

<b>Item No.</b>	<b>Classification:</b> Open	<b>Date:</b> October 20 2009	<b>Meeting Name:</b> Executive
<b>Report title:</b>		Aylesbury Regeneration – Phases 2 and 3	
<b>Ward(s) or groups affected:</b>		Faraday	
<b>From:</b>		Strategic Director Regeneration and Neighbourhoods	

## RECOMMENDATIONS

That the Executive:

1. Note the success of the first stage of the bidding process.
2. Approve the preparation of an Interim Outline Business Case (OBC) for a Private Finance Initiative (PFI) scheme for phases 2 and 3 of the Aylesbury Regeneration programme.
3. Requests officers to report back following the Interim Outline Business Case and advise further on the detailed options appraisal and preferred approach for delivery.

## BACKGROUND INFORMATION

4. In September 2005 the council agreed to a redevelopment strategy for Aylesbury. Summary information about the overall progress of the scheme is contained in Annex A.
5. In seeking public sector funding, the council was directed to the then emerging Homes and Communities Agency as a potential funding source and the HCA directed the council to consider the 6th bidding round for PFI.
6. In October 2008, the council submitted an expression of Interest for Housing Revenue Account (HRA) Private Finance (PFI) credits to the Department for Communities and Local Government in partial support of delivering Aylesbury phases 2 and 3. The application received cross party support.
7. This application was been successful; a government announcement was made on July 17 2009 confirming Southwark as the only London authority to be invited to receive a preliminary award of credits and to prepare an Outline Business Case (OBC).
8. The HCA PFI team attended a meeting with the council team on September 8 2009 to welcome the council to the 6th round of PFI schemes and to emphasise areas of specific interest. These are set out in paragraph 13-15.
9. This report to the Executive is submitted in order to support the progress of phases 2 and 3 and should be read in conjunction with a separate report to the October 20 Executive on phase 1.

## Scope of the Phase 2 and 3

10. Phases 2 and 3 currently comprise 1100 homes. Property details are listed at the redeveloped scheme will comprise 1094 mixed tenure homes and strategic and social infrastructure. The key elements of each phase are summarised as follows:

Phase 2	<ul style="list-style-type: none"> <li>• 645 new homes (241 rental, 81 intermediate, 322 for sale)</li> <li>• Surrey Square Gardens</li> <li>• A section of the community spine</li> <li>• A section of Albany Road</li> </ul>
Site 3	<ul style="list-style-type: none"> <li>• 450 new homes (169 rental, 57 intermediate, 224 for sale)</li> <li>• East Street Triangle</li> </ul>

**Table 1 – Key Elements of Phases 2 and 3**

**About Private Finance Initiative (PFI)**

11. The project will be delivered within the council's HRA using the PFI credits, using council owned land and an obligation on the council to acquire the existing leasehold interests. It is assumed that the project will have a 30 year term commencing in 2013/14. At the end of the PFI contract the rented homes will become under the council's ownership.
12. The PFI credits support the cost of demolition of all properties. Additionally they support the design, build, finance and maintenance and management of social rented homes and supporting infrastructure.
13. The PFI provider will be responsible for management, maintenance and community safety of properties prior to the demolition at the start of the PFI contract (although the re-housing process will have already commenced).
14. It should be noted that the cost of leasehold acquisitions which is substantial, is specifically excluded from PFI.

**Outline Business Case and Procurement of PFI provider**

15. The PFI procurement process is heavily prescribed, however there are two clear stages.
  - The preparation of an Outline Business Case. This is anticipated to take approximately 15 -18 months.
  - The second stage is the procurement which culminates with the award of the contract. This is anticipated to take approximately 3 years.

**Interim Outline Business Case**

16. The HCA PFI team attended a meeting with the council team on September 8 2009. The team consider that the Aylesbury scheme presents exceptional funding challenges and has a particularly high unit cost. The PFI team has requested that council officers revisit costs and technical assumptions e.g. unit size, sustainability requirements.
17. In light of the above they wish to introduce an interim OBC stage to address key challenges. It is anticipated that this will be concluded within approximately 9 months.
18. The HCA require that the interim OBC addresses the following;
  - An options appraisal which considers alternative routes to HRA PFI to achieve Aylesbury's regeneration e.g. land disposal, stock transfer, National Affordable Homes Programme and should also specifically consider whether a non-HRA PFI could be delivered at a lower overall cost

- A market assessment of whether the PFI programme can achieve the private sales envisaged in the Expression of Interest
- Soft market testing to assess the overall developer interest
- Soft market testing to assess the extent to which private finance will be available
- LBS capacity and commitment to underwrite costs in four key areas; leaseholder acquisitions, procurement, unitary charge, cross subsidy

19. It should be noted that the information above has been prioritised by the HCA for the interim OBC. It is not additional to the information usually required to be included in an OBC.
20. It is clearly of vital importance that the HCA and the council are satisfied with the outcome of the interim OBC before proceed to full OBC.
21. Representations are being made to the HCA that the preparation of the interim OBC start in November 2009, i.e. that the interim OBC be completed in June 2010.

### **Cost and Funding Sources**

22. There are significant upfront costs to be borne by the council. These are principally the costs of achieving vacant possession and cost of OBC and procurement, a unitary charge subsidy for the 30 years term of the contract. It is recognised that a scheme of this scope and scale will have a significant impact on the council's HRA. The costs are very early estimates and will be fully tested as part of the OBC process.
23. Concurrent with the preparation of the interim OBC will be identification of funding sources to meet the above costs.

### **PFI team and governance**

24. To achieve the interim OBC, the council will implement a project management structure which supports effective project delivery and governance, and will incorporate as appropriate:
  - A PFI Project Team, led by the PFI Project Director, and also comprising representatives of each of the key professional disciplines including property, planning, housing, finance, procurement and legal
  - An Aylesbury Project Board, comprising both council members and executive officers. The Board will act as the principal governance body for the Aylesbury PFI project, providing a key link between the Project Director (and Project Team) and the Council's Executive.
  - Lessons learned from other council PFI schemes i.e. Southwark Schools for the Future, Waste PFI and from EU competitive dialogue i.e. Southwark Schools for the Future and Aylesbury phase 1a.

### **RISK MANAGEMENT**

25. The council has already procured major capital investment through the use of PFI in waste management and through the BSF programme and has a good understanding of the capacity of the private sector to accept risk.

<b>Risks</b>	<b>Mitigations</b>
Abortive expenditure on fees for managing Interim OBC	Ensure regular on-going dialogue with the HCA's PFI team to ensure that key

Risks	Mitigations
	issues and risks are shared and managed as they arise in order that the Interim OBC process facilitates the identification of major challenges and avoids potentially abortive works. One of the objectives of the Interim OBC to provide a robust analysis at the earliest possible stage as to the deliverability of the scheme from

**Table 4 - Key risks and mitigations**

## **TIMETABLE**

26. An indicative timetable is shown in table 4

Major milestones	Indicative Date
Submit Expression of Interest	October 2008
CLG Invited to Develop OBC	July 2009
Executive	October 2009
Submit Interim OBC	June 2010
Submit OBC	December 2010 - March 2011
Commence EU procurement of PFI provider (competitive dialogue)	Early 2011
Complete procurement/Financial Close	End 2013

**Table 5 – Indicative Timetable for selection of PFI provider**

## **POLICY IMPLICATIONS**

### **Planning Policy**

27. The council is preparing an area action plan (AAP) for the Aylesbury estate and surrounding area. Preparation of the AAP is at an advanced stage and the council is aiming to adopt the plan in January 2010. Together with the Core Strategy, the AAP will replace the Southwark Plan and all future planning applications will be assessed against these documents. The quantum of units set out in paragraph 7 and the approach to delivery using PFI is consistent with the strategy outlined in the emerging AAP and Core Strategy

### **Housing Strategy**

28. The regeneration of the Aylesbury Estate is a key strategic housing priority both in terms of the new high quality housing to be delivered, and the reduced long term impact on the Housing Investment Programme. The new housing will contribute to the affordable and overall London Plan housing targets for new housing development in the Mayor's Housing Strategy. The project proposals are also supportive of the Southwark Housing Strategy. The phased re-provision strategy for the rental homes will also ensure that the size and mix are meeting specific identified housing needs.

### **Property**

29. The proposal will give rise to a number of property implications that will arise if this

route is followed. This will emerge and be reported upon fully at the appropriate stage.

30. As mentioned, it will be necessary to provide vacant possession of the site in order for the proposal to proceed and will necessitate the acquisition of residential leasehold interests and some business leases [e.g. in Taplow]. Ultimately, to achieve this, it is anticipated that compulsory purchase powers will be needed. Section 226 of the Town & Country Planning Act 1990 appears to be the most appropriate enabling legislation. This provision enables land to be assembled for redevelopment. To achieve an Order there is a prescribed process to be followed. The initial step is for Executive to pass a resolution to make an Order. A report in pursuance of this will be made at the appropriate time setting out the full rationale for the Order. Generally speaking, this should be made once a development partner has been selected and can demonstrate funding to achieve the purpose of the Order. In the meantime however voluntary negotiations are taking place with leaseholders with compulsory powers in the background; this means they are offered the same terms that they would receive if there was an operative Order.
31. The land and buildings in this phase are held by the council for housing purposes. The council is enabled by s32 of the Housing Act 1985 to dispose of land held for housing purposes. This authority is however subject to restrictions that are set out in the concurrent of the Strategic Director of Communities, Law & Governance.
32. Reference has been made in this report to the cost of acquiring leasehold interests. The estimated cost is based on current values. As has been well documented, there has been a substantial fall in property market activity and values in the past eighteen months. The regeneration of this phase is a long term project and it is likely that property market activity and values will change considerably over the duration of the project. This could result in substantial changes to the cost of acquiring leasehold interests. Since such changes cannot be predicted with any confidence current value levels have been used in making the estimate but it needs to be recognised that these may change radically over the lifetime of the project.

### **Financial**

33. The development of the Aylesbury Estate phases 2 and 3 including a PFI scheme represent large financial challenges for the council.
34. Where expenditure cannot be defrayed by the use of existing resources, it will where possible need to be resourced from external resources that have been earmarked for that purpose. Where this is not possible exploration of other external funding sources and testing of the assumptions sitting behind costs will need to be undertaken by financial advisors and the project team to establish how such costs can be resourced and what action can be taken to reduce the level, improving affordability.
35. The council is already undertaking diligent analysis of assumptions, options, cost levels, funding sources in order to identify affordability issues as early as possible so that mitigating action can be taken.

### **VAT implications**

36. The area of VAT implications for the Aylesbury scheme is complex and work is being undertaken to assess the VAT implications in this case, specialist advice will be sought as required to mitigate the risk of sub-optimal decisions being made with regard to VAT from the council's perspective.

37. The key issues for the council are:

- Assessing what implications the development of the Aylesbury estate with a PFI element has for the council's VAT exemptions limit.
- Ensuring appropriate classification of the eventual overall housing supplies as either statutory landlord ones (non-business) or business supplies. In the former case recovery of VAT incurred is possible and the council would seek to undertake this wherever it is appropriate to do so.
- Local Authorities can also elect to Opt to Tax (OTT) supplies in certain instances. This arrangement permits recovery of VAT incurred on costs based on levying VAT charges on sales to purchasers. The council would explore this option where appropriate.

### **Legal Implications**

38. All legal implications are included in comments from the Strategic Director of Communities, Law & Governance.

### **Consultation**

39. Prior to starting work on the AAP, the council prepared an overarching consultation strategy to guide the overall approach to consultation on the AAP. All consultation carried out on the AAP has been consistent with this strategy and also with the requirements of the Statement of Community Involvement (SCI). Details of consultation undertaken are set out in the Aylesbury AAP consultation report.

40. The successful partners will be required to work within the Aylesbury consultation strategy including working with a design team comprising of officers and residents. The partners will also be required to undertake a series of wider public consultation exercises with Aylesbury residents during the development of the scheme.

### **Community Impact Statement**

41. There are no implications arising from the preparation of the interim Outline Business Case at this time.

## **SUPPLEMENTARY ADVICE FROM OTHER OFFICERS**

### **Strategic Director of Communities, Law & Governance**

42. This report seeks to obtain approval to the preparation of an Outline Business Case (OBC) and as such there are no legal issues arising. A team of lawyers from Communities, Law and Governance are advising on this regeneration and will continue to assist during the PFI scheme.

43. It is noted at paragraph 31 that the land and buildings held in these phases is held by the council for housing purposes under Part II of the Housing Act 1985 and may therefore be disposed of pursuant to the disposal power contained at section 32 of that Act. However, section 32 disposals require the express consent of the Secretary of State (unless they fall within a general consent e.g. are for the best consideration that can reasonably be obtained) and the council's constitution requires applications to the Secretary of State for the disposal of housing land be approved by Council Assembly. An alternative would be to appropriate the land

for planning purposes and use the disposal power contained in section 233 of the Town and Country Planning Act 1990, which provides that disposals may be made in such a manner and subject to such conditions as appear to be expedient in order to secure the best use of that land or to secure the carrying out of works needed for the proper planning of that area. Should the disposal consideration be less than the best consideration for that particular type of development, Secretary of State consent to the disposal will still be required, but an application for Secretary of State consent can be made without Council Assembly approval. A further advantage of appropriating the land for planning purposes is that any private rights affecting the development (e.g. rights of way, rights of light) will be overridden (section 237 Town and Country Planning Act). However, appropriation of housing land may have an adverse impact on the Housing Revenue Account and this will need to be quantified before the disposal strategy is fixed.

## **Finance Director**

44. This report is seeking Executive approval to:
  - Note the success of the first stage of the PFI bidding process
  - Approve the preparation of an Interim Outline Business Case (OBC) for a Private Finance Initiative (PFI) scheme for phases 2 and 3 of the Aylesbury Regeneration programme.
  - Receive a detailed options appraisal as part of the Interim OBC in June 2010.
  - Agree funding for the production of the Interim OBC.
45. The Finance Director notes from paragraph 3 and 4 that the increased application for £180.25m PFI credits was successful and that a government announcement was made on July 17 2009 confirming a preliminary award of credits and to prepare an Outline Business Case.
46. The Finance Director acknowledges the proposal for a PFI scheme within the Housing Revenue Account, having an intended contractual term of 30 years commencing in 2013/14, with the units reverting to council ownership at the end of the contractual term. It is noted that the PFI credits support the cost of demolishing units, but specifically not the cost of acquiring leaseholder interests in order to commence the scheme. Alternative funding for these acquisition costs, and other infrastructure costs not met by PFI will have to be identified.
47. The two stages of the PFI procurement process outlined in paragraphs 15 and 30-33 are noted, with the sources for cost estimates being prior experience of similarly sized schemes and advice from the HCA.
48. Indicative funding for the production of the Outline Business Case (OBC) has been identified. Work will be needed by the project team and in conjunction with advisors and the HCA going forward to evaluate and monitor the cost of OBC production and to ensure that the funding sources identified for this purpose can be used to defray the cost to the level and at the time required.
49. Identification of such funding will be an important requirement to progressing successfully since funding at an appropriate level is required to ensure that the project team is sufficiently resourced to manage risk and complete the heavily prescribed procurement.
50. The Finance Director notes the proposed contents of the Interim OBC and that the information outlined in paragraph 18 has been prioritised by the Homes and Communities Agency. It is acknowledged that progressing to full OBC is

contingent upon acceptance by the HCA of the Interim OBC. The cost of preparing the Interim OBC is noted, however since this is the first time the Council has undertaken this stage diligent assessment and monitoring of the required tasks and costs will be needed to ensure that an appropriate cost of production is achieved.

51. The report highlights the fact that there are significant up-front costs to be borne by the council in order for this scheme to be successful.
52. Whilst the expenditure requirements have been outlined detailed analysis of these requirements will need to be undertaken as part of the completion of the Interim OBC with the intentions of reducing the impact of the costs where possible and concurrently identifying funding sources to defray them.
53. The estimated financial impact in relation to the PFI represents a very significant financial challenge to the council and will require continual re-examination moving forward.
54. The proposed PFI project management structure is seen. Establishment of the correct team will be crucial to the successful progression of the scheme and for the effective identification, management and mitigation of risks such as those detailed in table 4. The in-house project team will need to be sure that the funding sources can be identified to meet the cost of the project management team for the implementation period.
55. There are significant financial risks detailed in table 4. The project team will need, in conjunction with consultants to proactively and diligently address each risk in order to prevent a risk leading to the failure of the scheme. In particular those risks resulting from non-existence of funding sources and/or reliance on phased funding receipts must be fully analysed and understood since such could potentially lead to the council facing serious financial pressure and/or delay the progression of the phases.
56. The indicative timetable at paragraph 26 is acknowledged. This timetable is heavily prescribed and given the long lead in period sufficient understanding should be achieved by the project team in order to cope with changes or delays and the effect on resource implications fully understood. Robust scoping of cost incurrence and resource availability should be undertaken to mitigate any potentially negative effects to the council of timetable delays, or changes in cost and funding profiles.

## **BACKGROUND DOCUMENTS**

<b>Background Papers</b>	<b>Held By</b>	<b>Contact</b>
Aylesbury Area Action Plan	Planning Policy Team	Tim Cutts 020 7525 5380
Aylesbury Estate Regeneration Phases 2 and 3 - Application for provisional Communities and Local Government support for HRA PFI projects	Aylesbury Regeneration Team	Silvera Williams 020 7525 4806



## APPENDICES

No.	Title
1	Phase 2 and 3 property details

## AUDIT TRAIL

<b>Lead Officer</b>	Richard Rawes, Strategic Director of Regeneration and Neighbourhoods		
<b>Report Author</b>	Adeola Dada, Aylesbury Assistant Project Director		
<b>Version</b>	Final		
<b>Dated</b>	October 12 2009		
<b>Key Decision?</b>	Yes	<b>If yes, date appeared on forward plan</b>	June 2009
<b>CONSULTATION WITH OTHER OFFICERS / DIRECTORATES / EXECUTIVE MEMBER</b>			
<b>Officer Title</b>	<b>Comments Sought</b>	<b>Comments included</b>	
Strategic Director, Communities, Law & Governance	Yes	Yes	
Finance Director	Yes	Yes	
Strategic Director of Environment and Housing	Yes	Yes	
Executive Member for Regeneration	Yes	Yes	
Executive Member for Housing	Yes	Yes	
Executive Member for Resources	Yes	Yes	
<b>Date final report sent to Constitutional Support Services</b>			

## Appendix 1 - Property details

Phase 2	Tenanted	L/H	Total
Wendover 241 – 471	198	39	237
Foxcote	19	11	30
Padbury	16	9	25
Ravenstone	68	13	81
Winslow	21	9	30
Wolverton 152-192	32	9	41
Phase Total	354	90	444
Phase 3			
Wendover 37-72, 117-156, 201-240	101	15	116
Wolverton 126-151	21	5	26
Brockley House	12	3	15
Wendover 1-36, 73-116, 157-200	110	14	124
Wolverton 60-125	51	15	66
East Street	10	2	12
Northchurch	62	20	82
Taplow	191	24	215
Phase total	558	98	656
<b>Grand total</b>	<b>912</b>	<b>188</b>	<b>1100</b>

### Existing property details

The development proposals for the PFI project area are summarised in the following table. Properties will be developed in a range of sizes and types to meet the needs of later phase tenants and the housing market. Associated infrastructure including parking, although at reduced levels, is included. Infrastructure quality is a high priority for the council and residents.

	Rental	Intermediate	Sale	Total
Phase 2	241	81	322	645
Phase 3	169	57	224	450
Total	410	138	546	1094

### Proposed property details

The rental homes will range in size from one to five bedrooms, in a mix of houses, maisonettes and flats. Flats and maisonettes will be located in blocks of six to ten storeys. The breakdown of types is as follows:

Type	Number
Houses	124
Maisonettes	91
Flats	195
Total no. units	410
Total no. habitable rooms	1,534

### Proposed housing types