

MAIDSTONE BOROUGH COUNCIL

RECORD OF DECISION OF CABINET

Decision Made: 24 January 2024

1,000 Homes Update

Issue for Decision

To note the update provided and seek approval for the Director of Finance, Resources and Business Improvement, in consultation with the Leader of the Council, to enter into a grant funding agreement with Homes England, for the Affordable Homes Programme.

Decision Made

That:

1. The contents of the report be noted.
2. The Director of Finance, Resources and Business Improvement, in consultation with the Leader of the Council, be authorised to enter into "Local Authority Grant Agreement for the Affordable Homes Programme 2021 to 2026", with Homes England as detailed in Appendix 1 to the report.

Reasons for Decision

The Policy & Resources Committee approved the 1,000 Affordable Homes programme in January 2022. The report is the second annual progress report to review the work undertaken to date to deliver upon this key ambition.

The Council's current capital programme proposes considerable investment in housing over the coming years, as follows: -

- 1,000 Affordable Rented Homes £178.2m (net of grant) over 10-yrs.
- 186 Private Rented Sector (PRS) Homes £46.5m over 10-yrs.

Therefore, the Council is aiming to develop and or acquire around 1,186 homes over the next ten years. The main driver is of course the 1,000 Affordable Rented (AR) homes, which was the ambition set out by the Leader of the Council in early 2022. However, the Council was developing PRS homes before this ambition was launched, and the continuation of our investment in this tenure remains important, as it will enable us to achieve cross-subsidy, social cohesion, and risk management at both a project and programme level.

At the time of writing, the Council's housing portfolio comprises:

- Affordable Rented Homes – 29 units

- Temporary Accommodation (MBC owned) – 108 units
- Regulated / General Needs (MBC owned) – 11 units
- Gypsy & Traveller Plots – 32 units
- Private Rented Sector (PRS) (MPH Ltd) – 107 units
- **Total – 277 units**

Furthermore, by 31st March 2024, the 20 flats at Granada House, which are currently PRS, will transfer to become AR Homes, via funding from the Local Authority Housing Fund. Therefore, by the end of the current financial year, the Council's Affordable Rented portfolio will rise (from 29) to 49 units.

The Council continues to invest in Temporary Accommodation (TA), and it is envisaged that by the end of the next financial year (24/25), this portfolio will rise to around 160 units.

This report will assess the progress made to date, and the direction of travel against the following topic areas:

- Staffing
- Project pipeline
- Scheme viability pressures
- Conclusions

Staffing - New Business & Housing Development Team

Over the past two years the New Business & Housing Development team has been created to fulfil the Council's housebuilding ambitions, and is led by Philip Morris, the Head of Service. The team comprises six full time staff and is supplemented with external consultancy support from time to time.

The team is performing well and since its formation, it has secured several new scheme approvals and site acquisitions as set out below. This team also deals with the acquisition and repair of street properties for TA and will soon be starting work on the Private Sector Leasing (PSL) scheme for TA too, but this report will not focus on the TA aspects of their work, but rather the development and acquisition of homes for AR and PRS.

Project Pipeline

The programme secured to date is as follows:

	Affordable	Housing					
	AR	First Homes	PRS	Total	Status	Completion Year	Notes
Trinity Place	23			23	Complete	21/22	Stock tranfer from Hyde Housing
Appledown Grange	4			4	Complete	23/24	Zero SHG - Funded via S106 / Planning Gaine
Lyle Court	2			2	Complete	23/24	Funded by Local Authority Housing Fund
Granada House	20			20	On site	23/24	Funded by Local Authority Housing Fund
Royal British Legion and Heather House	7	4		11	On site	25/26	Cabinet tenure switch approval required
Bathstore	19			19	Acquired	25/26	Contractor procurment near complete
Corben's Yard	24			24	Acquired	25/26	Contractor procurment near complete
Britannia House	28			28	Acquired	25/26	Contractor procurment near complete
Land at Granville Road	12			12	Acquired	25/26	Contractor procurment near complete
Maidstone East	115		102	217	Acquired	26/27 onwards	Planning application submitted
Springfield Library	55		52	107	Acquired	26/27 onwards	Planning application submitted Dec 23
Approved PRS scheme			25	25	Approved	24/25	Approved but due diligence ongoing
Approved AR & PRS scheme	6		7	13	Approved	24/25	Approved but due diligence ongoing
Heathlands AR S106	100			100	Pipeline	28/29 onwards	Pipeline project
	415	4	186	605			

The table above demonstrates that excellent progress has been made towards delivering the overall target of 1,186 homes in the capital programme, inasmuch more than half (603) is credibly in place, with 465 of these homes contractually secured.

The tenure splits for Maidstone East and Springfield Library are indicative at this stage, whilst the Royal British Legion was approved on the basis of 7 PRS units but the intention is to convert these to AR – this scheme also contains 4 First Homes, which are a new form of Affordable Housing where the homes need to be sold at a discount to market value to first time buyers, and held as such in perpetuity. First Homes are a recent addition to the national planning framework, and so it is likely that more future schemes will contain an element of First Homes (in lieu of AR).

Scheme viability pressures and opportunities

The Council has an ambitious housebuilding programme, but as is the case for most housing developers, the present operating is extremely challenging for the following reasons: -

Prior to the pandemic, **construction prices** in the Maidstone area were stable, typically at around £2,250 per m2 of built accommodation (for medium density urban schemes). However, since 2020, construction prices have been gripped by very rapid inflation, driven by a combination of the following; BREXIT and post pandemic supply chain issues, rising build standards in the form of complying with Local Design Guidance (Supplementary Planning Guidance etc), National Space Standards, Nation Design Standards and the phased introduction of the Future Homes Standard (delivered through enhanced Building Regulations). Consequently, the comparable expected m2 build rate is now c £3,500 as we move towards 2024. IE the cost of construction has risen by around 55% in 5 years.

This situation causes a fundamental viability issue for new developments in Maidstone, as sales values of completed schemes are only presently a little higher than this at c £4,000 per m2 (£375 per ft2). This metric is worse for apartments because their communal parts typically add around 20% to the m2, but this element is not saleable.

The Council is just in the process of reviewing the construction tenders received for four schemes (Bathstore, Corben's Yard, Britannia House, & land at Granville Road), where the tender returns are above the construction sums approved on aggregate position. Potentially, this can be offset through higher levels of Social Housing Grant, and any re-approvals to reflect this situation will be sought in due

course.

Therefore, this situation means that on a “residual” basis, there is not much left in the development appraisal to allow for the purchase of land and the associated “on-costs” of development (fees, development finance, CIL / S106 etc), let alone a suitable allowance for developer’s risk. IE whilst schemes can still generate a reasonable Internal Rate of Return (IRR) and Net Present Value (NPV) with the benefit of internal and or external subsidy, the day one, cost / value ratio remains problematic, and realistically the Council continues to “take a view” that gradually increasing house prices over time will resolve this metric.

There are various **house price** forecasters, but Savills are among the most credible. Their latest position is as follows:

	2024	2025	2026	2027	2028	5 years to 2028
UK	-3.0%	3.5%	5.0%	6.5%	5.0%	17.9%
North East	-1.5%	4.5%	5.5%	7.0%	4.5%	21.4%
Wales	-2.0%	4.5%	5.5%	7.0%	5.0%	21.4%
North West	-2.5%	4.5%	5.5%	7.0%	4.5%	20.2%
Scotland	-2.0%	4.0%	5.5%	6.5%	5.0%	20.2%
Yorkshire and The Humber	-2.5%	4.5%	5.5%	7.0%	4.5%	20.2%
West Midlands	-2.0%	4.0%	5.5%	6.5%	5.0%	20.2%
East Midlands	-2.5%	4.0%	5.5%	6.5%	5.0%	19.6%
South West	-3.0%	3.5%	5.0%	6.5%	5.0%	17.9%
South East	-3.5%	3.0%	4.5%	6.5%	5.5%	16.7%
East of England	-3.5%	3.0%	4.5%	6.5%	5.5%	16.7%
London	-4.0%	2.0%	4.0%	6.0%	5.5%	13.9%

Therefore, Savills suggest a small dip for 2024, and steady growth thereafter through the five years to 2028, but this cannot be guaranteed. It does however provide some comfort and confidence when considering schemes for approval with an adverse cost / value ratio.

Furthermore **PRS rents** are rising strongly, and so this will help the viability of PRS schemes as they move towards delivery, and this phenomenon has meant that the government has recently announced in the Autumn Statement that the **Local Housing Allowance (LHA)** will be modestly adjusted upwards, and so this will help the viability for all Affordable Rented schemes as they move towards delivery too, as their rents are at the lower of 80% of the market rent or the LHA.

Turning to **contractor financial stability**, it would not be an understatement to say that 2023 has been the most tumultuous year for contractors serving the residential sector since the fallout of the 2008 crash. There has been an unprecedented number of established firms entering administration, caused by them incurring losses on fixed price contracts, where they have been caught out by inflationary pressures within their supply chains. It is also worth noting that there have also been some high-profile failures amongst Modern Methods of

Construction (MMC) contractors too, to include Ilke Homes, and the fact that Legal & General decided to close their MMC factory this year too.

To clients, such as the Council, this means that we need to be ever more diligent in terms of checking the financial standing of contractors pre award, ensuring Performance Bonds or enhanced retentions are in place, as well as monitoring performance on site closely in terms of both quality and time.

These adverse conditions are even more challenging for SME contractors, and so the Council will need to be extra cautious when considering entering projects with smaller firms, making sure deals are structured skilfully to mitigate the risks. These tactics will be described in specific project approval reports as they come forward.

If a contractor goes into administration mid project, there is the risk of a cost increase through switching contractor, although in theory this can be mitigated by the insistence upon a Performance Bond. Perhaps the larger impact of such failures, especially if it happens on larger schemes, or several schemes concurrently, is **the risk the Council's overall cash flow**, inasmuch there will be sunk costs, but there would inevitably be delays, until the scheme actually becomes income producing. This is arguably more often the more damaging impact on clients.

In terms of **interest rates**, the Council has secured its first tranche of borrowing on very competitive terms, but since then, the cost of borrowing has risen sharply, and most market commentators feel that rates will remain (relatively) high for longer. This is a big risk to the overall programme, inasmuch it may mean that the Council will need to phase the letting of the construction contracts on its larger projects until there is more certainty about what the terms will be on the Council's next tranche of borrowing.

The **volume housebuilders** operating in Maidstone are also facing headwinds with reduced buyer demand compounded by the recent cessation of the government's Help to Buy scheme. Therefore, there will most likely be a fairly steep fall in the number of completions delivered by volume housebuilders in Maidstone over the next 6-12 months. However, this sector tends to focus their delivery on houses rather than apartments, and they are now much more adept at managing their supply of new homes completed to firm buyer orders, than was the case following the 2008 crash. Accordingly, it is not envisaged that that there will be bulk deals available at discounts to the Council as a strategy for further developing our programme, but this will be kept under constant review.

In terms of **Registered Provider (RP) activity**, across Kent there has been evidence of diminished RP activity to acquire S106 stock from housebuilders across some parts of Kent, but to date, this has not been a feature of the RP/S106 market in Maidstone, which remains robust, so there is no need for the Council to step into this space at the present time. However, housebuilders operating in Maidstone are on notice that should the RP appetite wane here, the Council would certainly consider of S106 stock. To recap, the presumption is against the Council operating in this space as it secures the nomination rights to those homes, regardless of whether it owns them or not. More generally, RPs are known to be reducing their development ambitions owing to the following headwinds in their business plans; rising interest rates and costs, as well as the need to address their existing stock in terms of both building safety and its eco

credentials.

Therefore, for all housing developers, the overall viability position has worsened in the past twelve months for most residential projects. Anecdotally, the land market for larger housebuilder type sites, which would feature in the Local Plan/s is subdued. However, this does not seem to have meant that these strategic sites are coming to the market at subdued pricing, moreover, the land market for such sites is characterised by very low volumes of transactions. However, in terms of urban / brownfield / regeneration sites, there are definitely opportunities to buy sites more cheaply than would have been the case 1-2 years ago, and this is where the Council should and continues to focus its acquisition activity. IE the programme table earlier in this report largely comprises such sites.

When the Council launched its 1,000 homes programme, it made the assumption that it would be able to successfully apply to **Homes England (HE) for Social Housing Grant (SHG)** to enable AR rents to be viably charged. Homes England are currently inviting bids for affordable housing schemes that can deliver completions by March 2026. The Council currently has five such schemes that meet this requirement; RBL, Bathstore, Corben's Yard, Britannia House and Land at Granville Road, totalling some 90 homes for AR. The team have worked with the Director of Finance & Business Improvement to set our sought grant rate per home at a level that fully takes into account the challenges presented by the operating environment discussed in this report. With the approval of the S151 Officer, the bid was submitted to Homes England in December 2023 for those five schemes only, and the outcome is expected in January 2024. Assuming that the bid is successful, the Council will need to enter into a "Local Authority Grant Agreement for the Affordable Homes Programme 2021 to 2026" with Homes England, most likely before the end of the financial year. The sample form of contract is provided at Appendix 1 of the report.

In terms of the proposed contract with Homes England, its purpose is to set out the procedures as to how SHG claims should be made and processed, and what are the qualifying expenses against which SHG can be claimed. Homes England is under strict targets for the delivery of Affordable Housing from government, so this pressure is passed on to the recipients of SHG through the contract, in terms of the need to forecast scheme milestones for SHG claims accurately, and then draw down the SHG in a timely manner. Where this is not possible, there are obligations on the claimant to keep Homes England advised of changes to schemes, and ultimately grant can be withheld or re-claimed by Homes England if there are serious contractual or performance breaches, and the recipient is assessed against the agreed targets, and in due course, this performance becomes a consideration as to how successful the claimant is likely to be in future SHG bids. IE Homes England wants to work with the developers of affordable housing that can deliver their programmes to time, cost and quality.

The claimant holds the risk for scheme cost overspends and is responsible for delivering schemes in a manner that is reflective of them being publicly funded, so high standards around the procurement processes utilised, contract administration, health & safety as well as general value for money considerations are enforced. By utilising SHG for the development of affordable homes, the contract then binds claimants to the government's rent setting policy for affordable housing and the general due diligence processes and expectations for new schemes built, through the Homes England Capital Funding Guide.

By way of a summary, the funding and provision of affordable housing is tightly regulated and given the amount of SHG potentially available, once taken it fetters those residential assets in perpetuity, and even if they are disposed of, there remain strict rules as to how the SHG obtained needs to be either recycled into the re-provision of new affordable homes or returned to Homes England. Finally, to reiterate the key consideration, is that when an affordable home is funded through SHG, its valuation will be reduced on the Council's Balance Sheet relative to its previous unfettered market value. Generally, there are two alternative valuation methodologies that the Council will be expected to utilise by its Auditor, being "Existing Use Value - Social Housing" or "Market Value - Subject to Tenancy", with the former being more advantageous than the latter. In theory, the SHG received should largely fill the valuation gap (relative to market value), but if not, the Housing Investment Fund (internal subsidy) referred to elsewhere in the report, will fill the remainder. The terms of the contract available with Homes England are non-negotiable, other than the level of SHG obtained per home which is set via a continuous market engagement bidding process.

Social Housing Grant (SHG) provided by Homes England is intended to plug the income gap (as a capitalised lump sum) to the landlord (Council) between charging a market rent and charging an AR, it has that sole purpose.

The Council also collects monies from developers that can be utilised to help fund our programme. IE **commuted S106 sums for off-site affordable housing** (IE where the developer is not willing to deliver the affordable housing on site). This pot stands at £2.25m with a further £950k due. It is likely that the Council will use these sums as a match fund to Homes England when it applies for SHG.

However, there are **other funding streams** available that are intended to address underlying site viability issues such as demolition, contamination, and exceptional infrastructure cost etc. IE these issues could deem an important or strategic site unviable / undeliverable for any tenure (private or affordable), and it can be possible to secure both types of funding on a given site. An example of this, is where the Council has already been successful in securing Brownfield Land Release Fund (BLRF) monies of £2.1m for Maidstone East and £0.1m for the RBL & Heather House site, from the Department of Levelling Up Housing & Communities. The Council also intends to apply for BLRF monies for Springfield Library in 2024. Similarly, the Council is also engaging with Homes England in respect of their Brownfield, Infrastructure & Land (BIL) Fund, which has a similar purpose to BLRF, but is not restricted just to Councils. This BIL Fund could well be an alternative for Springfield Library.

The Council has secured £80m of borrowing to commence this programme, and it is envisaged that the next five schemes to start on site (RBL & Heather House, Bathstore, Corben's Yard, Britannia House and Land at Granville Road), that will total 94 homes, will have a net cost (after any sale and grant receipts) of around £25m. There are other components of the capital programme, such as the acquisition of TA stock, that will call upon this borrowing too. Accordingly, the Council does not have sufficient borrowing in place to also commit to the construction of both Maidstone East and Springfield Library, it may just be possible to fund only Springfield Library out of the borrowing facilities currently in place.

The Director of Finance and Business Improvement is evaluating the lending market closely, but presumably will only want to make a move once the terms

available become more conducive to long terms residential investment. This topic will be advanced through the regular reporting of the capital programme through 2024 and beyond.

In conclusion, the availability of long-term funding on competitive terms is a headwind to the programme. This situation together with the other various risks and opportunities described in this report means that the Council should “flex” its delivery strategy a little to achieve its overall ambitions as follows: -

Land Banking. The Council should continue to purchase (ideally) large urban sites that are available on reasonable terms at the present time owing to the financial climate and sector specific challenges in the housing development market. Whilst such sites may not have a straightforward path to viability, they can be purchased with site specific holding strategies in mind and brought forward to development once the climate is right coupled with the requisite grant funding package. This approach would tie into broader Council strategies to include the Local Plan Review and the emerging Town Centre Strategy, both of which signal considerable amounts of residential led mixed-use development in and around the town centre, which is unlikely to be taken forward by the private sector in at least the medium term. Obvious locations for land banking activity are on the west side of the river, between Maidstone West Station and the Maidstone East footbridge.

Partnership working. On larger sites that are particularly cash intensive, such as Maidstone East, the Council should look to attract joint venture partners that would be willing to participate in the scheme through the provision of non-affordable rented housing tenures, so market sale, shared ownership and potentially further PRS stock too. This approach could de-risk projects from the Council’s perspective, reduce the cash requirement to deliver them, and improve the long-term social cohesion of the schemes through the provision of increased tenure diversity. Furthermore, partnership working on such sites would enable the delivery to be brought forward faster, and the regeneration impacts of them enjoyed sooner, than if the Council elected to work alone on them.

Housing Investment Fund (HIF). In the previous reports on the 1,000 Homes, the concept of the Council providing internal subsidy for the provision of each affordable home built has been established. IE the costs of provision, coupled with modest SHG and rental levels make this a necessity. The Council’s Medium Term Financial Strategy (MTFS) sets the HIF at £50k per affordable homes built. There are not grounds to adjust this subsidy level at the present time because whilst build costs have increased, this is to some extent offset by lower land prices, a slightly higher rents through the increased LHA, and the (potential for) slightly higher than originally envisaged SHG from Homes England. The biggest variable is possibly the SHG situation, which will become a known once our forthcoming bid is determined in 2024.

Therefore, for business planning purposes, the current level of HIF should remain unchanged at the present time. It will however be reviewed again in the MTFS production for next year, which will be informed by longer-term (50-year) business planning work for the proposed Housing revenue Account (or alternative) that is being undertaken by Finance colleagues together with specialist expert consultancy advice from Altair. Their initial findings and conclusions will be reported in due course through Finance and Corporate Services PAC in the new year and will further scrutinise the financial deliverability

and sustainability of the Council's ambitious house building programmes.

The Council can hold up to 200 affordable homes in its General Fund, but after this it would need to re-open its ring-fenced **Housing Revenue Account** (HRA) (that was closed after the Golding Homes stock transfer). There are some alternatives to the HRA route, and these are all being explored and a report on this topic specifically will come through the Finance and Corporate Services PAC in the new year, which will make a firm proposal as to which approach to adopt.

Alternatives considered and why rejected

To not pursue a "Local Authority Grant Agreement for the Affordable Homes Programme 2021 to 2026" with Homes England.

This option was not selected because, without grant funding from Homes England, the Council's proposed investment in affordable housing would not be financially sustainable.

Background Papers

Affordable Housing Delivery by the Council – [Report to Policy & Resources Committee on 19th January 2022.](#)

1,000 Homes Update – [report to the Communities, Housing & Environment Policy Advisory Committee on 14th March 2023.](#)

I have read and approved the above decision for the reasons (including possible alternative options rejected) as set out above.



Signed: _____
Leader of the Council – Councillor David Burton

Full details of both the report for the decision taken above and any consideration by the relevant Policy Advisory Committee can be found at the following area of the [website](#)

Call-In: Should you be concerned about this decision and wish to call it in, please submit a call-in form signed by any three Members to the Proper Officer by: **5pm on 2 February 2024**