Government with interest.

7.2 Legal

Implications verified by: **Assaf Chaudry**
Major Project Lawyer

TRL's activities are within the Council's powers. Assuming Council approve the recommendations in this report, the final position will be checked with external legal advisers to confirm that state aid requirements are met. The legal agreements, including the formal Council guarantee, will be finalised, also with external legal advice, in preparation for signature between the Council and TRL. Approval will constitute a confirmation of the Council's approval of the FBC in the light of the updated circumstances.

7.3 Diversity and Equality

Implications verified by: **Becky Price**
Community Development Officer

Development of the Belmont Road site in Grays will have a positive impact on Grays, in terms of tenure mix. TRL objectives include not only quality housing but also holistic objectives around health and wellbeing, improving education and job creation and improving economic prosperity. TRL's developments will follow Council policies in relation to diversity and equality and, in particular, will ensure that contractors bidding for work from the Company will follow the Council's Equality Codes of Practice on Procurement.

Contractors and developer partners will be required to have relevant policies on equal opportunities, be able to demonstrate commitment to equality and diversity and to supporting local labour initiatives that achieve additional social value.

7.4 **Other implications** (where significant) – i.e. Staff, Health, Sustainability, Crime and Disorder)

None

8. **Background papers used in preparing the report**

- Final Business Case for Commencement of Operations by Gloriana Thurrock Ltd, Cabinet Report, March 2014
- Cabinet Report - Gloriana Thurrock Ltd. - Proposed Development at Belmont Road, Grays, Gateway 2 Report June 2015

9. **Appendices**

None

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