

GWYNEDD COUNCIL CABINET



Date of meeting:	16 February, 2021
Relevant Cabinet Member:	CLlr Craig ab Iago
Contact Officer:	Dafydd Gibbard - Head of Housing and Property Department
Title of Item:	Buy to Let Scheme to let properties for Gwynedd residents

Decision sought

The Cabinet is requested to:

- a) Approve the business case to invest £15.4m to purchase approximately 100 houses to let to Gwynedd residents on an affordable rent with every purchase to demonstrate its own financial viability on a case-by-case basis.
- b) That the Head of Housing and Property in consultation with the Head of Legal Services and the Head of Finance review the statutory arrangements for implementing the Scheme following the publication of revised Government Housing Revenue Account Guidance and report further to Cabinet if additional decisions are needed.

Background

1. At its meeting on 15 December, the Cabinet approved the Housing Action Plan 2020/21 to 2026/27 with the principle of purchasing houses on the market to be rented out for Gwynedd residents.
2. The financial ability to create the Housing Action Plan mainly derives from the decision to establish a Council Tax Premium for second homes. However, the plan also highlights an opportunity to take our aspirations in this field further by means of prudential borrowing in order to fund a purchase of approximately 100 houses to be let out for Gwynedd residents.
3. It was noted in the Cabinet report that the Buy to Let scheme would be subject to a specific report and business case as the scheme is based on prudential borrowing. The purpose of this report is to present the business case for implementing this scheme.

Summary of the need for the Buy to Let Scheme

4. The Housing Action Plan outlines the five challenges we face in the housing field in Gwynedd today and it sets out how we intend to address each of these five challenges. Two of these challenges were "*Ensuring that social housing is available to all who need one*" and that "*Everyone's home in Gwynedd is affordable to them*".
5. In the Housing Action Plan, it was highlighted that the two above challenges derived from the need to address the following in Gwynedd:
 - a. At present, over 2,000 Gwynedd residents have registered for social housing, with high demand in Bangor, Caernarfon, Dolgellau, Llŷn, Porthmadog and Tywyn. The average waiting time before being

offered social housing is consistently over 400 days. There is a lack of one and two bedroom housing stock especially; however the demand is high for all types of dwellings.

b. The latest Local Housing Market Assessment outlines what has emerged in the vast majority of Gwynedd communities today, namely that the average house prices are beyond the reach of the residents of these communities. 59% of Gwynedd residents have been priced out of the local housing market, and the gap between the intermediate income and the income required to be able to borrow a sufficient sum to buy a home in Gwynedd is increasing. In a number of cases, high rent levels restrict people's ability to save enough for a deposit to buy a house.

c. Research on Holiday Homes highlighted that out-of-county demand for housing in Gwynedd influenced house prices but also the supply of housing that is available for local residents, and that over 10% of the county's houses were holiday homes.

6. To summarise, the demand for affordable rented housing is much higher than the housing supply currently available within the county.
7. It was highlighted in the Housing Action Plan that purchasing houses on the market to be let out for local residents could contribute towards addressing this situation.

The Buy to Let Scheme

8. The simple concept of this scheme is to purchase houses on the market when opportunities arise, renovate/upgrade them and then reclaim that investment via rental income over a period of years. Purchasing houses that are currently for sale would be a comparatively swift method of increasing the number of social housing and affordable housing and is one of the measures that could help to increase opportunities for Gwynedd residents to get a house within their community.
9. The economics of the scheme are outlined below with two examples:

Example 1- Buying and Restoring a former social house

10. The following table summarises the financial model to buy and restore one former social house that is on the market today in Gwynedd.
11. Table 1 summarises the costs associated with the purchase and provides a rough estimate of restoration costs based on a desktop assessment of its condition.

Table 1. Purchasing and Restoration Costs

Asking Price	£115,000
Legal Costs	£1,000
Tax (3%)	£3,450
Restoration Costs (including 5% reserve)	£15,750
Total	£135,200
Restoration timetable	6 months

12. The expected annual income is noted in Table 2 below. The annual rent level is based on the social rent level in the area.

Table 2. Expected income

Annual Rent Level (based on the current social rent of the Arfon area)	£5,107 (£98.21/week)
Adjustment for vacant periods	1%

Adjustment for the risk of bad debts	1%
Annual Rent Level after adjusting for vacant periods and bad debts	£5,005
Annual inflation	2%
Annual increase above inflation	0%

13. Table 3 below notes the operational costs associated with maintaining and managing the property. Typical maintenance rates are used. A sum has been reserved for responsive maintenance and statutory work from year 1 onwards. Bearing in mind that we will undertake repair/upgrade work at the beginning, a fund is reserved from year 10 onwards for scheduled maintenance work, namely necessary work when elements of the house come to the end of their useful lifespan. This means that we can protect the asset and extend its useful lifespan for decades to come.
14. In relation to management costs, we will aim to try and collaborate with the Local Housing Associations but we will also assess the financial practicality and viability of delivering this work internally before determining which option offers the best value for the Council.

Table 3. Expected revenue costs

Cyclical and Responsive Maintenance Cost	£450
Management Costs	£500
Total Year 1 Operational Costs	£950
Scheduled Maintenance Cost (Yr 10 onwards)	£1,150
Total Year 10 Operational Costs (inflation not considered)	£2,100
Annual inflation	2%
Annual increase above inflation	1%

15. Therefore, the business case can be summarised in Table 4 below where it can be seen that the expected rent income is more than enough to meet the expected operational costs. Table 4 outlines the annual net expenditure in year 1, 25 and 50:

Table 4. Annual Net Expenditure

Expenditure Heading (adjusted for inflation in accordance with Tables 2 and 3)	Year 1	Year 25	Year 50
Cyclical and Responsive Maintenance Costs	£464	£942	£1,973
Management Costs	£515	£1,047	£2,192
Scheduled Maintenance Costs	£0	£1,887	£3,095
Total Operational Costs	£979	£3,876	£7,260
Rent Income* (*adjusted for vacant periods and bad debts)	£-5,105	-£8,212	-£13,472
Net Expenditure	-£4,126	-£4,336	-£6,212

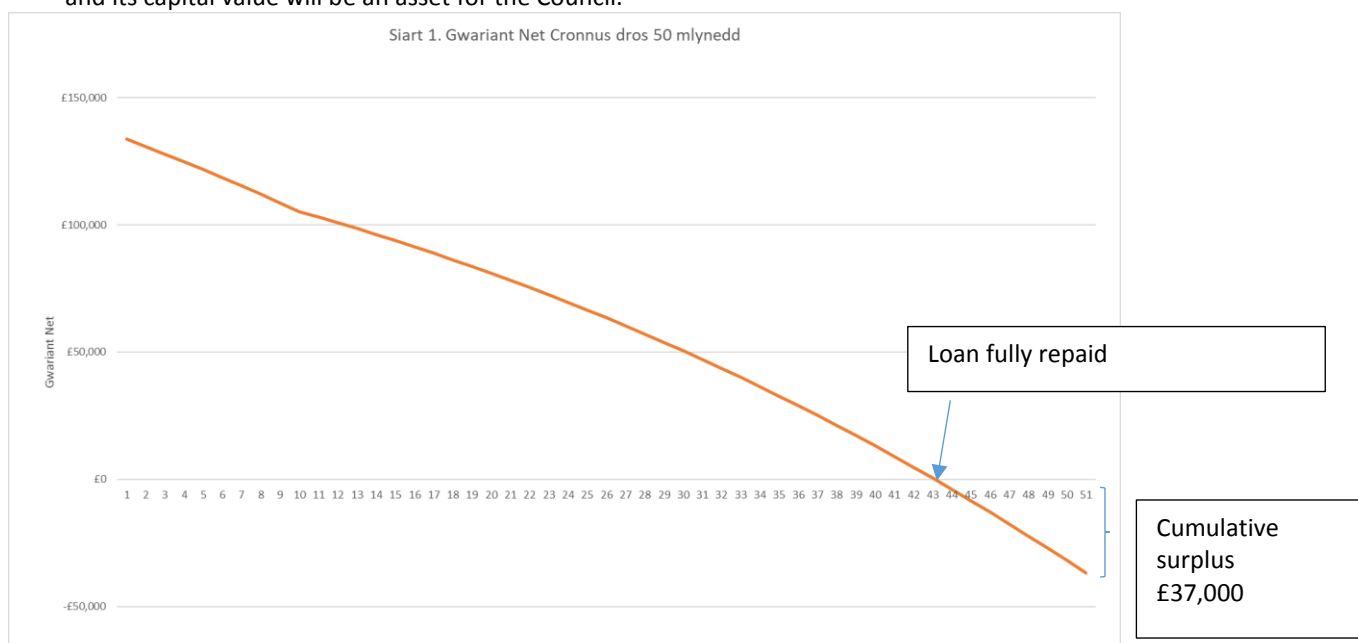
16. Should we fund the investment by borrowing over a 50-year period, namely the period recommended by Welsh Government to repay the housing investment, based on an interest rate of 1.7%, which is available for the Council today, this would lead to borrowing costs of £63,211, or £1,264 per annum. As highlighted in Table 5, there is sufficient surplus to fully cover the loan repayments and interest costs over a 50-year period.

Table 5. Annual position including loan repayment

	Year 1	Year 25	Year 50
Net Expenditure	-£4,126	-£4,336	-£6,212
Premium loan repayment	£2,704	£2,704	£2,704
Interest	£1,264	£1,264	£1,264
Total Repayment Costs	£3,968	£3,968	£3,968
Difference	-£158	-£368	-£2,244

17. Based on the proposed initial investment (Table 1) and the income projections and operational costs in Tables 2 and 3, it is anticipated that we will have finished paying the loan in full in year 43, as highlighted in Chart 1.

18. Therefore, in 43 years the Council would own the asset and benefit from the income for the remaining lifespan of the asset. In year 50 for example, the asset will have generated a cumulative surplus of £37k and its capital value will be an asset for the Council.



Example 2 - House to let for intermediate rent

19. Using the same financial model to evaluate a house for sale on the open market (which is not a former social house), which is suitable to let for intermediate rent (i.e. intermediate rent that is more than social rent but approximately 20% less than open market rent) the following tables summarise the financial projection for such an example:

20. Mostly, a higher asking price can be expected compared to a former social house. A rough estimate of restoration and upgrading costs has been drawn up based on a desktop assessment of its condition.

Table 6. Purchasing and Restoration Costs

Asking Price	£150,000
Legal Costs	£1,000
Tax (3%)	£4,500
Restoration Costs (including 5% reserve)	£15,750
Total	£171,250
Restoration timetable	6 months

21. Table 7 below outlines the expected income. The rent level is based on Local Housing Allowance Rates for north-west Wales. This is probably the minimum level, and the level varies depending on open market levels in different areas.

22. **Table 7.** Expected income

Annual Rent Level (based on North West Wales Local Housing Allowance)	£6,283 (£120.82/week)
Adjustment for vacant periods	1%
Adjustment for the risk of bad debts	1%
Annual Rent Level after adjusting for vacant periods and bad debts	£6,158
Annual inflation	2%
Annual increase above inflation	0%

23. Similar revenue costs are expected for the social model except for scheduled maintenance expenditure. The budget is associated with the value of the property and is, therefore, a higher cost in this case in order to reflect the expectations of tenants given that they would be paying an intermediate rent.

Table 8. Expected revenue costs

Cyclical and Responsive Maintenance Costs	£450
Management Costs	£500
Total Year 1 Operational Costs	£950
Scheduled Maintenance Costs (Yr 10 onwards)	£1,500
Total Year 10 Operational Costs (excluding inflation)	£2,450
Annual inflation	2%
Annual increase above inflation	1%

24. As highlighted in Table 9 below, the expected rent income is more than enough to meet the expected operational costs. Table 9 outlines the annual net expenditure in year 1, 25 and 50:

Table 9. Annual Net Expenditure

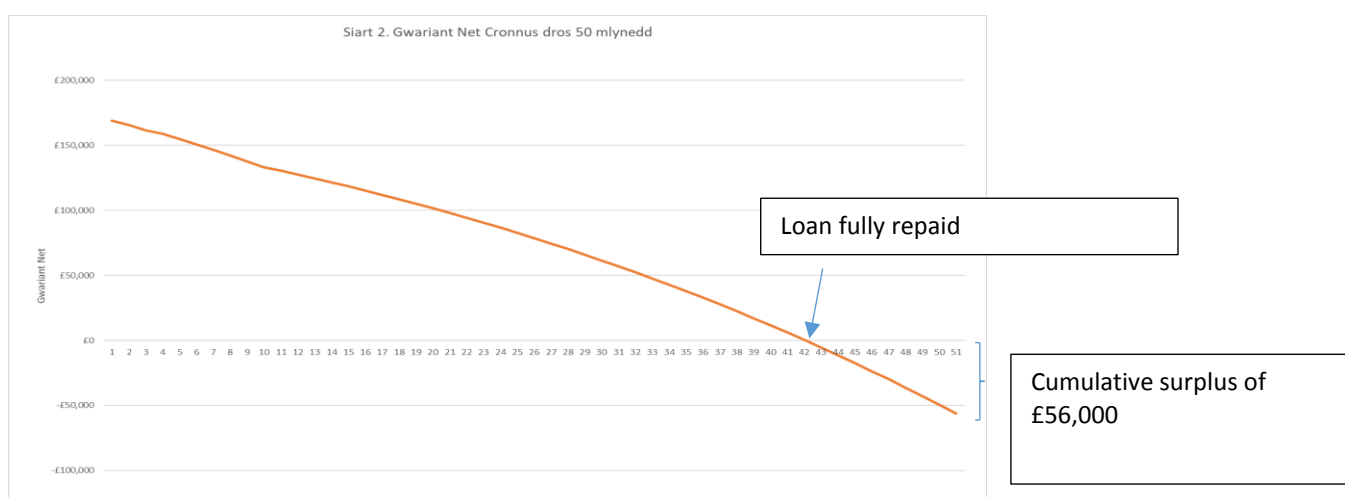
Expenditure Heading (adjusted for inflation in accordance with Tables 2 and 3)	Year 1	Year 25	Year 50
Cyclical and Responsive Maintenance Costs	£464	£942	£1,973
Management Costs	£515	£1,047	£2,192
Scheduled Maintenance Costs	£0	£2,461	£4,037
Total Operational Costs	£979	£4,450	£8,202
Rent Income* (*adjusted for vacant periods and bad debts)	-£6,281	-£10,102	-£16,574
Net Expenditure	-£5,302	-£5,652	-£8,372

25. Should we fund the investment by borrowing over a 50-year period, based on an interest rate of 1.7%, which is available for the Council today, this would lead to borrowing costs of £80,065, or £1,601 per annum. As highlighted in Table 10, there is sufficient surplus to fully cover the loan repayments and interest costs over a 50-year period.

Table 10. Annual position including loan repayment

	Year 1	Year 25	Year 50
Net Expenditure	-£5,302	-£5,652	-£8,372
Premium loan repayment	£3,425	£3,425	£3,425
Interest	£1,601	£1,601	£1,601
Total Repayment Costs	£5,026	£5,026	£5,026
Difference	-£276	-£626	-£3,346

26. Based on the proposed initial investment (Table 6) and the income projections and operational costs in Tables 7 and 8, it is anticipated that we will have finished paying the loan in full in year 42, as highlighted in Chart 2.
27. Therefore, in 42 years the Council would own the asset and benefit from the income for the remaining lifespan of the asset. In year 50 for example, the asset will have generated a cumulative surplus of £56,000 and its capital value will be an asset for the Council.



28. Naturally, the exact investment required to purchase and restore houses will vary over time and it will depend on their location and their general condition. Similarly, rent levels will vary depending on the size and use of the property, with more flexibility in terms of intermediate rent levels than social rents.
29. Therefore, it stands to reason that the business case will vary for each property and it is inevitable that every investment will need to be considered individually and on a case-by-case basis. Therefore, it is proposed that every purchase demonstrates its own financial viability and repays the original investment within 50 years as illustrated in example 1 and 2 of this report.
30. Some business cases will be better than others and focus can be placed on the best business cases and locations where there is clear evidence of a demand for such housing. However, cases can arise where there will be a need to address a specific need or demand in an area and house prices in that particular area could be beyond the reach of the business case presented in this report. As house prices are currently increasing yet again, it is also possible that this will lead to pushing the original investment beyond the amounts that we currently have under consideration.
31. If no other viable solution is available, it is possible that there will be a need to consider using the resources of the Housing Action Plan to support the scheme under such circumstances. Currently, the funding that will be available during the lifespan of this Scheme has already been earmarked in order to

implement other schemes. However, should additional funding become available, e.g. from grants, underspending on other schemes or higher income from the Council tax premium, then establishing a fund could be considered to meet the restoration and upgrading costs associated with this Buy to Let scheme. This would enable the repayment of the initial investment in a shorter period or allow houses of a higher value to be purchased, should the need arise. Any such changes to the business case presented in this report would be the subject of a further report to the Cabinet in future.

32. In Table 11 below, the proposed investment profile is noted in order to deliver the ambition set out in the Housing Action Plan, namely purchasing approximately 100 houses to let.

Table 11. Proposed investment profile:

2021/22	2022/23	2023/24	2024/25	2025/26	2026/27	Total
£1m	£2.88m	£2.88m	£2.88m	£2.88m	£2.88m	£15.4m

Legal Rights

33. Section 9 of the Housing Act 1985 gives the Council, as the "Housing authority" the power to provide housing by procuring land for construction, to construct and purchase houses. This is the legal power we will use in relation to social housing.
34. This power is specifically linked to a Housing Revenue Account, and the Welsh Government is currently reviewing guidance on Councils' rights to buy and build without reopening a Revenue Account. Discussions on this will continue with the Government and if it changes, then we will need to consider the impact of any new guidance in the context of these plans. Following the Gwynedd Stock Transfer to Gwynedd Community Homes (Adra) a direction was made by the Welsh Government to formally close the Gwynedd Housing Revenue Account in accordance with the provisions of Section 74 of the Local Government and Housing Act 1989. In summary guidance was given by the Government at the time it would be possible for the Council to hold up to 50 houses provided under Section 9 omitting a need to re-establish a Housing revenue account.
35. We have received expert legal opinion which states that the provision of intermediate housing can be approached through the use of alternative powers to the Housing Act 1985 to achieve the aim of providing intermediate housing, at present it is recommended that a general power of well-being be used under Part 2 of the Local Government Act 2000 to buy houses for intermediate rent.
36. However the Local Government and Elections (Wales) Act 2021 has now received Royal approval. Part 2 of the Act when it comes into force gives the Council a general power of competence which will replace the general well-being power. In this context change will not specifically affect the objectives and may work in favour of the authority. However, it is appropriate to draw attention to the proposed statutory change that comes into effect during the Scheme's implementation period.
37. As recognized in the Welsh Government's statutory guidance on the use of the general well-being power, a plan to provide good quality affordable housing is a key factor in improving well-being and states that "the breadth of the well-being power means local power to rely on it as a 'power of choice' if there is any doubt as to whether the existing powers would enable them to take certain actions or deliver a particular service. "Furthermore, the guidance also states that local authorities should" look r the well-being power in the first instance in taking forward measures likely to promote and improve well-being ". However, it must also be noted that these powers are subject to any existing statutory restrictions. The expert advice states that the use of these powers needs careful justification rather than Section 9 of the Housing Act. The Government is currently consulting on new guidance on the Housing Revenue Account and it is understood that there is an intention to allow a Council to provide up to a total of 200 houses outside the Housing Revenue Account regime. There is no specific guidance on the general power of competence in Wales at present but there must be a real need to revisit the exact delivery mechanism of this project as this situation develops and is clarified.

Housing allocation policy

38. The allocation of social housing will comply with the current Common Lettings Policy but there will be a need to establish a new policy to allocate intermediate housing, in accordance with the requirement in Section 167 of the Housing Act 1996.
39. It is anticipated that this lettings policy will follow the same principles as the Common Lettings Policy, namely prioritising a local connection along with the need for a house. Also, such policies are already being implemented in Gwynedd under the Tai Teg banner.
40. Prior to determining the most suitable lettings policy for intermediate rented housing, a further report will be submitted to the Cabinet for consideration following a further consultation.

Risks and other considerations

41. Delivering such a scheme will not be without its risks of course but in terms of financial risks, the main risks to the Council are managed by the fact that every purchase will be considered individually within the framework set in this report.
42. The main risks to the Buy to Let Scheme are identified as follows:
 - ❖ Increase in interest rates affecting the viability of business cases.
 - ❖ Failure to let the houses / higher vacant periods affecting the income received
 - ❖ Failure to meet Wales Housing Quality Standards
 - ❖ New legislation / regulations affecting the viability of business cases
 - ❖ Increase in house prices
 - ❖ Increase in construction costs
 - ❖ A lack of housing supply coming onto the market
43. There is also a combined risk should a number of the above risks become reality. However, the fact that we will be drawing up an individual business case for every purchase means that any financial risk to the Council will be low as we would not continue with the investment if the business case was not viable at the time.

Conclusions

44. By implementing this scheme successfully, at the end of the 6-year period of our Housing Action Plan, the Council will own approximately 100 houses that will be available to let for local residents.
45. At the end of the original loan repayment period, the Council will remain the owner of these assets and will continue to reap an annual rent income.
46. If we conclude that the scheme is working freely, then consideration can be given to increase the number of houses we will purchase. On the other hand, if circumstances change and we come across obstacles than cannot currently be anticipated, then the fact that we will assess the financial viability of every purchase, on a case by case basis, means that we would not continue with the investment unless the purchase corresponds with the principles highlighted in this business case. Either way, such a change would lead to a further report to the Cabinet.

Views of the Local Member: Not a local matter

Views of the Statutory Officers:

The Monitoring Officer:

The report refers to the legal considerations which relate to the proposed Plan. I note that there is need to develop further work when the revised guidance from the Government in relation to Housing Revenue

Account. This is a matter which can be reviewed as the Plan moves forward but we need to be prepared to give it further attention as part of the development of our arrangements.

Statutory Finance Officer:

I have worked with the author in developing the 'Buy to Let' model and confirm the facts as presented in the report.

This model is dependent on a number of assumptions, and its financial success requires the factors to match our assumptions. However, in order to ensure that social housing is available to the residents of Gwynedd, as the report admits in paragraph 31, it may be necessary to use an element of the Housing Action Fund's resources.

The main risks of the 'Lettings Purchase Scheme' are set out in paragraphs 41 - 43 of the report: risk of a financial blow from interest rate rises or vacancies, and other risks (such as house price increases) would impede progress, as the purchase of each individual property will be subject to a viable business case.

The houses would be purchased under Part 9 of the Housing Act 1985, which allows the Council to hold up to 50 houses without re-establishing a Housing Revenue Account. There would be prohibitive costs associated with running a Housing Revenue Account, so the Council's ability to buy and let 100 houses (over 6 years) will be subject to new regulations (see paragraph 37 of the report)