

Name of meeting and date: Cabinet 16th June 2009

Title of report: Fieldhead Regeneration Project – Temporary Borrowing Facilities to Cover Development Funding for Kirklees Community Association

Is it likely to result in spending or saving £250k or more, or to have a significant effect on two or more electoral wards?	Yes. Kirklees Community Association require temporary borrowing facilities of up to £4m to cover cash-flow for the development period of the Fieldhead Regeneration Project. This loan will be repaid, with interest, once Homes & Communities Agency grant has been received and long-term commercial sector borrowing has been secured on the new properties that have been built and on KCA's existing housing stock.
Is it in the Council's Forward Plan?	Yes
Is it eligible for "call in" by Scrutiny?	Yes
Cabinet member portfolio	Adults and Communities Cllr Marchington/Cllr Pandor

Electoral wards affected and ward Councillors consulted:

Birstall and Birkenshaw: Cllrs Smaje, Palfreeman & Light

Public or private: Public

1. Purpose of Report

- 1.1. To request that Cabinet approve borrowing facilities of up to £4m for Kirklees Community Association (KCA) for the development period of the Fieldhead Regeneration Project.

2. Background and Main Issues

2.1. Background

- 2.1.1. Cabinet has previously approved several stages of the Fieldhead Regeneration Project, the last being on 3rd March 2009. In summary the scheme involves the

demolition of 158 flats and the building of 140 2 and 3 bedroom houses, 77 of which will be affordable properties which will be owned by Kirklees Community Association (KCA). KCA have entered into a contract with Keepmoat Ltd to build the properties and significant Housing and Communities Agency (HCA) grant is being secured for the scheme.

- 2.1.2. Summarised, the latest overall costs of the scheme according to the successful bid is as follows:

	£m
Construction	7.8
Fees	0.9
TOTAL	8.7
HCA Grant	3.9
Long term financing raised by KCA on new stock	2.9
Long term financing raised by KCA on existing stock	0.5
Shared Ownership Sales	0.6
Land Receipts	0.8
TOTAL	8.7

- 2.1.3. The overall cost of the scheme to KCA will be £3.4m. This will be raised by long term loans on the new houses when they are built of £2.9m and long term mortgages on KCA's existing housing stock of £0.5m.
- 2.1.4. However whilst the project is under construction, KCA are projected to need up to £4m in temporary borrowing facilities to cover the lowest point of their cash flow, where they have construction costs to pay before HCA grant has been received and new houses have been finished and long term mortgages can be raised on these properties. The figure of £4m does includes contingencies; if the scheme is delivered on time and to budgets the overall amount that KCA needs to borrow is currently projected to be about £3.3m. Allowing for grant payments slipping and extra expenditure costs it is recommended that a maximum of up to £4m is allowed for.
- 2.1.5. Originally KCA intended to raise development funding from the commercial sector and initial negotiations had taken place with the Cooperative Bank, a long term partner of KCA. However the timetable of the successful bidder proposed a much shorter development period for the project which is desirable in terms of quicker project delivery and suits current economic conditions. But it meant that the maximum cash flow requirement during the development wouldn't be viable for KCA through commercial sector borrowing. The cash requirements for the project have also been adversely affected by the 3 month delay in grant being released by the HCA because of their decision to wait for full planning permission to be granted for the scheme, not for the application to be made as they had initially indicated.
- 2.1.6. Kirklees has the authority to approve this loan under its general well-being powers and also under S.24 of the Local Government Act 1988. Legal Services consider that it is only necessary to obtain consent from the DCLG if the power under Section 24 is used although there is some uncertainty on this point. Consequently, as we are already in the process of applying for consent from DCLG for the transfer of the

land it would be prudent to use the Council's power under Section 24 Local Government Act 1988 to enter into the loan and to get DCLG consent for the loan particularly as our informal discussions with DCLG indicate that such a consent would be likely to be forthcoming.

2.1.7. Legal advice from KCA's legal advisors Trowers and Hamlins, who are specialists in the HCA's Affordable Housing grant programme, have advised that although the loan is exempt from classification as state aid because the scheme relates to social housing, the issue of commercial advantage still needs to be considered. It is recommended that KCA be charged a "commercial" rate of interest in order that this borrowing facility could not be challenged as representing an unfair preferential competitive advantage over other providers who would be able to fulfil the same role that KCA is. For this report a "commercial rate" of 5% has been used to estimate the interest costs. Depending on the delivery of the scheme the total value of this interest could be between £100k - £300k. This is about twice as much as Kirklees would receive if they invested the funds through brokers.

2.1.8. Advice from Kirklees Legal Services is that so long as we do not charge a rate of interest less than the EU threshold rate for unsecured loans to a company of the nature of KCA then there is no question of State Aid. If this rate is lower, then State Aid rules apply but the loan will still be lawful so long as an audit trail to show that the subsidy would be no greater than if it had been granted to another provider. It will also be necessary to ensure that the loan agreement stipulates that the loan finance can only be used for the social housing element of the Fieldhead Regeneration Project and cannot be used in anyway to support the cash flow requirements of the private sector housing element.

2.1.9. The following risks have been identified:

- If the project overspends and will require more than the £3.4m from KCA, when completed, including the new stock, KCA will have borrowing capacity of £5.0m so the scheme is comfortably affordable for KCA.
- In the unlikely event that KCA couldn't raise sufficient long term loans, to repay all the 'loan facility' with the Council, any funding shortfall would have to be met from available Housing capital resources
- The development agreement includes an "overage" agreement between KCA and the developer which means that if the private sales properties which the developer will build later in the scheme are sold for more than an agreed amount that this extra value will be split between them. No income from this source has been included in the scheme costs, if any is achieved this will reduce the overall cost of the scheme to KCA.
- As part of the Fieldhead Project the total potential liabilities of KCA to the Council, the Homes & Community Agency and to Keepmoat Ltd will potentially be greater than the assets of KCA. There is therefore a risk that if the Fieldhead Project runs into severe difficulties or fails to be realised then the Council will not be able to recover the loan. This risk has though been mitigated by ensuring that the Council has sufficient controls and influence over the Fieldhead Project. This has been achieved by ensuring that key council personnel are on the Fieldhead Project Board and that Kirklees Neighbourhood Housing are appointed to act as KCA's managing agent on the Project. In addition the Council also has "step-in rights" as part of the Development Agreement with KCA which would

enable it to take remedial action in the event of the Fieldhead Project running into difficulties.

- There will be several key points during the scheme where the scheme will be checked for compliance with the grant agreement and in the unlikely event of a problem due to the other checks in place there will be time for remedy. Any problem would halt the project before all expenditure has been made, therefore reducing potential liability to only being part of the full value of the project.
- Even in the event of a problem with the grant, KCA will have value in the houses completed/partly completed to date by the contractor from which the Council could gain some value in the event of KCA ceasing to exist.
- The loan will be unsecured which means that if the Fieldhead Project runs into difficulties then the Council will not be a preferential creditor. The risk for the Council that this entails has to a certain extent been mitigated by providing that the Council has a right to acquire at nil value the land on the Fieldhead Estate that is earmarked for social housing.

2.2. Previous Approvals

2.2.1. In July 2008, Cabinet authorised the Head of Housing Services to invite tenders for the Fieldhead Regeneration Project. Cabinet also approved progress with the Housing Corporation bid, with a model that included the principle of the Council transferring the Land to KCA at nil cost in order to maximise the amount of social housing delivered.

2.2.2. In December 2008 Cabinet made a number of further approvals:

- agreed discontinuance of the previous EU procurement exercise which the Council were carrying out through KNH and noted the changed procurement method with KCA procuring a developer to work on the Fieldhead Regeneration Project;
- approved the partnership arrangement that KNH will enter into with KCA
- endorsed the contents of the project plan;
- delegated the suspension of lettings for the first phase of the project to the Head of Housing;
- granted authority to the Head of Housing Services to serve a demolition notice (either initial and/or final) as she considers appropriate on those secure tenants of those parts of the Fieldhead Estate that form part of the project;
- Agreed that the Council should enter into a development agreement with KCA to provide for KCA to redevelop the land in the 5 phases of the project; and
- Approved the transfer of the Land, highlighted in Appendix 1 of this report, to KCA at no cost subject to any necessary consents, and being done in a phased manner as each phase of the development is completed was granted.

2.2.3. In March 2009 Cabinet received a further report and approved the following recommendations

- That the transfer of five areas of freehold land shown at Appendix 1 to this report to Kirklees Community Association and/or their nominees at nil cost subject to consent of the Secretary of State be approved.
- That the suspension of lettings, and moving people out from the later phases of properties on the Fieldhead Estate, be delegated to the Head of Housing in line with the decommissioning plan.

- That Council be recommended to approve the making of an application under Section 32 of the Housing Act 1985 to DCLG for the consent to transfer the freehold interest in five areas of land shown in Appendix 1 to this report to Kirklees Community Association ("KCA") and/or their nominees.
- That, subject to full Council approval, the Head Legal Services be authorised to submit an application under Section 32 of the Housing Act 1985 (and any other applications for consent e.g. Section 25 of the Local Government Act 1988) to DCLG for the necessary consent to transfer the freehold interest in the land to KCA.
- That the Head of Legal Services be authorised to execute on behalf of the Council any legal documentation providing for a performance guarantee up to £4 million plus costs in respect of the Kirklees Community Association's ("KCA") use of Social Housing grant and negotiate and execute a deed of indemnity as part of the development agreement whereby KCA agree to indemnify the Council in the event of any losses suffered by reason of the HCA seeking to enforce the performance guarantee.
- That it be noted that the Council is legally empowered to enter into the performance guarantee under Section 2 of the Local Government Act 2000 in that having regard to the Council's Community Strategy it will contribute to promote or improve the economic, social and/or environmental well being of the Council's area.
- That the requirement of the Homes and Communities Agency ("HCA") that the Council enter into the performance guarantee and the fact that Officers consider that the risk exposure to the Council in entering into this performance guarantee has been satisfactorily managed and mitigated so that it is an acceptable liability for the Council to take on in order to ensure that this innovative project is realised be noted.

2.3. Subsequent Changes and Progress

- 2.3.1. Since agreeing to be a partner in the project Kirklees Community Association have already incurred significant costs including specialist legal advice from Trowers and Hamlins (c £100k), consultants costs (c £20k) and have liability for demolition costs of about £100k. However if the project does not proceed for any reason it has been agreed that the Council (more specifically, the Housing Revenue Account) will be liable for the demolition costs, not KCA.

2.4. What Needs to Happen Now

- 2.4.1. Should Cabinet approval be given for the borrowing facility, Strategic Finance in consultation with Group Finance for Strategic Housing and the officer supporting KCA will establish the most appropriate manner to make the borrowing facility work so that KCA has the funds available as and when required but in an efficient manner with minimum interest payable by the charity and in a way which satisfies the EU State Aid rules..

3. Implications for the Council

- 3.1. Risks have been identified elsewhere in this report (2.1.8) and in previous reports. As part of the project the council will provide a performance guarantee to the Homes & Communities Agency in respect of the performance of KCA under the grant Agreement. Legal Services have advised the Council on how to mitigate the

risks that such a guarantee entails. Officers from Development Regeneration, Strategic Housing, KNH, and Strategic Finance are closely supporting and advising KCA in order to mitigate the risk of default under the Grant Agreement.

- 3.2. The Council will make a profit on the borrowing facility to KCA as the returns will be more than the investment returns that Kirklees would normally make on its temporary cash surpluses over short periods.

4. Consultees and Their Opinions

Legal Services

- Legal Services have provided their advice in relation to the position on State Aid. They see no reason why the loan should not be provided. They endorse the position of Strategic Finance which is that the terms of the loan need to be properly documented in a binding loan agreement

Strategic Finance

- The borrowing facility will represent capital expenditure and repayments will represent capital receipts although in the medium term the net cost to the capital programme will be neutral. The borrowing facility will be included in the updated Strategic Housing Capital Plan 2009-14, as part of the overall Council capital plan rollover and 5 year update report , for approval at full Council on 24th June 2009.
- There will be no revenue impact on the council's budget as the interest rates charged will cover administration costs.
- A legal agreement should be drawn up between Kirklees and KCA to formalise the detailed terms and conditions of the borrowing facility.

Ward Members

- Local Ward Members have been consulted. All three local members have responded indicating that they agree with the recommendations of the report. In addition Cllr Smaje has indicated that the borrowing facility should only be used for the Fieldhead Regeneration Project.

5. Officer Recommendations and Reasons

- 5.1. Approve the grant of an unsecured borrowing facility of up to £4m to KCA in order that KCA can continue to work with Kirklees, KNH and the private developer in delivery of social housing as part of the Fieldhead scheme.
- 5.2. Delegate to the Head of Strategic Housing the power to negotiate and finalise the terms of the borrowing facility in consultation with the Strategic Head of Strategic Finance
- 5.3. As a commercial rate of interest will be charged on the borrowing facility, after administration costs have been covered the difference between the return the council would have received on this money and the actual commercial rate should be made available for re-investment in the Fieldhead area.

5.4. Authorise the application of the Head of Legal Services to DCLG for a consent under s.24 of the Local Government Act 1988 for the Council to grant the unsecured borrowing facility to KCA.

5.5. Authorise the Head of Legal Services to negotiate complete and execute the loan agreement between the Council and KCA.

6. Cabinet Portfolio Holder Recommendation

The Cabinet Members agree with the officer recommendations.

7. Next steps

7.1. The borrowing facility will be included in the updated Strategic Housing Capital Plan 2009-14, as part of the overall Council capital plan rollover and 5 year update report, for approval at full Council on 24th June 2009.

7.2. The Head of Legal service will apply to DCLG for consent to provide the loan under s.24 of the Local Government Act 1998.

8. Contact Officer and Relevant Papers

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Report on Fieldhead Regeneration project approved by Cabinet on 30th July 2008.

Report on Fieldhead Regeneration project approved by Cabinet on 17th December 2008

Report on Fieldhead Regeneration project approved by Cabinet on 3rd March 2009

Appendices attached to this report.