Finance and Resources Committee

10am, Tuesday, 23 January 2018

Extension of Temporary Accommodation Private Sector Leasing contract and increase to costs

Item number	7.17
Report number	
Executive/routine	
Wards	City Wide
Council Commitments	C9, C34, C45

Executive Summary

The use of private sector housing is critical to the Council's delivery of temporary accommodation to homeless individuals and families.

The Council has contracted with Link Group under a Private Sector Leasing (PSL) contract to secure leases of up to 1,750 properties and manage the properties during their use for temporary accommodation. The Council's lease agreements with landlords are negotiated, arranged, and managed by Link on behalf of the Council.

The contract runs from 1 April 2015 to 31 March 2018, with the option to extend for a further two years at the discretion of the Council.

Link has approached the Council in advance of the break point, and advised that a continuation of the contract will require:

1. an increase to the amount of rent that can be offered to landlords; and
2. an uplift on the management fee paid to Link

The Private Rented Sector in Edinburgh is very buoyant and the general market rent is now much greater than the lease payments offered to PSL landlords. Current payment levels are linked to specified levels of Local Housing Allowance (LHA), as determined by the Department for Work and Pensions (DWP), and assessed as eligible to be recovered through housing benefit.

Since 2015, the number of properties in the scheme has declined from an average of 1,698 to the current position of 1,420, as a consequence of landlords moving away from the scheme. Most leases fall due for renewal over the next two years and there is a significant risk that numbers will reduce further.

Following negotiations with Link, it is proposed to offer landlords a maximum of 110% of the applicable LHA rate for one and two bedroom properties, to improve retention rates, stabilise property stock numbers and reduce the number of landlords withdrawing from the scheme. This would require a Council subsidy of up to 20% of the LHA rate for one and two bedroom properties.

As well as reducing the number of handbacks, it is hoped that this will encourage new landlords to join the scheme, increasing stock beyond current levels, and resulting in fewer families in unsuitable and costly bed and breakfast accommodation.

The subsidy would not be eligible for housing benefit, and the annual cost is estimated at £1.241m. This is based on a maximum subsidy of 20% and an average of 15% being paid.

Removal of the CPI uplift from lease agreements would save £0.115m, giving a net increase of £1.126m, which would be phased in over the next three financial years as leases fall due for renewal.

Link has requested a 10% uplift on the management fee paid to them, effective from the 31 March 2018 break point. This would increase the fee from £49.55 to £54.50 per property per week. Link has advised that this uplift is required for the contract to remain financially viable. The additional cost of the £4.95 uplift is £0.365m per annum.

Including the uplift in the management fee, total additional costs are estimated at £1.491m.

Officers from Temporary Accommodation services, Procurement, and Finance, in discussions with Link, are satisfied that the proposals are reasonable, and reported back to the Corporate Leadership Team (CLT) on 22 November 2017, on the outcome of the negotiations. CLT agreed that the proposal will now form part of the budget setting process in February 2018.

Report

Extension of Temporary Accommodation Private Sector Leasing contract and increase to costs

1. Recommendations

1.1 It is recommended that the Finance and Resources Committee:

1.1.1 Refer the report to City of Edinburgh Council for approval as the contract extension and additional costs are subject to Council approval as part of the budget setting process on 22 February 2018, and subject to approval by the Board of Link Group;

1.1.2 notes a proposed increase in lease payments to landlords for one and two bedroom properties up to a maximum of 110% of the applicable LHA rate, at an estimated annual cost of £1.241m;

1.1.3 notes the proposed removal of automatic inflation-based annual rent increases from new lease agreements, with an estimated saving of £0.115m; and

1.1.4 notes a proposed 10% uplift in the management fee at the contract break point, at an additional cost of £0.365m.

2. Background

2.1 The Homelessness and Housing Support Service discharges the Council's statutory duty towards people who are homeless. This includes the provision of temporary accommodation for anyone who is homeless and requires it, until a permanent or settled offer of housing can be made.

2.2 On 1 April 2015, the Council entered a contract with Link Group to manage the Council's Private Sector Leasing (PSL) scheme. Link was the previous managing agent and offered the best tender during a procurement process, both in terms of quality and value for money.

2.3 The contract with Link Group ends on 31 March 2018, and in accordance with the existing terms, it can be extended for a period of two years.

2.4 There is a significant risk to the Council that unless improved lease payments are made to landlords to stabilise property stock, and the management fee is increased to cover increasing operational costs, Link will not agree to extend the contract beyond 31 March 2018, as it would not be financially viable for them to do so.

2.5 Currently the contract with Link places all financial risk for rent recovery, arrears, repairs, landlord hand-back costs and other associated costs on Link. The Council receives all housing benefit payments for PSL properties and pays Link's management fee and landlord lease payments monthly.

3. Main report

3.1 There are currently 1,420 properties in the PSL scheme, down from a peak of 1,698 in early 2015. The number of landlords withdrawing from the scheme is increasing because higher returns can be achieved on the open market.

3.2 For housing benefit purposes, the maximum eligible rent for PSL properties is 90% of the applicable Local Housing Allowance (LHA). This is currently the maximum amount charged by CEC to the tenant's rent account and the maximum amount that is paid to the landlord (subject to annual Consumer Price Index uplifts during the lease term).

3.3 The LHA rate has failed to keep track with market rents and has been frozen for several years, except for a 3% increase to the rate for one-bedroom properties applied in 2017/18.

3.4 Link predict that more landlords will choose to leave the scheme to achieve a higher return on the open market, unless a Council subsidy is introduced.

3.5 There is an acute shortage of affordable housing in Edinburgh and the mainstream private sector is unaffordable for most people who access Homelessness Services.

3.6 In the longer term, if numbers of properties cannot be stabilised, the PSL scheme is likely to fail. There are no viable alternatives to the PSL scheme as the Council could not accommodate 1,420 households in public sector properties and alternative private sector lets or other types of accommodation would be more expensive. Bed and Breakfast accommodation would be unsuitable and would cost an additional £17m per year, net of housing benefit.

3.7 The current average costs of PSL properties have been compared to market rents for normal private let properties per independent reports produced by Citylets, and there is a considerable price difference.

3.8 The benefits of PSL are that the landlord has a guaranteed rental income, does not incur the costs of agency fees, void periods, rent default, repairs in excess of tenant deposit and other landlord requirements, but may incur higher insurance and borrowing costs. The Edinburgh average private sector market rent was therefore reduced by 15% to take account of this, enabling a comparison to be made with PSL rents. The adjusted market rent is substantially greater than PSL currently offers.

3.9 Based on this comparison, the proposed increase in rent for one and two bedroom properties is considered reasonable, and necessary to reduce the gap to an acceptable level for landlords.

3.10 The tables below show a breakdown of properties by size and lease end periods. The greatest period of risk of falling stock levels is during 2018 and 2019 when 1,274 leases will fall due for renewal.

PSL Stock Profile – total and % of properties by number of bedrooms

No. of bedrooms	Total Properties	% of Total
1	301	21%
2	837	59%
3	253	18%
4	29	2%
	1,420	

Lease Expiry

836 leases fall due for renewal during 2018/19 and a further 296 during 2019/20.

Year	Total
2017	34
2018	786
2019	488
2020	42
2021	35
2022	13
2026	18
2027	4
	1,420

3.11 Rental income from the scheme covers the current cost of landlord lease payments. The Council will require to fund the difference between the 90% rate eligible under housing benefit regulations and the proposed 110% maximum lease payment for one and two bedroom properties. The shortfall in supply affects three and four bedroom properties to a much lesser extent and the average rental payments are currently well below 90% of LHA (78% and 59% respectively). However, in some circumstances, it may be necessary to offer a landlord slightly more than 90% to secure a property.

3.12 The management fee/service charge was previously eligible for housing benefit. Welfare Reform changes introduced in 2010, when Link was initially awarded the contract, limited the management fee that could be charged to £60 per property per week.

3.13 With effect from 1 April 2017, management fees applicable to temporary accommodation were removed from eligible rent for the purposes of housing benefit claims for non-Council-owned accommodation, creating a projected pressure of £4.8m. The greatest impact of this has been in PSL (£4.5m). This loss of income is partially mitigated by £2.1m of additional government funding, leaving a net pressure of £2.7m.

3.14 The £60 management fee is currently split £49.55 to Link and £10.45 to the Council to cover operating costs, with full year fees of £4.5m split £3.7m to Link and £0.8m to the Council.

3.15 Link has advised that for the contract to remain financially viable, and to enable Link to enter into a contract extension, a 10% uplift in their fee is required, which would increase it to £54.50 per property per week. This is to pay for increased rent loss and court actions as a result of Welfare Reforms, additional marketing required to increase stock, and increases in staff salaries and pension costs.

3.16 On 2 October 2017, the Scottish Government amended the terms of the Unsuitable Accommodation Order 2004, placing a duty on councils to keep pregnant women and families with school age children in bed and breakfast accommodation for no more than 7 days (reduced from 14 days).

3.17 Welfare Reform announcements affecting supported housing and the wider social housing sector continue to be monitored.

4. Measures of success

4.1 Stabilise or increase the stock of PSL properties.

4.2 Making changes to new landlord leases by removing the automatic annual uplift to lease payments linked to CPI and replacing this with a capped increase of 1% to be offered to landlords only by exception, will limit the Council's exposure to cost increases in 2018/19 and 2019/20 until a new contract can be procured.

5. Financial impact

5.1 The 2017/18 gross projected costs of the PSL scheme are £13.5m, comprising £9.5m of lease payments, £3.7m of management charges and £0.3m of storage/removal costs. Link's management charges of £3.7m include £2.1m of void costs and tenant liability, £0.13m of hand-back costs (repairs) and pays for 54 employees who operate and manage the PSL scheme.

5.2 Rental costs of up to 90% of LHA are currently eligible for housing benefit. Introducing a subsidy for one and two bedroom properties of up to 20% above this amount would cost an estimated £1.241m per annum.

5.3 Removing the automatic annual CPI uplift to lease payments from the new lease agreements would reduce costs by £0.115m.

5.4 The proposed 10% increase to Link's management fee will cost an estimated £0.365m.

5.5 The net additional cost of the proposals is estimated at £1.491m, which would be phased in over the next three financial years as leases fall due for renewal:

- 2018/19 £0.872m
- 2019/20 £0.506m
- 2020/21 £0.113m

5.6 This cost increase will create a further budget pressure for Safer and Stronger Communities in 2018/19, in addition to the £3.5m reported in the revenue budget framework considered by Finance and Resources Committee on 27 October 2017. Subject to approval, sustainable means of addressing these costs will therefore need to be identified as part of setting the Council's budget framework on 22 February 2018.

6. Risk, policy, compliance and governance impact

6.1 There is a risk that the scheme will fail if the number of properties cannot be stabilised.

6.2 This would result in the Council being unable to fully discharge its statutory duties towards people who are homeless.

6.3 If Link do not extend the contract, the scheme will need to be brought in house with TUPE applying to 50 plus staff who will be entitled to employment with the Council.

6.4 There is a risk the Council will not have sufficient office accommodation or the appropriate IT systems to properly manage the scheme in house.

7. Equalities impact

7.1 There are no negative equality or human rights impacts arising from this report.

8. Sustainability impact

8.1 There are no impacts on carbon, adaptation to climate change or sustainable development arising from this report.

9. Consultation and engagement

9.1 Consultation was undertaken during the initial procurement exercise for the award of the contract in 2015.

9.2 Consultation with Link Housing and colleagues in Temporary Accommodation, Partnership and Planning, Finance and Procurement has taken place.

10. Background reading/external references

10.1 None.

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11. Appendices

None.