

# Financial Appraisal Report - PUBLIC

HRA Capital Project – Construction of new affordable homes at West End Avenue, Smethwick and submission of an external funding application to Homes England

## Report to Cabinet

Date Issued: 27<sup>th</sup> May 2022

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## 1 Executive Summary

### Introduction

Regeneration & Economy are seeking approval for a capital project for the construction of 11 new properties on council owned land at West End Avenue, Smethwick. The new homes will be added to the Council's housing stock of properties for affordable rent.

Approval is also sought to apply to Homes England for grant funding through Strategic Partnerships, to assist with the delivery of the project. Homes England are inviting bids as part of a continuous market engagement process. There is no fixed closing date for bids.

The proposed development site is in council ownership and was previously the site of 'Westville' maisonettes which were demolished in 2002.

With over 6,000 people on the Council's Housing Register and 65% requiring properties with 2 or more bedrooms, additional affordable housing is needed across the borough.

Demand for the proposed property types is supported by the Council's Housing Register, which evidences strong demand for 2 and 4 bedroom properties in Smethwick.

Strategic Finance has been asked to carry out an appraisal of the funding application, which has been evaluated against HM Treasury Green Book guidance. The appraisal process recorded a score of 69%, with some areas of risk identified.

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## Project Objectives

- To increase the number of authority owned housing stock and reduce the amount of under-utilised land within council ownership.
- To support the Council's Vision 2030, where Sandwell has many new homes to meet a full range of housing needs, in attractive neighbourhoods and close to key transport routes.

## Project Details

The proposed residential sites will provide the following:

- 2-bedroom semi-detached houses x 7
- 4-bedroom detached houses x 4

Homes England's Strategic Partnerships allow for the delivery of affordable housing under the same principles as the Shared Ownership and Affordable Homes Programme (SOAHP) 2016 to 2021. Delivery through the Strategic Partnership must start on site by March 2023, with completion by March 2025.

Details of each scheme will be submitted to Homes England for approval prior to commencement.

The proposed development site is currently held as an asset in the Council's Housing Revenue Account. The planning application for the proposal will be submitted in May 2022, with project completion expected by December 2023.

Total project costs have been estimated by Urban Design & Building Services. Sandwell Metropolitan Borough Council will apply to Homes England for £0.374m, with the remaining funding to be provided from a Revenue Contribution to Capital Outlay (RCCO) and prudential borrowing, funded from the Housing Revenue Account. Prudential borrowing will incur additional costs over a 40-year period.

The proposed project is expected to generate a net rental income of £3.970m over a 40-year period.

Accord Housing Association will manage and monitor grant funding from Homes England on behalf of the Council, at a cost of £417 per unit. The total revenue cost for the service of £4,587 will be funded through the Housing Revenue Account.

## Scope and objectives of financial appraisal

The purpose of financial appraisals is to consider the guidance provided by HM Treasury in evaluating business case proposals and assessing the potential risk to

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the Council in achieving its objectives. The following components and risks are assessed:

HM Treasury Green Book	Potential Risks
<u>Strategic Case</u> Objective, need, demand and reasonableness	Insufficient justification for project/will not meet strategic objectives
<u>Economic case</u> Option analysis and risk	Poor use of council resources & excessive risk to Council
<u>Commercial Case</u> Legal and statutory implications	Project may contravene legal/statutory regulations
<u>Financial Case</u> Affordability	Proposals are not affordable or realistic
<u>Management Case</u> Governance, project management, monitoring and evaluation	Non-delivery of project and outputs
Limitations to scope of appraisal	Information provided by Project Officer

#### LEVEL OF ASSURANCE GAINED FROM FINANCIAL APPRAISAL

Limited (0%-65%)	Satisfactory (66%-80%)	Substantial (81%-100%)
There is a high risk of objectives not being met due to insufficient assurance within the project proposals. There is limited evidence to confirm that the risks to the Council could be adequately mitigated.	There is adequate assurance that objectives could be met, but further actions are required to adequately mitigate the risk to the Council.	There is good assurance that objectives will be met, with little risk to council resources.

### Overall Conclusion

The appraisal scored 69% and provides **satisfactory assurance** over the adequacy of the proposals.

Financial appraisals will identify the following levels of issues:

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## Fundamental

Action is imperative to ensure that the objectives of the project are met

## Significant

Action is required to avoid exposure to significant risks in achieving objectives

## Merits Attention

Action is advised to enhance operational efficiency

### Summary of key issues identified

- The financial appraisal has identified NO 'fundamental' issues
- The financial appraisal has identified 1 'significant' issue
- The financial appraisal has identified NO 'merits attention' issues

## 2 Issues Arising

Action is required to avoid exposure to significant risks in achieving objectives  
**Significant**

### 2.1 Economic Case – Value for Money & Option Analysis

(a) Construction costs average £0.315m per property, although it is acknowledged that the use of Homes England grant funding will reduce the cost to the Council to £0.281m per unit.

Estimated construction costs have been measured against the Building Cost Indices for the West Midland's region. Whilst it is recognised that there has been a significant increase in construction costs in recent months, the following should be noted:

- i. The unit cost does not include the value of the land, which if included, would increase average unit costs by a further £0.053m.
- ii. It is understood that the site has never been marketed for sale and therefore the level of market interest from private developers is unknown.
- iii. Construction costs appear high in relation to current property prices within the area. However, high construction costs per unit will partially be due to current market conditions within the construction industry and the development of small sites, which do not offer economies of scale.

Whilst local authority housing generally provides larger homes with a higher build quality than those of private developers, and privately purchased homes potentially require adaptations/modifications for council house use, it is still not clear whether all other options have been fully explored to deliver the Council's objectives at a lesser cost.

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Such options may include site disposal, purchase of privately owned properties, alternative house types/construction methods or a temporary delay to construction to develop other sites at a lower cost.

In addition to this, whilst funding from Homes England would provide grant monies of £0.034m per property, the use of the Council's Right to Buy receipts could reduce the Council's funding requirement by £0.126m per property. Although the Local Government Act 2003, will not allow both types of funding to be utilised on individual schemes, the use of receipts from Right to Buy house sales are time limited to 5 years, after which they must be returned to government with interest. Use of Right to Buy receipts or HRA balances may offer a suitable alternative or additional source of funding to the project.

**Implication:**

That the proposed option may not optimise value for money for the Council.

**Recommended Action:**

That Cabinet consider the alternatives and are satisfied that the proposal to construct the new build homes will meet the Council's objectives in the most appropriate manner.

(b)A list of sites for the Council's house building programme was provided, identifying council owned sites with potential for future development. Whilst the proposed site was included within the programme, it was unclear how sites are prioritised for development or the process for evaluation and approval.

**Implication:**

That development of the proposed site may not offer the most effective use of the Council's resources.

**Recommended Action:**

That a process is developed to prioritise the development of sites against pre-determined criteria and alternative options for achieving the Council's housing objectives within each locality.

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