
STATES OF JERSEY



STATES OF JERSEY HOUSING TRANSFORMATION PROGRAMME: FULL BUSINESS CASE

**Presented to the States on 4th March 2013
by the Minister for Housing**

STATES GREFFE

Friday, 01 March 2013

States of Jersey Housing Transformation Programme

Full Business Case

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1 Executive summary

1.1 Introduction

This Full Business Case seeks approval for the establishment of a suitable delivery vehicle and funding mechanism for the management of States of Jersey social housing in Jersey.

Sector Treasury Services Limited were appointed as financial advisers to the Housing Transformation Programme and to assist in the development and assurance of a business case to consider the options for change. Sector Treasury Services recommended the use of the UK HM Treasury 5 Case Model for Public Sector Business Cases to evaluate the options for change and this was adopted by the Housing Transformation Programme which is the format of this report.

The preferred solution is for the establishment of a new, not-for-profit, wholly States owned social Housing Company (the "Housing Company") and implementation of its business plan (set out in the financial case in section 5).

The Housing Company will be a self-sustaining Social Housing service provider which is flexible and able to adapt to change with fully separate regulatory, policy and service functions.

The States of Jersey will transfer the current Social Housing stock, which has no debt burden, to the Housing Company for nil proceeds and the Housing Company will continue to deliver a significant annual return to the States of Jersey.

The proposed rent policy of 90% of market rents on new tenancies protects tenants in receipt of the housing component of Income Support and for tenants not in receipt of the housing component of Income Support it provides a balance between:

- ✚ Requiring those who can afford to pay more to do so
- ✚ Recognising that tenants have entered in to tenancy agreements and planned their finances on the basis of the prevailing rent levels

Decent Homes will be achieved within 10 years and maintained thereafter, funded by a combination of an investment from the Currency Fund and the rent increases achieved from the proposed rent policy. Furthermore, the stock will be improved to better meet the needs of Jersey's changing population funded from additional income generated.

1.2 Strategic case

The current provision for States of Jersey social housing in Jersey involves a single tier of government with responsibility for housing strategy, governance, regulation, policy making and delivery. This results in inherent conflicts of interest for the Minister for Housing who is simultaneously required to be policy maker, regulator and the largest landlord in the Island.

It is also a fact that over a number of years rents in the social sector have fallen a long way behind the market and therefore provides a hidden and unintended subsidy to all Tenants in the sector, whether or not their personal circumstances mean that they need that assistance.

In July 2010 the former Minister for Housing issued a policy statement establishing a Housing Transformation Programme to address the outcomes of a review carried out by the Cambridge Centre for Housing and Planning Research and set out in a report by Professor Christine Whitehead OBE. The Minister's statement indicated his commitment to:

- ✚ The establishment of an independent Regulator of social housing applicable to all residential providers in Jersey

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- ✚ The formulation of a new rents policy to establish a sustainable relationship between social housing rents and the overall rental market
- ✚ The change in status of the present Housing Department

Also of key importance here is the alignment of the proposed transformation with the States' Strategic Plan 2012 (P28/2012) and the corporate priority "House our Community".

The proposed business case enables resolution of the following key actions with the House our Community" priority:

- ✚ Continue work on existing homes to meet the Decent Homes Standard
- ✚ Address the funding of the maintenance and reinvestment of the States owned social housing stock.
- ✚ Complete the Housing Transformation Programme to allow more flexibility in tackling housing issues

The proposed rent policy (90% of equivalent market rents for new tenancies) would also enable the following actions to be met:

- ✚ Put in place schemes to generate affordable housing for social rental and purchase
- ✚ Bring forward schemes to support first time buyers

1.3 Economic case

The review carried out by the Cambridge Centre for Housing and Planning Research identified 7 possible delivery options for the provision of landlord services, which are noted in the table below (and detailed in section 3.4.3). Each option has been appraised in order to identify the most economically advantageous option, which best meets the service needs and optimises value for money.

A 30 year business model has been developed for each option. It is recognised that external finance is required in order to deliver stock development plans (noted in section 1.5 below) and so the ability of each option to obtain sufficient borrowing is considered in the option appraisal process.

The key assumptions for each business model are as follows:

- ✚ Decent Homes Standard achieved in 10 years and maintained
- ✚ Return to Treasury maintained in real terms from 1 January 2016 after delivering the returns set out in the Medium Term Financial Plan including Comprehensive Spending Review savings in 2013 (option 6 only (for other options surpluses are returned))
- ✚ Refurbishment and new build plans noted in Appendix B with a net gain of 434 units
- ✚ Sales of 300 properties (15 per annum for years 1-20 of the business model)
- ✚ £40m internal borrowing facility (for options 2 to 7)
- ✚ External borrowing facility to fund stock development and any remaining cash flow shortages (for options 4 to 7). External borrowing assumptions are noted in section 3.3.4
- ✚ Proposed rent policy and implementation thereof noted in section 3.4.1 (except for option 1 which incorporates the existing rent policy)
- ✚ States of Jersey Statistics Unit central scenario RPI projections and average earnings inflation of 0.75% in excess of RPI (which represents half of the long term expectation)
- ✚ Market rent inflation at RPI plus average earnings inflation

The following financial critical success factors were developed in order to appraise the delivery options:

- ✦ The resulting delivery organisation must be a self-sustaining social housing services provider
- ✦ The resulting delivery organisation must be a flexible delivery organisation able to adapt to change
- ✦ The resulting delivery organisation must provide a continued significant income stream to States of Jersey
- ✦ The resulting organisational framework must fully separate Regulatory, Policy and Service functions

The results of the options appraisal are noted in the table below.

| | | Ranking | Overall risk assessment |
|----------|--|---------|-------------------------|
| Option 1 | Status quo | 7 | High |
| Option 2 | States department with internal borrowing | 6 | High |
| Option 3 | Arms length management organisation (ALMO) | 5 | Medium to High |
| Option 4 | Trading operation | 3 | Medium |
| Option 5 | Hybrid trading company | 2 | Low to Medium |
| Option 6 | Wholly States owned social Housing Company | 1 | Low |
| Option 7 | Freehold sale to a new social landlord | 4 | Low to Medium |

Option 6 ranks highly against all critical success factors and offers the lowest risk. Stock development plans can be delivered as can the expected return to the States of Jersey. A separate landlord function and the availability of finance provide the required independence and autonomy. Option 6 is, therefore, the preferred option which is taken forward to the Commercial, Financial and Management cases.

1.4 Commercial case

The Commercial case covers the following areas for the establishment of the proposed Housing Company:

- ✦ Transfer agreement between the States of Jersey and the Housing Company
- ✦ Procurement, legislative and organisational arrangements
- ✦ Asset management arrangements
- ✦ Commercial risk allocation
- ✦ Human resource implications
- ✦ External funding sources
- ✦ Financial reporting and financial protocols
- ✦ Contractual milestones

1.5 Financial case

The key financial objectives of the Housing Company are as follows:

Objective

To achieve Decent Homes Standard within 10 years and maintain the standard thereafter

To develop the current social housing stock to better meet the needs of Jersey's changing population by:

- Making more homes more lifelong compatible by refurbishing existing stock and building on new sites
- To realign the current social housing stock and provide affordable housing solutions to those in a position to buy. This will be achieved through the sales of current social housing stock

To provide the agreed annual return to States of Jersey

The Housing Company will manage the social housing service including maintaining the 90% of market rent policy on new tenancies described in section 3.4.1 and summarised in section 5.2.1. The key elements from the Financial case are noted below.

1.5.1 Stock development

The Housing Company plans to invest £201.4m (in real terms) in stock development and obtain proceeds from sales of £96.1m (in real terms) as follows:

- Build on new sites with a net gain of 434 units (20 of which will be sold for lifetime enjoyment as affordable homes for proceeds of £4.4m) at a projected cost of £147.1m
- Refurbish 578 units at a projected cost of £54.3m
- Sell 300 units (projected at 15 per annum for 20 years with proceeds of £366k per property, with a 25% bond provided on half of sales)

Additionally, the Housing Company plans to invest £300.0m (in real terms) in maintenance to bring all properties up to Decent Homes Standard and maintain it thereafter (this is £19.0m more than that allowed for in the Medium Term Financial Plan).

The stock movements are summarised in the table below.

| | Units | Units |
|---|-------|--------------|
| Current social housing stock | | 4,539 |
| Gained through new build projects | 598 | |
| Lost through demolition | -164 | |
| Sold as part of a new build project | -20 | 414 |
| Units sold* | | -330 |
| Units held by the Company at year 30 | | 4,623 |
| Gained by Social Housing Trusts | | 203 |

*The sale of 330 properties includes 30 sales prior to the commencement of the new Housing Company on 1 July 2014

The proposed sales in years 1 to 20 and those that will take place prior to 2014 will all be classified as 'Affordable' in perpetuity and this will mean that the stock of affordable homes is actually increased by 414 units albeit that 330 homes will be targeted at affordable home ownership. Overall the Islands' stock of Affordable Housing will be augmented further by the addition of 203 units to the Housing Trusts.

Sales are proposed for years 1 to 20 of the business plan because the proceeds are used to fund the stock development and loan repayments which will be completed by year 20.

1.5.2 Borrowing

The States of Jersey has indicated that the following borrowing facilities could be made available:

- ✚ **Internal borrowing:** A facility of £40m as set out in R132/2011 States Investment Strategies with a fixed interest rate of 4% to be repaid by year 20 of the business model
- ✚ **External borrowing:** The Treasury Department has indicated that borrowing of up to £200m over a 20 year period is proposed to be made available to the Housing Company at a fixed interest rate of 5%. A financial advisor has been appointed initially to recommend the best finance options

These borrowing facilities have been incorporated in to the Housing Company's business model and are considered to be sufficient for the Housing Company to meet the above noted objectives.

1.5.3 Return to Treasury

The Housing Company will continue to return a significant agreed amount to the States of Jersey each year (as described in section 3.4.2).

1.5.4 Sensitivity analysis

Sensitivity analysis has been performed to assess the robustness of the business model against identified risks. It is concluded that, on the assumption that the matters noted in section 1.7 below are resolved as planned, the Housing Company is considered to be viable.

1.5.5 States' sector income support costs

Additional Income Support costs resulting from the proposed rent policy will be met by the Treasury through an additional budget allocation to the Social Security Department. Given the nature of the implementation of the proposed rents policy, these increased costs will build slowly over many years and peak at approximately £2 million per annum in real terms for Company properties after 30 years.

Section 5.2 of the financial case documents the income support implications resulting from this programme.

1.6 Management case

The Management case covers the following areas for the management of the proposed Housing Company:

- ✚ Project management
- ✚ Business change management
- ✚ Benefits realisation arrangements
- ✚ Risk management
- ✚ Contract management
- ✚ Post project evaluation

1.7 Next steps for the programme

The next steps for the programme are as follows:

- ✚ The States to consider the business case as part of the wider proposed transformation programme
- ✚ If the incorporation of States Housing Report and Proposition proposing enabling establishment of the Housing Company is approved, a shadow board would be recruited to lead development of the new organisation
- ✚ This would require:
 - ✚ Confirmation of proposed funding
 - ✚ Confirmation of risk allocation
 - ✚ Confirmation of the transfer agreement
- ✚ The above will be formalised through Regulations brought to the States in 2014

2 Strategic Case

2.1 Introduction

In July 2010 the Minister for Housing issued a policy statement establishing a Housing Transformation Programme to address the outcomes of a review carried out by the Cambridge Centre for Housing and Planning Research and set out in a report by Professor Christine Whitehead. The Minister's statement indicated his commitment to:

- ✚ The establishment of an independent Regulator of social housing applicable to all residential providers in Jersey.
- ✚ The formulation of a new rents policy to establish a sustainable relationship between social housing rents and the overall rental market.
- ✚ The change in status of the present Housing Department

This initial announcement was followed up by a further statement by the Minister within the 2011 Housing Department Business Plan highlighting the scope of the Programme. The statement is set out below.

"The Review of Social Housing undertaken by Professor Christine Whitehead from the Centre for Housing and Planning Research at the University of Cambridge was an independent, in depth study of social housing provision in the Island. In her report, published in 2009 and consulted upon during the first half of 2010, Professor Whitehead identifies that the existing method of delivering social housing is unsustainable. It is she says the States system of housing provision which is not fit for purpose, rather than the Housing Department itself which operates with significantly fewer resources than would be normal elsewhere.

Professor Whitehead has suggested that if a modern 21st Century social housing sector is what we desire then change and very significant change at that, is required.

Of the options presented by Professor Whitehead it is clear that we can maximise the impact of our social housing provision by moving to a situation where the States is very much the facilitator and regulator of all social housing provision. This would necessitate placing the present Housing Department, with all of its inherent experience and highly skilled staff, at arms length from the States where it can concentrate more fully on providing the housing service to those who most need that assistance. This arms length body will have the ability to access private finance as a means of developing new affordable homes to meet existing and any future demand for homes.

The role of regulation is something which should stay with the States and developing a suitable framework is fundamental to having a successful social housing sector.

The unsustainable nature of the Housing Department's financing whereby it is under funded by £7.5 million per annum whilst having a commitment to make a return of £23 million per annum to the Treasury must be addressed and work is already in hand with Treasury to find a solution. Of course one significant way of bridging this gap will be through the development of new homes which, once private development funding has been repaid, will be unencumbered income generating assets. This growth in the States owned social housing stock will certainly allow the much needed realignment of the housing stock to take place whilst also providing for some growth in the sector which will help to address the needs of those who presently do not meet the rather stringent allocations criteria."

In order to implement the Housing Transformation Programme a governance structure has been established by the Minister for Housing. The structure includes a Political Steering Group, comprising the Chief Minister and Ministers for Treasury and Resources and Social

Security together with a Programme Board of senior civil servants, and a Programme Management Team established within the Housing Department.

The role of this FBC is to provide a financial business case for the establishment of a suitable delivery vehicle and funding mechanism for the management of social housing in Jersey.

2.2 Strategic Context

2.2.1 Organisational Overview

The States of Jersey Housing Department is the predominant provider of social housing in Jersey with approximately three quarters of the total social housing stock. Other providers include 4 Housing Trusts who have and continue to be in receipt of support from the States and a number of other providers including some Charities and a number of Parishes who have developed small housing stocks without significant States support. A table setting out the provision of social housing by landlord is shown below.

| Landlord | Dwellings |
|---|-----------|
| States of Jersey Housing Department | 4,539 |
| Jersey Homes Trust | 741 |
| Les Vaux Housing Trust | 346 |
| Christians Together in Jersey Housing Trust | 123 |
| FB Cottages Housing Trust | 48 |
| Parish/Charities and other Social Housing Providers | 346 |
| Total | 6,143 |

In January 2012 the Minister for Housing launched the Affordable Housing Gateway. The aim of the Gateway was to bring together the waiting lists held by the 4 States supported Housing Trusts and the Housing Department into one consolidated waiting list with common eligibility criteria, improving equity and streamlining access for applicants.

There is a finite amount of social housing and the social housing sector has seen little growth since 2008, other than a small number of Parish developments and a small number of homes developed by the Housing Department on existing States owned land. Some new supply is now in development; however, this has only been possible with the advance of stimulus funding by the States.

To ensure that the limited amount of social housing available is occupied by those who need it most eligibility criteria have been developed. The current eligibility criteria for acceptance onto the Gateway list require that applicants must fulfil the following criteria:

- be residentially qualified households; and
- either have young children living with them or be over fifty years of age, or otherwise have medical, physical or mental disabilities; and
- have income less than defined maximum limits, which roughly equate to the bottom two quintiles of income distribution in Jersey.

2.2.2 The Housing Department

Jersey currently operates a single tier of government with responsibility for housing strategy, governance, regulation, policy making and delivery. The States itself is landlord for 65% of all social housing. This is quite different from other European countries. In the UK over 50% of social housing is provided by independent social landlords. Social housing provided by local authorities is funded from a ring-fenced account where expenditure and income on housing landlord activities is separated from the cash flows of the other activities provided by local authorities so that local taxes aren't used to subsidise social housing and housing rents aren't used to subsidise services funded by local taxes.

Jersey's system of government and the way in which Social Housing has been organised means that there are inherent conflicts of interest for the Minister for Housing who is simultaneously required to be policy maker, regulator and the largest landlord on the Island.

The Housing Department 2013 MTFP allows for a total of 47.6 Full Time Equivalents ("FTEs") staff. Additionally, 2.6 Full Time Equivalent Customer Service staff transferred to the Housing Department during 2012 (as the customer service function moved from Cyril Le Marquand House to the Housing Department). Total staff at 2013 is as follows:

| | No. of FTEs |
|--------------------------------------|-------------|
| Chief Officer and Personal Assistant | 2 |
| Strategic Development Directorate | 13 |
| Operations Directorate | 24.6 |
| Finance Directorate | 10.6 |
| Total Housing Department Staff | 50.2 |

Sector Treasury Services compared this to local authority housing organisations in the UK with broadly equivalent stock numbers and concluded that this represents a very lean establishment. For example in the UK for services provided by best practice organisations you would expect to find a ratio of staff to dwellings of approximately 1:67 (depending on density levels, housing and social conditions). In Jersey the ratio in accordance with the 2013 MTFP is 1:95. The preferred delivery organisation forecasts a ratio of 1:81 at inception.

2.2.3 The Housing Trusts

In contrast to the States, the Housing Trusts operate as not-for-profit organisations and unlike the Housing Department are able to retain all of their rental income and to reinvest it into housing related expenditure, to make repayments of borrowing entered into to acquire their respective property portfolios or to accumulate surpluses.

In the majority of cases borrowing by the Housing Trusts has only been possible with support from the States.

The various Trusts are managed by Boards of Trustees and whilst they employ no direct staff of their own, managing agents are employed to coordinate day to day administrative and landlord activities.

2.2.4 Council of Ministers

High level decisions on social housing policy and the role of the Housing Department are formally made by the States, but responsibility for developing policy rests with the Council of Ministers which set out its approach to Housing issues in its 2009 – 2014 Strategic Plan.

The Council of Ministers concluded that:

- All Island residents should be housed adequately.
- Older people need to be housed in accommodation which support the principles of 'lifetime homes' and which can adapt over time to allow independence to be maintained.
- Changing demographics and migration may put pressure on certain types of accommodation.
- If we want to meet the aspirations of Islanders to own their own homes, then homes must be made more affordable.
- The affordable housing should be targeted at only those who need the support.

A new Strategic Plan was approved by the States in 2012. Once again Housing related issues are given a high degree of priority and the Council of Ministers committed to:

- ✚ put in place schemes to generate affordable housing for social rental and purchase
- ✚ bring forward schemes to support first time buyers
- ✚ continue work on existing homes to meet the 'Decent Homes Standard'
- ✚ establish a Strategic Housing Unit to co-ordinate a long term housing strategy
- ✚ address the funding of the maintenance and reinvestment of the States owned social housing stock
- ✚ complete the Housing Transformation Programme to allow more flexibility in tackling housing issues

In response to the Council of Ministers strategy the Housing Department has set out its key objectives in its 2013 Business Plan. They are identified as:

- ✚ Effective management of the States owned social rental stock
- ✚ Introduce the proposed changes in the provision of social housing
- ✚ Greater emphasis given to the delivery of social landlord services
- ✚ Staff and resources managed to improve performance and provide value for money.

Also of key importance here is the alignment of the proposed transformation with the States' Strategic Plan 2012 (P28/2012) and the corporate priority "House our Community".

The proposed business case enables resolution of the following key actions with the House our Community" priority:

- ✚ Continue work on existing homes to meet the Decent Homes Standard
- ✚ Address the funding of the maintenance and reinvestment of the States owned social housing stock.
- ✚ Complete the Housing Transformation Programme to allow more flexibility in tackling housing issues

The additional rental income generated from the proposed rent policy level (of 90% of equivalent market rates on new tenancies) would provide funds to enable the following actions to be met:

- ✚ Put in place schemes to generate affordable housing for social rental and purchase
- ✚ Bring forward schemes to support first time buyers

2.2.5 Existing Financial Performance

The States' Housing Department has historically been funded from States' revenue funding streams. As a result the Housing Department is debt free and consequently the Housing Business Plan is able to project a surplus of £26.8m for 2013 (excluding depreciation) which is returned to Treasury. In recent years this has translated into a transfer of £21.5m in 2009, £18.7m in 2010, £21.5 in 2011 and £24.5m in 2012.

Investment decisions therefore involve balancing the requirement to return funds to the Treasury to be used for other purposes and increasing expenditure on social housing.

It is recognised that the current levels of contributions from the Housing Department are not sustainable, particularly if the service is to invest sufficient resources in maintenance and improvement works to bring the housing up to the decent homes standard by the target date within the Property Plan (P6/2007) of 2016 and maintain it at that standard. A stock condition survey prepared for the States of Jersey by Ridge and Partners shows a projected expenditure requirement of £328m over the next 30 years to deliver and maintain the decent homes standard (this is without further investment in refurbishing or

increasing the housing stock). This equates to £73k per dwelling, which Ridge and Partners indicated is at the top end of the benchmark range for survey projections in the UK - a reflection of higher house prices in Jersey.

2.2.6 Rent and Income Support

When valuations were obtained in 2010, the average weekly rent in States sector housing was £154 exclusive of service charges. This is approximately 69% of the market rent that would be charged for equivalent dwellings in the private sector. Valuations have been obtained at December 2012 and the relationship has continued at the same rate.

Rent increases for States' housing have been constrained in recent years because of an adverse relationship between States sector rent increases and the resulting cost to the States of Income Support payable to tenants of States housing, Trusts' housing and private rented housing.

A review of options to address this issue has been undertaken and it is proposed to change the link between States' housing rents and income support payable to private tenants. In future, it is proposed that private sector income support levels will be linked to the average of the market rents in the States' sector. The impact of this change in policy has been allowed for in the Medium Term Financial Plan and the Minister of Social Security will bring forward detailed proposals to be debated at the same time as the rent policy.

2.2.7 Demographic Change and Housing Costs

The residential qualification system that operates in Jersey has a major impact on total population and how housing is allocated in Jersey. The current policy includes the following:

- ✚ Maintain the level of the working age population on the island
- ✚ Ensure the total population does not exceed 100,000
- ✚ Ensure population levels do not increase continuously in the longer term

A census was carried out on 27 March 2011. On that day the total population of Jersey was recorded as being 97,857. This represented an increase of 10% since 2001. 82% of the population were residentially qualified (categories A to H) and 2% in categories J and K, whilst 13% were unqualified.

Average house prices in Jersey rose by 56% between 2002 and 2011. The most rapid increases were observed in three bed and houses (as opposed to flats) purchased by first time buyers. Flat prices rose by less than half the average rate. The main pressure in Jersey is for family homes and 'homes for life' for older people rather than flats although evidence set out in the Whitehead review indicates that buying a family home is generally only possible for qualifying residents with earnings in the two highest quintiles.

Younger households, single people, and those on lower incomes cannot afford to become owner occupiers, and must rent their accommodation, either from private landlords or in the social housing sector, unless they have access to significant savings or loans from parents or others. It is worth noting that in 2011, the average price of the 13 flats sold under the First Time Buyer scheme was £272,000, and the average price of the 22 first time buyer houses sold was £420,000. These prices are unaffordable for residents earning below the top two income quintiles without additional assistance.

2.2.8 Conclusions from Professor Christine Whitehead's Review of Social Housing in Jersey

This Green Paper (published in 2010) suggested that certain changes were necessary. These were:

- ✚ The conflict for the Minister for Housing being responsible for housing policy and regulation whilst also being the largest landlord needs to be resolved;
- ✚ There is a requirement for a long term cross tenure housing strategy;

- ✚ There has been a long period of under investment resulting in a considerable backlog -in the funding of maintenance and reinvestment of States owned social housing;
- ✚ A new regulatory framework applicable to all social housing providers needs to be created;
- ✚ Social housing needs to become more accessible for those in long-term housing need;
- ✚ Eligibility criteria need to be made clear and consistent across all providers;
- ✚ A long-term rental policy needs to be introduced;
- ✚ The Housing Department needs to be restructured to be more financially sustainable in order to adequately maintain States owned social housing in the long term.
- ✚ It is also a fact that over a number of years rents in the social sector have fallen a long way behind the market and therefore provide a hidden and unintended subsidy to all Tenants in the sector, whether or not their personal circumstances mean that they need that assistance.

2.2.9 Business Case Scope

Since the publication of the Whitehead review, the Political Steering Group for the Housing Transformation Programme have considered the structure and status of the current Housing Department and have concluded that there are seven alternative options available including the Status Quo. These span four financing mechanisms, as follows:

| Financing Mechanism | Delivery Vehicle |
|---|--|
| Revenue Funded (no borrowing) | 1. Status Quo |
| Internal Borrowing | 2. States Department 3. Arms Length Management Organisation 4. Trading Operation |
| Private Borrowing | 5. Hybrid Trading Company 6. Wholly States owned Housing Company |
| Private Borrowing following Freehold Sale | 7. Freehold sale to a new social landlord |

Detailed descriptions of the delivery options are set out in Appendix C and an economic appraisal of each of the delivery vehicle options are set out in the Economic Case in section 3.

In developing the new organisation, the Housing Transformation Programme is charged with endeavouring to provide increased "housing for life". The scope for this Full Business Case therefore also includes a review of the capacity of each delivery vehicle to invest in new affordable housing to meet the demand for additional social housing in Jersey.

2.2.10 Strategic Benefits / Investment Objectives

The main benefits associated with the Housing Transformation Programme were set out within the Programme Brief approved by the Programme Board at its meeting in November 2010 and validated by the Political Steering Group in April 2011. In the table below they are referenced to Government Strategic Priorities and the Social Policy Framework.

| Strategic Priority Ref | Strategic Priority Description | Contribution from Housing Transformation Programme |
|--------------------------------|--|---|
| 14 | Adequately House the Population | <p>Support the Development of Social Housing</p> <p>The funding proposals within this Outline Business Case provide a funding framework which would give the optimum scope for the provision of new social housing to meet the profile of housing types needed in Jersey</p> <p>Continue to upgrade and improve older States rental homes to meet the adopted Jersey 'Decent Homes Standard'</p> <p>This Full Business Case establishes the business planning implications of funding the cost projections associated with delivering the required dwelling standard. In addition, it enables comparison of delivery options to identify the approach which best addresses the investment needs for States' housing</p> |
| 3 | Reform Public Service Provision to Improve Efficiency | <p>Determine those services that must be provided by Government</p> <p>The economic appraisal of funding options within this Full Business Case will enable assessment and comparison of funding options based on continued ownership of the housing stock but with varying degrees of States managerial control against the option of a sale of the freehold to a new social housing provider</p> <p>Promote/review private sector involvement and more commercial approaches to service provision</p> <p>The economic appraisal of funding options within this Full Business Case will compare the existing revenue funded approach to meeting the investment needs of social housing with debt funding including borrowing by the Government and options for borrowing by the housing organisation</p> |
| 10 | Develop funding mechanisms to address the backlog of deferred maintenance of social rented housing | <p>Development of a Financial Business Model</p> <p>Development of a financial model with the flexibility to compare the ability of different funding mechanisms to deliver the investment priorities of social housing in Jersey, including addressing the backlog of maintenance works.</p> |
| Social Policy Framework | | |
| Criteria 6 | Households can access suitable accommodation for their needs | <p>The proposed Policy and Regulatory changes proposed as a result of the Programme would address the assessment of demand for different types of social housing and the delivery of an Affordable Housing Gateway to social housing spanning States housing and Trust housing. This Full Business Case addresses the scope for providing new housing to meet the needs of residents requiring social housing</p> |

The brief for this FBC has been to further develop the work undertaken in the Outline Business Case to set out the role that the proposed new Wholly States owned Housing Organisation will play in the provision of States of Jersey social housing. The following four key financial Critical Success Factors have been identified for evaluating the 7 delivery options:

- ✚ For the new Housing Organisation to become a self-sustaining social housing services provider
- ✚ For the new Housing Organisation to become a flexible and agile delivery organisation able to adapt to change
- ✚ For the new Housing Organisation to continue to make a significant annual return to the States of Jersey
- ✚ For the Regulatory, Policy and Service functions of the existing Housing Department to be fully separated

2.2.11 Strategic Risks

The main business and service risks associated with the potential scope for this project are shown below, together with their countermeasures.

| Risk | Mitigating action |
|--|--|
| Project Management | |
| Delay in delivering programme outcomes | <ul style="list-style-type: none"> ✚ Experienced Delivery Team and Advisers ✚ Clear programme planning, implementation and monitoring process ✚ Clear consultation and effective inter-Departmental working |
| Political | |
| Lack of public or political support for the Programme objectives and proposals | <ul style="list-style-type: none"> ✚ Regular reporting to the Political Steering Group, and the Council of Ministers ✚ Active engagement with the Health, Social Security and Housing Scrutiny Sub-Panel ✚ Pro-active and meaningful briefing of States Members |
| Financial | |
| Failure to adequately resolve the potentially adverse financial relationship between changes in States rent and income support costs | <ul style="list-style-type: none"> ✚ Joint, inter-Departmental review of housing elements of Income Support by experienced independent Advisers ✚ Social impact assessment of proposals |
| Lack of acceptance for the proposed contribution from the proposed housing solution towards States costs | <ul style="list-style-type: none"> ✚ Identification of a funding delivery mechanism that addresses the investment needs of the housing stock whilst providing an agreed contribution to States expenditure |
| Financial modelling doesn't adequately address future investment needs and / or management and financing costs | <ul style="list-style-type: none"> ✚ Validated stock condition survey and stock valuations ✚ Review of capital investment programme that optimises value for money delivery; ✚ Experienced financial advisor to validate modelling and validate assumptions in business model |

| | |
|--|---|
| Borrowing costs are higher than projected in Outline Business Case | <ul style="list-style-type: none"> Early reporting on implications of any changes in projected funding costs |
| Communication with Stakeholders | |
| Failure to gain the support of Tenants to proposals | <ul style="list-style-type: none"> Delivery of an effective communications strategy Active engagement with tenant representatives and frontline staff |
| Failure to gain the support of Housing Trusts to proposals | <ul style="list-style-type: none"> Ministerial consultation with Chairs of Housing Trusts Effective information sharing A proportionate and fair approach to policy changes affecting Housing Trusts |
| Failure to gain the support of staff to proposals | <ul style="list-style-type: none"> Delivery of an effective communications strategy Clear and transparent communication of benefits and implications for staff Seek advice on appropriate communication material |
| Organisational | |
| Service disruption to Tenants during change process | <ul style="list-style-type: none"> Experienced Delivery Team and Advisers Clear delivery outcomes, benefits and risk management and programme of change management Clear consultation and effective inter-Departmental working |

2.2.12 Assumptions and Dependencies

The Full Business Case is subject to the following assumptions and dependencies that will be carefully monitored and managed throughout the lifespan of the Housing Transformation Programme.

- That the proposal to separate the existing link between States of Jersey housing rents and private sector income support will be agreed and that an alternative approach to setting the housing element of private sector income support will be accepted;
- That a return to previous fair rent levels set at 90% of equivalent market levels for new tenancies is approved which provides sufficient resources for the delivery and maintenance of the decent homes standard and the provision of new social housing
- That a sustainable agreed level of annual contribution from the proposed Housing Organisation to the States of Jersey is agreed and fully funded within the Company's business plan
- That the Ridge stock condition survey, Jones Lang LaSalle valuations, and assumptions regarding business modelling provided by the Treasury and Resources Department remain valid
- That the proposed regulatory function is delivered independent of the strategic policy and service delivery functions
- That the strategic housing function remains within the States of Jersey, with effective internal and external stakeholder relationships, to enable delivery of the States' strategic housing priorities

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- ✚ Agreement regarding the scope of housing functions and assets which are to be transferred to the new organisation and the financial arrangements between it and States of Jersey.

That the future arrangements for service delivery of social housing to current States of Jersey tenants delivers a modern, customer-focussed service which meets the proposed regulatory expectations for enhanced governance, financial viability and service delivery. Resources will need to be employed appropriately to enable the day-to-day service to continue whichever option is chosen while managing change, potential disengagement and implementation of new systems

3 Economic case

3.1 Introduction

This section of the Full Business Case documents the options appraisal process and provides evidence to show that the most economically advantageous option, which best meets the service needs and optimises value for money has been selected. This Economic Case updates analysis provided in the Outline Business Case.

3.2 Matters considered at the Outline Business Case stage (August 2011)

3.2.1 Key Critical Success factors) considered in Outline Business Case

The critical success factors evaluated within the Outline Business Case, and the associated assessment questions, were as follows:

| Critical success factor | Assessment questions |
|---|--|
| The resulting delivery organisation must be a self-sustaining social housing services provider | <p>What scope is there to improve housing standards for residents?</p> <p>How accessible is the finance needed to pay for investment and delivery plans?</p> <p>What freedom is there to re-invest efficiency gains and additional income streams?</p> <p>How viable is the business model?</p> |
| The resulting delivery organisation must be a flexible delivery organisation able to adapt to change | <p>What capacity is there to deliver new housing – e.g. 'housing for life' (strategic priority no. 14)?</p> <p>How accessible is the finance needed to pay for investment and delivery plans?</p> <p>What autonomy is there to make independent decisions on procurement and service delivery?</p> |
| The resulting delivery organisation must be provide a continued significant income stream to States of Jersey | <p>What is the level of income stream available to States of Jersey?</p> <p>How does the income stream compare with States of Jersey estimates?</p> <p>What are the external factors that might influence this income stream?</p> |
| The resulting organisational framework must fully separate Regulatory, Policy and Service functions | <p>How separate are the service, regulatory and policy functions?</p> <p>How independent is governance of the delivery organisation?</p> |

The above critical success factors and associated assessment questions, which were developed by Sector Treasury Services at Outline Business Case stage, have been reviewed and it is concluded that they continue to be an appropriate basis for the Full Business Case assessment.

3.2.2 Refurbishment and new build plans considered in Outline Business Case

In assessing the capacity to deliver new housing at the Outline Business Case stage, 2 scenarios were modelled to build 552 or secondly 1,104 net new properties. At the Outline Business Case Stage these were not based on real, current schemes but broadly reflected maximum stock anticipated in the Island Plan. The scenarios were designed to test the ability of the business model under each option to finance the costs of borrowing implied by these levels of additional investment, should the Strategic Housing Unit wish the proposed Housing Organisation to invest to this level.

Following the developments since the Outline Business Case noted in section 3.3 below, schemes identified for development have been included in the updated business modelling. Updated plans are described in section 3.3.3 and Appendix B.

3.2.3 Rent policy and income support options considered in Outline Business Case

This Full Business Case proposes a 90% of market rents policy for new tenancies (as described in section 3.4.1.1).

Several rent policies and methods of implementation were considered prior to taking the decision to propose this rent policy. Considerations at Outline Business Case stage are noted below, and considerations subsequent to that are noted in section 3.3.

The rent policy options evaluated at the Outline Business Case stage were:

- ✚ Scenario 1: Rents set at 80% of equivalent market rent. Annual rent increases for existing tenants limited to a maximum of £3 per week above the level of the annual uplift* in rental values.
- ✚ Scenario 2: Rents set at 80% of equivalent market rent. Annual rent increases for existing tenants limited to a maximum of £5 per week above the level of the annual uplift* in rental values.
- ✚ Scenario 3: Rents set at 90% of equivalent market rent. Annual rent increases for existing tenants limited to a maximum of £3 per week above the level of the annual uplift* in rental values.
- ✚ Scenario 4: Rents set at 90% of equivalent market rent. Annual rent increases for existing tenants limited to a maximum of £5 per week above the level of the annual uplift* in rental values.

*Annual uplift is equivalent to Retail Price Index ("RPI") plus 0.75%. 0.75% represents half of the average annual increase in earnings in excess of RPI

For all scenarios above, increases in Income Support costs would be returned to the States of Jersey and funded by the rental income raised by the new housing organisation.

At Outline Business Case stage, 80% of equivalent market rents was determined not to enable viability for the social housing sector in general and the proposed Housing Organisation in particular. Updated business modelling performed for this Full Business Case indicates that the 80% of market rents policy is not viable due to the required level of borrowing. Furthermore, an 80% of market rents business model is not robust when sensitivity analysis is performed in, for example, a weak property and rental market (resulting in lower proceeds from property sales than expected). In order to make the business model viable with an 80% of market rents policy, the return to the States of Jersey would need to be reduced significantly.

Following the developments since the Outline Business Case noted in section 3.3, the implementation of the rent policy has been revised. The updated proposed rent policy is described in section 3.4.1.

3.2.4 Delivery options considered in Outline Business Case

The delivery options evaluated within the Outline Business Case, along with the overall ranking and risk assessment at that stage, were as follows:

| | | Ranking | Overall risk assessment |
|----------|--|---------|-------------------------|
| Option 1 | Status quo | 7 | High |
| Option 2 | States department with internal borrowing | 6 | Medium |
| Option 3 | Arms length management organisation (ALMO) | 4 | Medium |
| Option 4 | Trading operation | 5 | Low to Medium |
| Option 5 | Hybrid trading company | 3 | Low to Medium |
| Option 6 | Wholly owned housing Company | 1 | Low |
| Option 7 | Freehold sale to a new social landlord | 2 | Medium |

The delivery options have been reviewed, and are not materially different to those in the Outline Business Case. The revised options are described in more detail in section 3.4.3.

3.2.5 Preferred option at Outline Business Case stage

The preferred option at the Outline Business Case stage was:

- ✚ Setting up a wholly owned Housing Company and adopting the rent policy based on 90% of equivalent market rents with increases towards these rents limited to increases in average market rents (RPI + 0.75%) plus £5 (the 0.75% represents half of the average annual increase in earnings in excess of RPI)
- ✚ To maintain fair rent levels at 90% of equivalent market rent

3.3 Developments since the Outline Business Case

3.3.1 Political steering group conclusions

Outcome of presentation of the Outline Business Case to the Political Steering Group on 9 August 2011

Option 6 was agreed as the basis for further work, which needed to include:

- ✚ Further work on the business case in order to ensure a robust case for change
- ✚ How P6/2007 had contributed to Housing Department's finances and the future extent of sales and disposals would need to be set out within proposals
- ✚ Whilst there was general support for the proposal to use States of Jersey funding to smooth the funding profile within the business case, sensitivities looking at faster convergence to the proposed 90% near market rent level to attempt to preserve the annual return to Treasury should be undertaken

The Political Steering Group also recognised the importance of the social impact of the rent policy change and asked the delivery team to consider options for its implementation.

The proposed Outline Business Case position presented to the Political Steering Group at briefings held between 13 December 2011 and 9 January 2012

The proposed assumptions, based on updated financial modelling, presented to the Political Steering Group at briefings held between 13 December 2011 and 9 January 2012 were:

- ✚ Decent Homes Standard achieved in 10 years and maintained
- ✚ Refurbishment and improvements to existing stock to adapt into Life Long Homes
- ✚ Re-develop selected low density estates

The modelling of the proposed position allowed for:

- ✚ Sales of 450 properties (15 per year amounting to £4.6m per year at today's prices)
- ✚ Demolish 224 and re-build 592 units on States-owned sites
- ✚ Social housing stock would be approximately 4,444 units at the end of the 30 year plan
- ✚ Phased increase to 90% rent policy with an increase of £5 per week above the level of the annual uplift in rental values
- ✚ £40 million internal (States of Jersey) borrowing and £108 million external (privately funded) borrowing
- ✚ Return to Treasury maintained in real terms from 2014 after Comprehensive Spending Review savings are delivered in 2013 (as set out in the Medium Term Financial Plan)
- ✚ Additional income support costs resulting from the initial implementation of the proposed rent policy added to the return to Treasury

Sensitivity analysis was performed with respect to:

- ✚ Rent convergence with weekly increase caps of £0, £5, £10, £15 and £20
- ✚ 15 and 20 sales of properties per annum, and calculation of the number of sales required if no external borrowing was taken out
- ✚ Interest rates of 4% for internal borrowing and 4.7% or 6% for external borrowing
- ✚ Different stock investment options:
 - ✚ Option A: Decent Homes Standard only
 - ✚ Option B: Option A + intensification on existing sites*
 - ✚ Option C: Option A + Option B + 318 new build on acquired sites**

*Decent Homes Standard plus completion of refurbishment and intensification of La Collette low rise, Le Squez phases 4 to 8 and Victoria Cottage Homes phases 1 to 4

**Decent Homes Standard plus completion of refurbishment and new build projects listed in Appendix B

The outcome of the sensitivity analysis was presented to the Political Steering Group at briefings held between 13 December 2011 and 9 January 2012.

Conclusions of the Political Steering Group at briefings held between 13 December 2011 and 9 January 2012

The Political Steering Group agreed that the proposed Outline Business Case solution should be further investigated and presented in the FBC and this should incorporate a 90% of market rents policy. The implementation of the 90% of market rents policy which was discussed with the Political Steering Group, which is not the policy proposed in this FBC, was as follows:

- ✚ Tenants in receipt of any amount of the housing component of Income Support:
 - ✚ These tenants would be charged 90% of market rent from April 2014. Their Income Support payments would increase by the same amount as their rent increase. Therefore, tenants in receipt of the housing component of Income Support would be fully protected
- ✚ Tenants not in receipt of Income Support
 - ✚ These tenants would be charged rent at 90% of market rent from 1 April 2014. At the same time they would receive a subsidy for the same amount as their rent increase

- ✚ Between April 2014 and April 2015, tenants would be given the opportunity to apply for means testing in order that their subsidy is not immediately withdrawn. The criteria for the means test would be designed to ensure that tenants do not encounter financial hardship and would include consideration of their expenditure
- ✚ For means-tested tenants, the subsidy would be phased out from 1 April 2015, dependent upon the circumstances of the tenant, within the following parameters
 - ✚ Minimum of £5 per week reduction in the subsidy per year (or the total or remaining subsidy where this is less than £5 per week)
 - ✚ Maximum of 10 years
- ✚ Cottage Homes tenants
 - ✚ Residents of Cottage Homes properties are governed by a constitution. The constitution contains terms and conditions which are different to those included in the standard tenancy agreement used for tenancies in general stock. Amongst other things, the constitution stipulates that a contribution is paid rather than a rental
 - ✚ A Report and Proposition to repeal the constitution would be proposed which, if successful, would result in future Cottage Homes tenants moving to the standard tenancy agreement
 - ✚ Cottage Homes residents with tenancies at 1 April 2014 would be fully protected (including after the property is refurbished and if a decanting period is required) unless and until such time that they wish to move to an alternative property

Additional Income Support costs arising from the implementation of the rent policy would be paid for by the Housing Organisation through an increase in the annual return made by the Housing Organisation to the States of Jersey.

Final approval for the proposed rent policy is subject to an acceptable option for the housing component of income support being identified. This is addressed in the Financial Case in section 5.2.

Updated proposed rent policy

In December 2012, the Housing Minister met and consulted with States Members and the Health and Social Security Scrutiny Panel in relation to his proposals for the future of Social Housing in Jersey. Recurring concerns expressed to the Minister were:

- ✚ The return to the 90% of market rent policy
- ✚ The size of the annual return to Treasury
- ✚ The social impact of the rent policy on tenants given current economic circumstances

80% rents policy consideration

In December 2012, the Housing Minister asked for modelling to be undertaken to establish the financial implications of an 80% of market rent policy whilst still performing redevelopment plans and achieving Decent Homes Standard objectives.

3 additional scenarios were modelled, using the assumptions noted in section 3.4 and rent policy implementation noted above. The scenarios were as follows:

1. 80% of market rents policy
2. 80% of market rent policy with a one off reduction to the return to Treasury in 2016 of £4,750k (which represents £4,204k in real terms)

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3. 80% of market rent policy with a one off reduction to the return to Treasury in 2016 of £1,800k (which represents £1,593k in real terms)

An 80% of market rent policy with no reduction to the return to the States of Jersey (scenario 1), would result in a loan period of 26 years and generate significantly lower cash surpluses at year 30.

If the return to the States of Jersey was reduced by £4,750k (scenario 2), the outputs for the Housing Organisation would be similar to the business model with a 90% rents policy (with no reduction in the return).

Reducing the return by £1,800k (scenario 3) would result in increased borrowing requirements and lower cash surpluses at year 30.

It was considered that scenario 2 could represent a suitable compromise. Therefore, the robustness of this model was assessed through the performance of sensitivity analysis.

The results of the sensitivity analysis revealed that the Housing Organisation did not have a viable business model in a weak rental and/or property market. Therefore, there was a high risk that additional support would be required from the States of Jersey.

The outcome of the review concluded that the 80% of market rents policy, with a reduction in the annual return to the States of Jersey of £1,800k in 2016, did not represent a viable solution because there was a high risk that the Housing Organisation would not be self-sustainable.

90% of market rent on new tenancies

In January 2013, the Minister for Housing, taking in to account the outcome of business modelling in the round and stakeholder views, including concerns raised by States Members and the Health and Social Security Scrutiny Panel noted above, agreed to the development a Full Business Case incorporating the following assumptions:

- ✚ An annual return to Treasury that is maintained in real terms from 1 January 2016 (after commitments contained within the Medium Term Financial Plan have been delivered)
- ✚ A rent policy of 90% of market rent on new tenancies. This is described in section 3.4.1.1 and summarised below
 - ✚ Existing tenancies would remain on the same rental charges with annual inflation linked increases (capped at 90% of market rents if applicable)
 - ✚ Rents on new tenancies would be charged at 90% of market rent with annual inflation linked increases (capped at 90% of market rents if the inflation linked increase was greater than the increase in the market rent)
 - ✚ Tenants in receipt of any amount of the housing component of Income Support would not be financially impacted by this rent policy in their current tenancies or if they transfer to another property within the Housing Organisation's stock
 - ✚ Tenants not in receipt of the housing component of Income Support would not be financially effected by this rent policy whilst they remain in their current properties. Should they move to another property they would be required to pay 90% of market rent for the new property. Section 5.2 of the Financial Case includes analysis that shows the affordability of the proposed rent policy for tenants in these circumstances

The Minister for Housing requested that a financial business model was developed to assess the viability of this option. The results of the business model revealed that the Housing Organisation would have a self-sustaining viable business model including in times of economic downturn (including a weak rental and/or property market).

It was agreed to prepare the Full Business Case on this basis, which incorporates the updated business modelling assumptions noted in section 3.4.

The remainder of the Economic Case assesses the 7 delivery options. The Financial Case summarises the business case of the preferred option and tests the robustness of the business case by performing sensitivity analysis.

A further change in the assumptions per the business modelling performed for the Political Steering Group in December 2011 to the financial business modelling contained in this Full Business Case is a reduction in the number of property sales. In the assumptions in this Full Business Case, properties sales are 300, not 450 which were incorporated in the Outline Business Case. This change represents 15 sales per annum for 20 years rather than for 30 years. Proceeds from property sales are used to fund the new build projects. This funding will only be required until external borrowing is repaid, which is forecast to be within 20 years.

3.3.2 Other progress

The proposed solution and a near market rent policy was incorporated in the "Achieving Decent Homes, An Affordable Housing Framework for the Future" White Paper which was issued on 12 April 2012 after being approved by the Council of Ministers on 15 March 2012.

The Council of Ministers agreed to provide £27.1m to the Housing Department in 2012 to advance 6 refurbishment and new build projects. Report and Proposition P40/2012 was lodged on 12 April 2012 and has been approved. The cash advanced will be repaid on inception of the new delivery organisation.

3.3.3 Changes to stock development plans and external borrowing

New build plans and external debt at Outline Business Case stage noted in section 3.3.1 resulted in net additional units of 368 and external debt of £108m identified within the "Achieving Decent Homes" White Paper. Further sites have now been identified for new build development by the Minister for Planning and Environment and have been incorporated in the updated business modelling to demonstrate their capacity and flexibility to deliver new homes (see Appendix B for a full list of proposals). This results in the following changes to new builds, major refurbishments and external borrowing since the proposed Outline Business Case solution was agreed by the Political Steering Group at briefings between 13 December 2011 and 9 January 2012. Refurbishment projects are also noted below for further information.

| | Cost of refurbishment projects | Cost of new build development | Peak external borrowing* |
|---|--------------------------------|-------------------------------|--------------------------|
| | £m | £m | £m |
| Proposed solution agreed by PSG on 12 January 2012 | 42 | 90 | 108 |
| Further sites identified and/or changes to estimated cost | 12 | 57 | 52 |
| Updated business modelling | 54 | 147 | 160 |

*the peak shown in the above table are for option 6 – Wholly owned Housing Company

3.3.4 External borrowing

It is recognised that the new Housing Organisation requires external finance in order to meet its objectives. The States of Jersey may, for major investments such as social housing, which have long term benefits, decide to borrow in order to finance the project and spread an element of the cost to future tax payers who will also benefit from the new facility. The States of Jersey are presently exploring a range of options.

A financial advisor has been appointed initially to recommend options for the best financing options. Once a workable solution is identified, a proposition will be taken to the States to seek their approval for the proposed funding strategy, in compliance with Article 21 of the Public Finances (Jersey) Law 2005.

The Treasury Department have estimated that borrowing of up to £200m over a 20 year period is proposed to be made available to the Housing Organisation at a fixed interest rate of 5% per annum. This facility is considered when appraising the options in this section, and performing sensitivity analysis for the preferred solution in section 5.7.

3.4 Summary of updated business modelling assumptions

The results of business modelling for the 7 delivery options (which are described in section 3.4.3 and Appendix C) incorporated in this report are based on the following key assumptions:

- ✚ Decent Homes Standard achieved in 10 years and maintained
- ✚ Return to Treasury maintained in real terms from 1 January 2016 after delivering the returns set out in the Medium Term Financial Plan including Comprehensive Spending Review savings in 2013 (option 6 only (for other options surpluses are returned))
- ✚ Refurbishment and new build plans noted in Appendix B with a net gain of 434 units
- ✚ Sales of 300 properties (15 per annum up to year 20 of the business model)
- ✚ £40m internal borrowing facility at a repayment interest rate of 4% per annum (for options 2 to 7)
- ✚ External borrowing facility to fund stock development and any remaining cash flow shortages (for options 4 to 7). External borrowing assumptions are noted in section 3.3.4
- ✚ Proposed rent policy and implementation thereof noted in section 3.4.1 (except for option 1 which incorporates the existing rent policy)
- ✚ The use of the States of Jersey Statistics Unit central scenario RPI projections and average earnings inflation of 0.75% in excess of RPI (which represents half of the long term expectation)
- ✚ Market rent inflation at RPI plus average earnings inflation of 0.75%

The detailed business models for each option are available on request.

3.4.1 Updated assessment of proposed rent policy and income support

It was noted in the Outline Business Case that social housing rent levels have fallen below fair rent levels.

On average, States of Jersey social housing rent levels are approximately 70% of market rents (based on a valuation of social housing rents performed and validated by professional valuation experts). The rents range from under 50% of market rents to (in a small number of cases) over 100% of market rents.

Rents at these levels are not appropriate because:

- ✚ Aggregate rents at these levels are insufficient to maintain States housing at Decent Homes Standard and make the annual return to States of Jersey
- ✚ Rent levels set below fair rent provide a subsidy to the tenant. This subsidy is unintended, hidden and not means tested

It is recognised that tenants will have entered in to tenancy agreements and will have planned their finances on the basis of the prevailing rent levels. It is proposed to allow current tenants to continue on their current rent levels (with annual increments explained below) for the duration of their tenancy.

3.4.1.1 The proposed rent policy

The proposed rent policy modelled in this FBC sees a return of social housing rents to fair rent levels for any tenancy that commences on or after 1 April 2014. Fair rent levels are set at 90% of market rents to track but not inflate market rents in the private sector.

New tenancies (and existing tenancies that are at 90% of market rents) will be adjusted annually by RPI plus average earnings inflation of 0.75% in excess of RPI (which represents half of the long term expectation). However, where this would take the rent above 90% of market rent, the rent will only be increased to 90% of market rent.

For existing tenancies that are above 90% of market rent (approximately 450 properties), rent will be frozen until it matches 90% of market rent. Thereafter, it will be adjusted annually as noted above.

The annual return to Treasury will be maintained in real terms (i.e. adjusted annually by RPI). Therefore, increases in rental income above RPI will be retained by the Housing Organisation. Where increases in rental income are below RPI, i.e. in a weak rental market, the Housing Organisation will absorb this into its operations, therefore, not requiring additional support from the States of Jersey.

This could be achieved by changing stock development plans (including re-profiling maintenance costs), overhead cost reductions, alternative income sources from widened activities, further property sales in some years, delaying repayment of the internal loan and obtaining further external financing. The Housing Organisation would be required to keep its operating practices under continuous review, with a view to minimising costs and maximising flexibility within its business model.

The amount of additional rent forecast to be generated by the proposed rent policy is noted in the table in section 3.4.1.3.

3.4.1.2 Implication for tenants

Tenants in receipt of the housing component of Income Support

Rents charged for properties held by the Housing Organisation will continue to be at a level that would be covered by the housing component of Income Support. Therefore:

- ✚ Tenants entitled to the full housing component of Income Support will continue to have the full amount of their rent paid whilst they are a tenant of the Housing Organisation
- ✚ Tenants entitled to any lower amount of the housing component of Income Support will continue to receive the level of Income Support appropriate to their circumstances

In other words, tenants in receipt of any amount of the housing component of Income Support will not be financially impacted by the proposed rent policy in their current tenancies or if they transfer to another property within the Housing Organisation's stock.

Tenants not in receipt of the housing component of Income Support

Existing tenants not in receipt of the housing component of Income Support will not be required to pay additional rent as a result of the proposed rent policy (other than annual increases explained in section 3.4.1.1) whilst they remain in their current properties.

Should those tenants transfer to another property within the Housing Organisation's stock (thus creating a new tenancy), rent will be charged at 90% of market rent for the new property.

Section 5.2 of the Financial Case includes analysis that shows the affordability of the proposed rent policy, in terms of the ability of tenants to pay additional rent for those not currently in receipt of Income Support.

3.4.1.3 Implication for the States of Jersey

The return to Treasury is maintained in real terms from 1 January 2016 after delivering the returns set out in the Medium Term Financial Plan including Comprehensive Spending Review savings in 2013 (option 6 only (for other options surpluses are returned)).

This section explains the forecast housing component of Income Support resulting from the proposed rent policy.

The table below includes forecasts for:

- ✚ The additional rental income received by the Housing Organisation as a result of the proposed rent policy being implemented (compared to the existing rent policy)
- ✚ The amount of the additional rent that will be paid by the Social Security Department. This is modelled as 67% of the additional rent because approximately 67% of the tenants of the Housing Department are entitled to an element of the housing component of Income Support

| Year | Year | Results in real terms* | |
|-----------|------------------------|--------------------------|--|
| | | Additional rental income | Additional rent paid by Income Support |
| | | £m | £m |
| 2014 | 1 | 0.5 | 0.3 |
| 2015 | 2 | 1.1 | 0.7 |
| 2016 | 3 | 1.1 | 0.7 |
| 2017 | 4 | 1.5 | 1.0 |
| 2018 | 5 | 1.6 | 1.1 |
| 2019 | 6 | 1.9 | 1.3 |
| 2020 | 7 | 2.2 | 1.5 |
| 2021 | 8 | 2.2 | 1.5 |
| 2022 | 9 | 2.2 | 1.5 |
| 2023 | 10 | 2.4 | 1.6 |
| 2024-2028 | 11-15 (annual average) | 2.5 | 1.7 |
| 2029-2033 | 16-20 (annual average) | 2.8 | 1.9 |
| 2034-2043 | 21-30 (annual average) | 3.0 | 2.0 |

*The amounts shown in the above table are in real terms, therefore, the impact of inflation has been removed

Based on recent activity, it is expected that approximately 55% of new tenancies will be to tenants from the waiting list. Therefore, the Income Support paid for these tenancies replaces Income Support paid in the private sector.

The additional units built by the Housing Organisation will provide growth to the social housing sector. This will change the proportion of Income Support payments made to social housing landlords (relative to private landlords) but the overall cost would be the same.

Section 5.2 of the Financial Case includes analysis that shows the affordability of the proposed rent policy in terms of the above noted additional Income Support costs.

3.4.2 Proposed required annual return to the States of Jersey

The proposed solution is to maintain the return to States of Jersey in real terms from 1 January 2016. This is after delivering the returns set out in the Medium Term Financial Plan including Comprehensive Spending Review savings. In years 2013 to 2015 the return will be adjusted to reflect agreed transitional costs.

The table below illustrates the returns up to 2015, thereafter the return would be adjusted annually by RPI.

| | 2012 | 2013 | 2014 | 2015 |
|---|--------|--------|--------|--------|
| | £000s | £000s | £000s | £000s |
| Near cash return as per MTFP | 24,559 | 26,798 | 27,972 | 29,339 |
| One off set up costs of the new organisation | - | (706) | - | - |
| Transfer of costs to Chief Ministers Department | - | - | 182 | 182 |
| Agreed return | 24,559 | 26,092 | 28,154 | 29,521 |

Note that this is the return incorporated in the business model for option 6. The amounts returned to the States of Jersey differ for the other options. This is explained as follows:

- ✚ Option 6 (a wholly owned Housing Company) would involve setting up a new company (with the States of Jersey being the ultimate controlling party). The return to the States of Jersey would be an annual expense governed by a contractual arrangement. The business modelling for option 6 therefore assumes the proposed required return noted in the table above
- ✚ Under options 1 to 5 the Housing Organisation would, with varying degrees of independence, remain part of the States of Jersey and so surpluses would be returned each year (surpluses are defined in section 3.4.3) and this is the basis of the business modelling for those options. The surpluses are compared to the proposed required return in section 3.5.3.2. In reality, where the surplus is less than the required return to the States of Jersey, the Organisation and the States of Jersey would be required to discuss how the shortfall would be covered (either by reducing stock development plans or the amount returned to the States of Jersey)
- ✚ Under option 7, the social housing stock is sold to a third party for a one-off payment on day one. This payment is compared to the required return (per the table above) in section 3.5.3.2

Comparison of proposed return to existing arrangements

Maintaining the annual return in real terms represents a change from the current policy. Currently, the return is set by the States of Jersey. This is usually based on:

- ✚ An increase representing the increase in rental income
- ✚ A reduction representing an inflationary increase in the Housing Department's expenditure

Rental income is expected to increase by more than RPI under the proposed rent policy. Therefore, under the current arrangement for the annual return, the return would increase by more than RPI.

However, the return under the current arrangement could not be delivered, even if the proposed rent policy is adopted. This is because of the additional costs of delivering the stock development plans (including meeting Decent Homes Standard within 10 years). Therefore, under the current arrangement, the business model is not viable.

If the proposals contained in this Full Business Case are accepted, the States of Jersey would receive a fixed return (in real terms) and can therefore plan their finances with that certainty (without the risk that the return would reduce if rental income is lower than forecast). Furthermore, the States of Jersey would be sole guarantor for a self-sustainable Social Housing provider which meets Decent Homes Standard without the need for further investment.

3.4.3 Updated description of delivery options

For each of the 7 options the criteria used to differentiate them for the purpose of this appraisal are set out in Appendix C. This has been updated for any changes since the Outline Business Case stage.

The table below provides a summary of the key differences between the 7 options considered.

| Option | Transfer of ownership of social housing assets | Separates policy and management from regulation | Enhanced governance | Borrowing | Surpluses returned to States of Jersey *** |
|--|--|---|---------------------|--|--|
| Option 1 – Status Quo | N | N | N | N | Y |
| Option 2 – States Department (with internal borrowing) | N | N | N | Y (internal borrowing) | Y |
| Option 3 – ALMO | N | Y | Y | Y (internal borrowing) | Y |
| Option 4 – Trading Operation | N | Y | N | Y (internal borrowing and external borrowing*) | Y |
| Option 5 – Hybrid Trading Company | N | Y | Y | Y (internal borrowing and external borrowing*) | Y |
| Option 6 – Transfer to a housing company, wholly owned by States of Jersey (Leasehold or Freehold**) | Y (transfer may be freehold or leasehold) | Y | Y | Y (internal borrowing and external borrowing*) | N (Separate company, therefore, agreed return made to States of Jersey) |
| Option 7 – Sale of freehold to a new social landlord | Y | Y | Y | Y (independent of States) | N |

*External borrowing for options 4, 5 and 6 would be taken out by States of Jersey or be States of Jersey supported

**See Appendix C for further information on leasehold and freehold considerations.

***Definition of surpluses

Projected surpluses which are treated as a contribution to States of Jersey, noted in the description of options, are defined as:

- ✚ Profit/(loss) reported in the annual financial statements adjusted as follows:

- ✚ Profit/(loss) on disposal of social housing stock is excluded as proceeds from such disposals are used to fund capital expenditure
- ✚ Depreciation is excluded as this is not a cash item
- ✚ Impairments to social housing stock are excluded as they are not cash items
- ✚ The capital element of new build loan repayments are deducted in order to retain the cash to make these repayments (which are made from additional income generated by the new build projects)

3.5 Update on assessment and conclusions of each Critical Success Factor

The assessment of each delivery option against each Critical Success Factor and associated assessment question has been updated.

The results of the updated assessment are noted in the remainder of this section.

3.5.1 Critical Success Factor – Self-sustaining social housing services provider

3.5.1.1 What scope is there to improve housing standards for tenants?

In line with the Outline Business Case, the assessment of the delivery of improved housing standards has focused on the stock condition survey investment requirements (Decent Homes Standard), as assessed for States of Jersey by Ridge and Partners.

This assessment:

- ✚ Excludes other types of investment (such as new build and refurbishment schemes), and
- ✚ Excludes any sale of social housing stock in order to maintain the stock size.

Under option 1, it is not possible to meet Decent Homes Standard because the business model cannot fund cash shortfalls (as all surpluses are returned to States of Jersey and there is no internal or external loan facility). Cash shortfalls arise because pre-transformation advances from States of Jersey are repayable in year 1. This option is ranked lowest of the options.

All other options enable Decent Homes Standard to be met and are therefore ranked joint first.

3.5.1.2 How accessible is the finance needed to pay for investment and delivery plans?

The sources of finance available to the new delivery organisation are as follows:

- ✚ Capital receipts from the sale of social housing stock
 - ✚ The 30 year business model incorporates the sale of 300 properties (15 per year for 20 years) at average proceeds of £366k. This is retained by the Housing Department in its current form to fund capital projects. This is an available source of finance for options 1 to 6
 - ✚ For option 7, sales proceeds would be returned to States of Jersey (net of expenses and rent lost as a result of the sale). Therefore, for option 7, sales of social housing stock would be cash neutral and not an available source of finance
- ✚ Retained surpluses
 - ✚ For options 1 to 5, surpluses are returned to States of Jersey. Therefore this is not a source of finance for options 1 to 5

- ✚ For option 6, an agreed return (described in section 3.4.2) is delivered to States of Jersey. Any surpluses in excess of the return to the States of Jersey are retained by the new delivery organisation. This provides the new organisation with the incentive to be more efficient and would be a source of finance where the surplus is in excess of the agreed return. However, this does not differentiate it from options 4 and 5 for this assessment question because the agreed return is expected to exceed the surplus for the first 8 years of the business model
- ✚ For option 7, surpluses are retained annually and so this is an available source of finance for the new organisation

- ✚ **Internal borrowing**
 - ✚ The States of Jersey have confirmed that an internal borrowing facility could be made available to the new delivery organisation under options 2 to 6. This is set out in R132/2011 States Investment Strategies which was presented to the States of Jersey on 1 November 2011 by the Treasury and Resources Minister. The Treasury Department has indicated that this could be a £40 million facility attracting fixed interest of 4% per annum, this will be formalised in the transfer agreement between States of Jersey and the new organisation.

- ✚ **External borrowing**
 - ✚ External borrowing would be utilised in options 4, 5 and 6 to fund new build projects and certain refurbishment projects as set out in section 3.3.4. As noted in section 3.3.4, the form of external borrowing for options 4, 5 and 6 is being considered at present which adversely impacts on the ranking of these options for this assessment question.
 - ✚ The option 7 debt is significantly higher than the other options, even though the landlord pays no returns to States of Jersey, because it has to buy the stock from States of Jersey. This high level of debt carries a higher interest rate risk than other options and finance costs would be higher for this option as no States of Jersey guarantee would be provided. Additionally, in the current economic climate, commercial lenders have limited appetite for this type and extent of lending therefore potentially making option 7 unviable. This has a significant adverse impact on the ranking of option 7 for this assessment question.

The table below summarises the available sources of finance for each of the delivery options. The rankings for each assessment are also noted in the table below.

| Option | Transfer of ownership of social housing assets | Capital receipts retained | Retained surpluses* | Borrowing | Interest rate risk | Finance sufficient to fund investment and delivery plans? | Ranking |
|---------------------------------|--|---------------------------|------------------------------|---------------------------------|--------------------|---|---------|
| 1 Status Quo | N | Y | N | None | None | N | 7 |
| 2 States Department | N | Y | N | Internal | Minimal | N | 5 |
| 3 ALMO | N | Y | N | Internal | Minimal | N | 5 |
| 4 Trading Operation | N | Y | N | Internal and external borrowing | Medium | Y | 1 |
| 5 Hybrid Trading Company | N | Y | N | Internal and external borrowing | Medium | Y | 1 |
| 6 Wholly Owned Housing Company | Y (freehold transfer) | Y | Yes (if above agreed return) | Internal and external borrowing | Medium | Y | 1 |
| 7 Newly Created Social Landlord | Y | N | Y | Independent of States | Highest | Y | 4 |

*Surpluses are returned under option 1 to 5 as the Housing Organisation would remain part of the States of Jersey. Under option 6 a new company would be formed enabling a contractual payment to the States of Jersey. Under option 7, the social housing stock is sold to a third party for a one-off payment on day one

Options 1, 2 and 3 do not have access to the finance needed to deliver investment and delivery plans and so rank the lowest.

Options 4, 5 and 6 have the ability to access to the finance needed to deliver investment and delivery plans (the form of the borrowing is currently being considered) as to the form and/or availability of such finance. These options are therefore ranked joint first.

Option 7 is ranked fourth because there is significant doubt that borrowing sufficient to fund the initial purchase would be obtainable by the new landlord.

Under option 7, the States of Jersey carries a further risk (through loss of income from property sales) if fewer than 15 properties are sold in a year (which is the assumption in the business modelling up to year 20).

This assessment question is also dealt with under the Critical Success Factor – Flexible delivery agent able to adapt to change: See section 3.5.2.2.

3.5.1.3 What freedom is there to re-invest efficiency gains and additional income streams?

At the Outline Business Case stage, the freedom to re-invest efficiency gains by way of reducing expenditure and generating additional income was considered as this incentivises management to operate more efficiently.

For the Full Business Case this question is extended to the freedom to manage capital receipts. This is because the freedom to manage capital receipts incentivises management to achieve higher sale proceeds, reduce the cost of sales and to effectively plan the timing of sales to support stock development projects and overall business model. It also provides incentives for better asset management, achieving the best performance from the available stock.

The table in the previous section summarises the potential for surpluses and capital receipts to be retained under each option.

A wholly owned Housing Company (option 6) retains surpluses in excess of the agreed return and capital receipts. This option has been ranked first for this question.

A newly created social landlord (option 7) would retain all surpluses. It would not, however, retain capital receipts from the sale of properties in years 1 to 20.

For options 1 to 5, all surpluses are returned to States of Jersey and capital receipts from the sale of properties are retained.

Options 1 to 5 and 7 have been ranked joint second.

3.5.1.4 How viable is the business model?

The basis of preparation of the business models

At the Outline Business Case stage, 30 year business models were prepared for the 7 options as noted in section 3.4.3. The business models for each option have been updated as described in section 3.4.

Borrowing assumptions

In calculating the level and length of period of borrowing, the following has been assumed:

Where there is no debt available (option 1):

- ✚ Surpluses (defined in section 3.4.3) are returned to States of Jersey
- ✚ Where cash shortfalls are generated this indicates that the business model is not viable

Where internal borrowing, but no external borrowing, is available (options 2 and 3):

- ✚ Surpluses (defined in section 3.4.3) are returned to States of Jersey
- ✚ Cash shortfalls are funded by internal debt up to the facility of £40m. This is repaid when cash surpluses become available
- ✚ Where cash shortfalls are generated this indicates that the business model is not viable

Where internal and external debt is available (options 4, 5 and 6):

- ✚ The applicable surpluses (defined in section 3.4.3) or agreed return (defined in section 3.4.2) are returned to States of Jersey
- ✚ External debt is used to finance new build projects. The debt is repaid using additional income generated by these projects (after deducting lost rent and operating expenses) and cash surpluses when available
- ✚ Cash shortfalls are funded by internal debt up to the facility of £40m. This is repaid when cash surpluses become available

- Remaining cash shortfalls are funded by external debt which is repaid when cash surpluses become available

Where external debt, but no internal debt, is available (option 7):

- Surpluses are retained in the business
- External debt is used to finance the initial purchase of the stock, new build projects and remaining cash flow shortages. The debt is repaid when cash surpluses become available

The basis of appraisal of the business models

The business models have been appraised based on the following criteria:

- Cash surplus at end of 30 year forecast period (2043)
- Amount and length of period of borrowing
- Peak bank overdraft (as there is no overdraft facility available, an overdraft indicates an unviable business model)
- Interest rate risk

The results of the business models

The table below summarises the relevant results and the ranking of the business models for each option.

| Option | NPV* of 30 year cash surplus | Internal borrowing | | External borrowing | | Cash shortfall | Interest rate risk | Ranking |
|---------------------------------------|------------------------------|--------------------|-------------|--------------------|-------------|----------------|--------------------|---------|
| | | Peak | Year repaid | Peak | Year repaid | | | |
| | | £000s | | £000s | | | | |
| 1 Status Quo | (1,181) | - | n/a | - | n/a | 167,303 | None | 7 |
| 2 States Department | - | 40,000 | 30+ | - | n/a | 128,450 | Minimal | 5 |
| 3 Arms Length Management Organisation | - | 40,000 | 30+ | - | n/a | 128,754 | Minimal | 5 |
| 4 Trading Operation | 4,748 | 40,000 | 19 | 113,010 | 16 | - | Medium | 2 |
| 5 Hybrid Trading Company | 4,712 | 40,000 | 19 | 113,316 | 16 | - | Medium | 2 |
| 6 Wholly Owned Housing Company | 63,656 | 40,000 | 18 | 159,538 | 16 | - | Medium | 1 |
| 7 Newly Created Social Landlord | 118,310 | - | n/a | 615,097** | 22 | - | Highest** | 4 |

*This represents the net present value ("NPV") of the cash balance at the end of the 30 year business model. The NPV is calculated using the inflated discount rate of 7.12% which is recommended by States of Jersey for this type of financial modelling. The NPV calculation estimates the cash surplus after taking in to account the time value of money. It is an estimate of the cash surplus as though it

were received immediately and not in the future, giving a 'real' indication of the amounts that will be generated

**Option 7 borrowing is significantly higher than other options due to the initial purchase of the stock. Option 7 interest rate risk is also highest for the new organisation due to the magnitude of the borrowing (interest rate is, however, low for States of Jersey as the payment for social housing stock is made up front)

Explanation of ranking

Options 1 to 3 do not have viable business models because there is insufficient funding available. Option 1 is ranked lowest because the cash shortfall is the highest (due to their being no internal debt available).

Options 4 to 7 have viable business models because:

- ✚ There are sufficient sources of finance available to fund the stock development plans
- ✚ The borrowing can be repaid within 20 years resulting in cash surpluses at the end of the plan. 20 years is the preferred borrowing period indicated by the Treasury Department as noted in section 3.3.4

Option 6 has higher cash surpluses than options 4 and 5. Option 6 requires a higher level of borrowing (compared to options 4 and 5) but it is within the facility indicated by Treasury and can be repaid earlier than the debt in options 4 and 5. Option 6 is ranked highest with options 4 and 5 joint second.

Option 7 generates the highest cash surpluses. However, high borrowing levels and high interest rate risk make the business model inherently more risky, particularly in the current economic climate. On balance, option 7 has been ranked fourth.

Option 6 external borrowing

Option 6 results differ from options 4 and 5 because under option 6 the agreed return is made to the States of Jersey. Under options 4 and 5 the surpluses are returned. For the first 8 years of the plan the return exceeds the surplus by a total of £38m.

In the later years of the option 6 business model, the surplus exceeds the return and so larger cash balances are accumulated.

3.5.1.5 Overall assessment

The table below summarises the results for the Critical Success Factor - Self-sustaining social housing services provider.

| Assessment question | Option 1 | Option 2 | Option 3 | Option 4 | Option 5 | Option 6 | Option 7 |
|--|----------|----------|----------|----------|----------|----------|----------|
| What scope is there to improve housing standards for residents? | 7 | 1 | 1 | 1 | 1 | 1 | 1 |
| How accessible is the finance needed to pay for investment and delivery plans? | 7 | 5 | 5 | 1 | 1 | 1 | 4 |
| What freedom is there to re-invest efficiency gains and additional income streams? | 2 | 2 | 2 | 2 | 2 | 1 | 2 |
| How viable is the business model? | 7 | 5 | 5 | 2 | 2 | 1 | 4 |
| Overall ranking | 7 | 5 | 5 | 2 | 2 | 1 | 4 |

Option 6 ranks highly as it has finance available to deliver stock development plans. It has the appropriate level of freedom to incentivise it to act efficiently and has a viable business model.

Option 7 is ranked fourth (compared to joint first at the Outline Business Case stage). This is because of the high interest rate risk associated with the high level of borrowing and doubt that sufficient commercial borrowing would be available. This is of particular importance in the current uncertain economic climate.

3.5.2 Critical Success Factor – Flexible delivery agent able to adapt to change

3.5.2.1 What capacity is there to deliver new housing?

The business models have been updated to incorporate actual stock development schemes noted in Appendix B. The same borrowing assumptions noted in section 3.5.1.4 have been used for this assessment.

In order to assess this criterion, the following has been considered:

- ✚ Can stock development plans be delivered?
- ✚ The level of borrowing
- ✚ The length of period of borrowing
- ✚ The interest rate risk associated with the borrowing

The results of these considerations are noted in the table below along with the rankings for each option.

| Option | Internal borrowing | | External borrowing | | Cash shortfall | Interest rate risk | Ranking |
|---------------------------------------|--------------------|-------------|--------------------|-------------|----------------|--------------------|---------|
| | Peak | Year repaid | Peak | Year repaid | | | |
| | £000s | | £000s | | | | |
| 1 Status Quo | - | n/a | - | n/a | 167,303 | None | 7 |
| 2 States Department | 40,000 | 30+ | - | n/a | 128,450 | Minimal | 5 |
| 3 Arms Length Management Organisation | 40,000 | 30+ | - | n/a | 128,754 | Minimal | 5 |
| 4 Trading Operation | 40,000 | 19 | 113,010 | 16 | - | Medium | 1 |
| 5 Hybrid Trading Company | 40,000 | 19 | 113,316 | 16 | - | Medium | 2 |
| 6 Wholly Owned Housing Company | 40,000 | 18 | 159,538 | 16 | - | Medium | 3 |
| 7 Newly Created Social Landlord | - | n/a | 615,097 | 22 | - | Highest | 4 |

Options 1 to 3 cannot deliver the stock development plans due to insufficient funding and so are ranked lowest. Due to the ability to borrow £40m internally, options 2 and 3 rank higher than option 1.

Options 4 to 7 can deliver the stock development plans and repay external loans within 20 years.

Options 4 and 5 are ranked first and second respectively because they have the lowest level of debt over a shorter period of the viable options. Option 6 is ranked third as it has the next highest level of debt (due to the agreed return to the States of Jersey under

option 6 being higher than the surpluses returned to the States of Jersey under options 4 and 5).

Option 7 is ranked lowest of the viable options. The interest rate risk associated with the level of borrowing and doubt that sufficient commercial borrowing would be available makes this option less viable.

3.5.2.2 How accessible is the finance needed to pay for investment and delivery plans?

This assessment question is also dealt with under the Critical Success Factor – Self-sustaining social housing services provider in section 3.5.1.2. Taking in to consideration the change in emphasis noted below, options 4 to 7 continue to be ranked most highly of the available options for the same reasons noted in section 3.5.1.2.

The emphasis for the assessment question under this Critical Success Factor (Flexible delivery agent able to adapt to change) is extended to the criteria noted in the table below. Rankings are also noted in the table below.

| Option | Finance sufficient to fund investment and delivery plans? | Freedom to re-invest capital receipts | Ability to utilise surpluses | Freedom to access borrowing | Interest rate risk | Overall |
|---------------------------------------|---|---------------------------------------|------------------------------|-----------------------------|--------------------|---------|
| 1 Status Quo | N | 5 | 2 | 7 | None | 7 |
| 2 States Department | N | 5 | 2 | 6 | Minimal | 6 |
| 3 Arms Length Management Organisation | N | 3 | 2 | 5 | Minimal | 5 |
| 4 Trading Operation | Y | 4 | 2 | 3 | Medium | 3 |
| 5 Hybrid Trading Company | Y | 2 | 2 | 2 | Medium | 2 |
| 6 Wholly Owned Housing Company | Y | 1 | 2 | 1 | Medium | 1 |
| 7 Newly Created Social Landlord | Y | 7 | 1 | 4 | Highest | 4 |

The assessment of the freedom to re-invest capital receipts is linked to the level of autonomy of each option (except for option 7 as capital receipts are not retained by the organisation).

Option 7 scores highest on the ability for the organisation to retain surpluses as it makes no annual return to States of Jersey. Option 6 is able to retain profits in excess of the agreed return, however, this does not influence the rankings as the return to be made by option 6 is in excess of the surplus for the first 12 years of the business model.

The freedom to access finance is assessed as follows:

- ✚ Option 1: No borrowing available
- ✚ Options 2 and 3: Internal borrowing only available. Option 3 more favourable of the two due to the organisation being arms length and therefore more likely to have a robust loan agreement in place
- ✚ Options 4, 5 and 6: Internal and external borrowing available. External debt would be taken out by States of Jersey on behalf of the operation as noted in section 3.3.4. The ranking of these options is linked to the level of autonomy of each option
- ✚ Option 7: External borrowing could be secured on the assets of the business. However, in the current economic climate the freedom to access finance is reduced due to the limited availability of commercial borrowing

3.5.2.3 What autonomy is there to make independent decisions and service delivery?

The assessment of the options is on the same criteria as at the Outline Business Case stage, which was the ability of the new organisation to:

- ✚ Decide on its own organisational and staffing structures
- ✚ Specify services and standards
- ✚ Make independent procurement decisions

The results of the analysis, and the associated rankings, are summarised below.

| Option | Ability of the organisation to: | | | Ranking |
|---------------------------------------|---|--------------------------------|--|---------|
| | Decide on own organisational and staffing structure | Specify services and standards | Make independent procurement decisions | |
| 1 Status Quo | None | None | None | 6 |
| 2 States Department | None | None | None | 6 |
| 3 Arms Length Management Organisation | Low | Low | Minimal | 4 |
| 4 Trading Operation | Minimal | Minimal | Minimal | 5 |
| 5 Hybrid Trading Company | Medium | Medium | Medium | 3 |
| 6 Wholly Owned Housing Company | High | High | High | 2 |
| 7 Newly Created Social Landlord | Highest | Highest | Highest | 1 |

Options 5 to 7 provide for the greatest levels of autonomy. Option 7 ranks highest because, while it would need to work closely with States of Jersey, it would not be owned by States of Jersey.

Under Option 2 housing would continue to be owned and directly provided by a department of the States, which offers the same level of autonomy as available under the Status Quo.

Option 3 has more independence than option 4 and so is ranked higher of the two options.

Overall assessment

The table below summarises the results for the Critical Success Factor – Flexible delivery agent able to adapt to change

| Assessment question | Option 1 | Option 2 | Option 3 | Option 4 | Option 5 | Option 6 | Option 7 |
|---|----------|----------|----------|----------|----------|----------|----------|
| What capacity is there to deliver new housing? | 7 | 5 | 5 | 1 | 2 | 3 | 4 |
| How accessible are sources of finance needed to pay for investment and delivery plans? | 7 | 6 | 5 | 3 | 2 | 1 | 4 |
| What autonomy is there to make independent decisions on procurement and service delivery? | 6 | 6 | 4 | 5 | 3 | 2 | 1 |
| Overall ranking | 7 | 6 | 5 | 3 | 2 | 1 | 3 |

Option 5 and 6 are the most highly ranked options. Option 6 is ranked highest based on its total score.

Option 6 scores less well on the first assessment question due to the higher level of debt required compared to options 4 and 5 (due to the return to States of Jersey being higher for option 6 for the first 12 years of the plan).

Option 7 is ranked third compared to first at the Outline Business Case stage. This is largely due to the increased interest rate risk associated with the high level of borrowing required for the initial purchase of social housing stock. Additionally, there is some doubt that commercial funding would be available for this option.

3.5.3 Critical Success Factor – Significant income stream

3.5.3.1 What is the level of income stream available to States of Jersey?

The net present value of income streams available to States of Jersey are noted in the table below, along with their relative rankings. The income streams are calculated as described in section 3.4.3.

| Option | Form of income stream | Including stock development plans | | | Payments to States of Jersey continue beyond 30 year business model | Ranking |
|---------------------------------------|-----------------------|-------------------------------------|-----------------------------------|--|---|---------|
| | | NPV* of total payments in years 1-5 | NPV* of total payments years 1-30 | Cash available to deliver payments to States of Jersey | | |
| | | £000s | £000s | | | |
| 1 Status Quo | Surplus | 110,611 | 601,185 | N | Y | 7 |
| 2 States Department | Surplus | 111,043 | 630,783 | N | Y | 5 |
| 3 Arms Length Management Organisation | Surplus | 103,041 | 604,022 | N | Y | 6 |
| 4 Trading Operation | Surplus | 97,985 | 581,547 | Y | Y | 2 |
| 5 Hybrid Trading Company | Surplus | 89,941 | 554,669 | Y | Y | 3 |
| 6 Wholly Owned Housing Company | Agreed return | 115,833 | 472,835 | Y | Y | 1 |
| 7 Newly Created Social Landlord | Tenanted market value | 471,012 | 532,302 | Y | N | 4 |

*This represents the Net Present Value ("NPV") of total payments to States of Jersey over the period noted above. The NPV is calculated using the inflated discount rate of 7.12% which is recommended by States of Jersey for this type of financial modelling. The NPV calculation estimates the total payments after taking in to account the time value of money. It is an estimate of the total payments as though they were received immediately and not in the future, giving a 'real' indication of the amounts that will be generated

Options 1 to 3 are ranked lowest because they do not have cash available to deliver the surplus to States of Jersey. (The surpluses are higher for options 1, 2 and 3 because they do not include interest payments for cash shortfalls (this is consistent with the options described in Appendix C).

Options 4 to 6 are able to deliver required payments to States of Jersey. They are ranked in order of total payments in years 1 to 5. Options 4 and 5 return the most to States of Jersey over 30 years but, on balance, it is considered less desirable than option 6 due to the lower payments in years 1 to 5 which means that the required return is not delivered in all years of the business model.

Option 7 is ranked lowest of the viable options. Although option 7 appears to provide the highest income streams for States of Jersey and delivers the majority of them in year 1,

beyond the initial 30 year business model no further payments are made to States of Jersey (other than in tax revenue if applicable). For other options, the income stream continues indefinitely which makes them more preferable.

The above rankings incorporate current stock development plans. If Decent Homes Standard was achieved with no other stock development the relative rankings would change as options 2 to 7 would be viable and loan interest would be substantially lower. In this scenario, the options with the lowest additional costs are more preferable (Option 2 ranks highly in this scenario).

The rankings taken forward are those that incorporate the stock development plans as this is the option being modelled in this Economic Case.

3.5.3.2 How does the income stream compare with States of Jersey requirements?

The appraisal of income streams above provides a comparison between each of the delivery options but not against the income stream which is required by States of Jersey.

The States of Jersey income stream requirement is described in section 3.4.3. Income streams generated by each option are noted in the table below along with the relative rankings. Option 6 is designed to deliver the income stream required by States of Jersey.

| Option | Including stock development plans | | | | Cash available to deliver payments to States of Jersey | Payments to States of Jersey continue beyond 30 year business model | Ranking |
|---------------------------------------|-----------------------------------|------------------------------------|------------------------------------|-----------------------------------|--|---|---------|
| | NPV* of total payments years 1-10 | NPV* of total payments years 11-20 | NPV* of total payments years 21-30 | NPV* of total payments years 1-30 | | | |
| | £000s | £000s | £000s | £000s | | | |
| 1 Status Quo | 233,915 | 203,644 | 163,625 | 601,185 | N** | Y | 7 |
| 2 States Department | 239,529 | 216,122 | 175,132 | 630,783 | N** | Y | 5 |
| 3 Arms Length Management Organisation | 226,388 | 208,152 | 169,482 | 604,022 | N** | Y | 6 |
| 4 Trading Operation | 200,605 | 203,175 | 177,767 | 581,547 | Y | Y | 2 |
| 5 Hybrid Trading Company | 187,380 | 195,172 | 172,117 | 554,669 | Y | Y | 3 |
| 6 Wholly Owned Housing Company | 213,632 | 151,677 | 107,526 | 472,835 | Y | Y | 1 |
| 7 Newly Created Social Landlord | 493,514 | 38,788 | - | 532,302 | Y | N | 4 |

*This represents the Net Present Value ("NPV") of total payments to States of Jersey over the period noted above. The NPV is calculated using the inflated discount rate of 7.12% which is recommended by States of Jersey for this type of financial modelling. The NPV calculation estimates the total payments after taking in to account the time value of money. It is an estimate of the total payments

as though they were received immediately and not in the future, giving a 'real' indication of the amounts that will be generated

**The cash payments represent the surpluses generated (as defined in section 3.4.3). However, there is insufficient cash available to deliver the surplus to the States of Jersey and deliver the stock development plans for options 1 to 3 making their business models unviable. This is because there are insufficient sources of finance for options 1 to 3. As no finance is available, no account is taken in the business models for options 1 to 3 for interest charges that would be applied on cash shortfalls

Option 6 is ranked first because the income stream generated is in line with States of Jersey requirements.

Options 1 to 3 are not able to make the payments to the States of Jersey due to cash shortfalls in the first 20 years of the business model and there being insufficient sources of finance available. The business models for options 1 to 3 are therefore not viable. They are therefore ranked lowest of the options in order of their 30 year return.

Options 4 and 5 have a viable business model because they are able to deliver the payments to the States of Jersey and deliver stock development plans. The level of payments to the States of Jersey for options 4 and 5 is lower than the required return in the first 7 and 9 years of the plan respectively. However, over the 30 year period they return more than the required return. On balance, they are ranked second and third due to the requirement for the return to be sustained in all years of the business model.

Option 7 is ranked fourth. The income stream exceeds States of Jersey requirements for the 30 year business model. However, option 7 would provide no further income streams beyond the 30 year business model and the States of Jersey expectation is that the income stream would be maintained in real terms from 2014.

3.5.3.3 What are the external factors that might influence this income stream?

In line with considerations at the Outline Business Case stage, there are external factors that present risks associated with the income stream each option would generate. These include:

- ✚ Increases in the cost of finance
- ✚ Costs caused by delays in delivery of investment
- ✚ Restrictions on realising efficiencies
- ✚ Changes to social rent policy
- ✚ Lower sales of properties than forecast
- ✚ Falls in the market value of properties sold

Changes to social rent policy would impact equally against all of the options (except option 1). Prudent assumptions have been made where possible to counteract the risks, but they still have the potential to affect delivery under each of the options. It is difficult to make prudent assumptions to mitigate risks that are caused by an organisation's reduced autonomy to make independent decisions, and so these areas have a greater impact on rankings.

Change in market rents would also impact equally against all of the options (except option 1). Sensitivity analysis is performed for this risk in section 5.7.6.

The table below summarises the overall assessment of each option's exposure to these risks which is further explained in Appendix D.

| Option | Risk to States of Jersey | Ranking |
|--|--------------------------|---------|
| Status Quo – Option 1 | Medium | 7 |
| States Department – Option 2 | Medium | 5 |
| Arms Length Management Organisation – Option 3 | Medium | 5 |
| Trading Operation – Option 4 | Medium | 4 |
| Hybrid Trading Company – Option 5 | Low to medium | 2 |
| Wholly Owned Housing Company – Option 6 | Mostly low | 1 |
| Newly Created Social Landlord – Option 7 | Low to medium | 3 |

Options 5 and 6 are ranked most highly because they provide for the lowest element of risk transfer affecting the income stream.

Option 7 (Newly Created Social Landlord) ranks third. Risk is transferred effectively from States of Jersey to the new Landlord and the main income stream is received as a capital receipt in year 1. However, interest rate risk associated with option 7 is high due to the high level of borrowing required. This increased interest rate risk would apply, in the first instance, to the new organisation and not the States of Jersey. However, there is a secondary risk to States of Jersey that, as a result of higher interest rate costs, the new organisation would not be able to deliver the planned investment or ultimately that it would fail and need support from States of Jersey.

Options 1 to 4 score less well because there is potential for decisions made in other parts of States of Jersey to impact on their ability to deliver the required income stream.

The scores for the remaining options reflect the differing extents to which risk can be externalised, or met from the available resources. The Status Quo option ranks lowest, because no risk is transferred and it has the least resources available.

3.5.3.4 Overall assessment

The table below summarises the results for the Critical Success Factor – Significant income stream.

| Assessment question | Option 1 | Option 2 | Option 3 | Option 4 | Option 5 | Option 6 | Option 7 |
|--|----------|----------|----------|----------|----------|----------|----------|
| What is the level of income stream available to States of Jersey? | 7 | 5 | 6 | 2 | 3 | 1 | 4 |
| How does the income stream compare with States of Jersey requirements? | 7 | 5 | 6 | 2 | 3 | 1 | 4 |
| What are the external factors that might influence this income stream? | 7 | 5 | 5 | 4 | 2 | 1 | 3 |
| Overall ranking | 7 | 5 | 6 | 2 | 2 | 1 | 4 |

Option 6 is ranked first as it is able to deliver the agreed income stream to States of Jersey. Options 1 to 5 are expected to deliver a lower return to States of Jersey for the first 12 years of the business models.

Option 7 would deliver a higher return to States of Jersey in the 30 year business model (including the initial purchase). However, it would not return any further funds to States of Jersey after 30 years whereas the other options would deliver a return indefinitely.

3.5.4 Critical Success Factor – Separate regulatory, policy and service functions

The assessment criteria and conclusions for this Critical Success Factor have been reconsidered and have not changed since the Outline Business Case stage. The text from the Outline Business Case has been repeated in this FBC for convenience.

The final key Critical Success Factor identified for the Housing Transformation Programme is the delivery of 'fully separate Regulatory, Policy and Service functions'. At present the States of Jersey housing department combines housing policy delivery with operational housing management and regulatory role. There is no separate regulatory function in existence, which means that both the States of Jersey housing and the other providers of social housing, e.g. the Housing Trusts, are not open to external review.

Proposed changes reflecting best practice are for a light touch, proportional approach to regulation, with the regulator, social housing providers and tenants all having a role in ensuring that services are provided at the highest possible standard.

The housing policy function for the States of Jersey would encompass the whole housing market, including the private sector, and the separation of functions will enable a broader focus. This will be located in the Strategic Housing Unit.

The extent to which each of the 7 delivery options would facilitate the achievement of this Critical Success Factor has been analysed by considering two questions:

3.5.4.1 How separate are the regulatory, policy and delivery functions?

As set out above, under the current situation (option 1) there isn't any separation between these functions. This would be the case for the Status Quo option and the States Department option. With the Arms Length Management Organisation and Trading Operation options decisions on social housing policy are expected to be made by States of Jersey with delivery of services being managed by the delivery vehicle and regulation being administered by a new independent regulator. However, these models would both have strong links with States of Jersey and the Housing Department and therefore some of the benefits associated with full separation may be reduced.

The Hybrid Trading Company and wholly owned Housing Company options are likely to have a greater degree of separation, operating as independent enterprises, albeit within a States of Jersey reporting framework, and therefore more able to focus on the delivery of housing services. Under option 5, States of Jersey would retain ownership of the assets and govern the regulation creating a potential conflict of interest.

Finally, the new social housing landlord option would operate outside the States of Jersey reporting framework and would provide greater freedom for the delivery vehicle to develop its own methodology for delivering services, for example by collaborating with other housing companies and landlords or perhaps outsourcing some services.

A summary of the relative ranking of the delivery options against the objective of achieving separation between the regulatory, policy and service functions is set out in the table below.

| Option | Level of separation | Ranking |
|--|---------------------|---------|
| Status Quo – Option 1 | Low | 6 |
| States Department – Option 2 | Low | 6 |
| Arms Length Management Organisation – Option 3 | Medium | 4 |
| Trading Operation – Option 4 | Low to Medium | 5 |
| Hybrid Trading Company – Option 5 | Medium to High | 3 |
| Wholly Owned Housing Company – Option 6 | High | 2 |
| Newly Created Social Landlord – Option 7 | Highest | 1 |

3.5.4.2 How independent is governance of the delivery organisation?

There are benefits and value to having independent governance of the delivery vehicle: the full focus of Board Directors is on delivering the objectives of the organisation, with the interests of tenants at its heart. As all Board Directors would have a primary responsibility to act in the best interests of the delivery vehicle it should minimise potential conflicts of interests.

Independent governance would not be possible with the Status Quo, States Department or Trading Operation options. It would be a key feature of the Arms Length Management Organisation option but again it is likely that the governing body would be subject to political influence from States of Jersey.

The governing bodies for the Hybrid Trading Company and wholly owned Housing Company options are expected to be subject to less influence from States of Jersey and better able to focus on the delivery of housing services but still subject to a reporting requirement. Again, the greatest degree of independence would be available to the New Social Landlord option.

The relative ranking against this question is set out below.

| Option | Level of independence | Ranking |
|--|-----------------------|---------|
| Status Quo – Option 1 | None | 6 |
| States Department – Option 2 | None | 6 |
| Arms Length Management – Option 3 | Low | 4 |
| Trading Operation – Option 4 | Minimal | 5 |
| Hybrid Trading Company – Option 5 | Medium | 3 |
| Wholly Owned Housing Company – Option 6 | High | 2 |
| Newly Created Social Landlord – Option 7 | Highest | 1 |

The potential impact of not separating the policy, regulatory and service functions is high. Separation will provide greater focus for each of the three areas on their core functions.

For all options except Options 1 and 2 there is a strong likelihood of separation taking place.

3.5.4.3 Overall assessment

The rankings below are based on an assessment of the options against the separation of functions and the level of independence of the governance of the delivery vehicle.

| Assessment question | Option 1 | Option 2 | Option 3 | Option 4 | Option 5 | Option 6 | Option 7 |
|--|----------|----------|----------|----------|----------|----------|----------|
| How separate are the regulatory, policy and service functions? | 6 | 6 | 4 | 5 | 3 | 2 | 1 |
| How independent is governance of the delivery organisation? | 6 | 6 | 4 | 5 | 3 | 2 | 1 |
| Overall ranking | 6 | 6 | 4 | 5 | 3 | 2 | 1 |

It is the level of independence for each delivery option that guides this assessment.

3.6 Update risk and legal aspects

3.6.1 Risk analysis

The assessment of the inherent risks for each option from the Outline Business Case have been updated. In preparing the assessment the likelihood of the risk of failing to deliver for each Critical Success Factor has been taken in to account. The same risks have been considered at the Outline Business Case and Full Business Case stage, which are noted in the table below:

| Key risk | Factors | Reasons for considering |
|---|--|---|
| Delivery vehicle is not self-sustaining | Investment shortfalls | Affects the ability to deliver the necessary investment |
| | Available sources of finance | Identify any external factors that could reduce the availability of finance to deliver investment |
| | Ability to re-invest efficiencies and surpluses | Incentivises the organisation to generate resources from improving value for money and re-invest them in the stock |
| | Business model viability | Covers risks associated with funding certainty, cost and availability of self-generated resources |
| Delivery vehicle is not flexible and able to adapt to change | Scope to generate capacity to deliver new units and service improvements | Review debt levels and the ability to repay debt quickly, providing capacity for further investment |
| | Available sources of finance | Identify any external factors that could reduce the availability of finance to deliver additional investment |
| | Autonomy to make delivery and procurement decisions | Identify potential constraints, which might prevent the organisation from making decisions in the best interests of services to tenants |
| | Independence of governance | |
| Required income stream is not delivered | Income stream (net present value) delivered over 30 years | Long term assessment of the income stream generated |
| | Performance against net present value required over 30 years | Comparison of the income stream generated in the long term with the long term contribution requirement |
| | Cash flows generated over 10 years | Assessment of cash flows generated for States of Jersey in the early years of the business model |
| | External factors affecting the income stream | Identify the risk of external factors preventing delivery of the income stream |
| Regulatory, policy and service delivery functions not separated | Separation of the service delivery, policy and regulatory functions | Presence of checks and balances that encourage tenant-focused housing management and investment |
| | Independence of governance | Focus of the governing body on delivering the best outcomes for tenants |

The updated results of the analysis are summarised in the table below.

These results are placed alongside the assessment of the rankings in section 3.8.1, below.

Option 6 offers the lowest risk to States of Jersey because it has sufficient separation from States of Jersey and sufficient sources of finance to be self-sustaining and deliver stock development plans without the level of interest rate risk associated with option 7.

Option 7 is higher in risk than option 6 because the scale of borrowing increases interest rate risk which could jeopardise the organisation's ability to be self-sustaining and adaptable. At current projected debt levels, and given the current economic climate, option 7 may not be fundable.

Option 5 offers low to medium risk to States of Jersey because it is self-sustaining, but cannot deliver the required return to States of Jersey and has a lesser degree of separation from States of Jersey when compared to options 6 and 7.

The reasons for the risk assessments for each option are noted in Appendix A.

| Option | Not self-sustaining | Not flexible/adaptable | Required income stream not delivered | Poor separation of functions | Overall |
|--|---------------------|------------------------|--------------------------------------|------------------------------|----------------|
| Status Quo – Option 1 | High | High | High | High | High |
| States Department – Option 2 | High | High | High | High | High |
| Arms Length Management Organisation – Option 3 | High | Medium | High | Medium | Medium to High |
| Trading Operation – Option 4 | Low | Medium | Medium | Medium to High | Medium |
| Hybrid Trading Company – Option 5 | Low | Low | Medium | Low to Medium | Low to Medium |
| Wholly Owned Housing Company – Option 6 | Low | Low | Low | Low | Low |
| Newly Created Social Landlord – Option 7 | Medium | Low | Low | Low | Low to Medium |

Certain risks remain in the business models due to future uncertainties such as RPI levels, financing costs and property sales (number of units and sales price). Risks have been mitigated by being prudent in the assumptions that form the basis of the business modelling. This will be explored further for the preferred option by performing sensitivity analysis. The results will be documented in section 5 - Financial Case.

3.6.2 Legal aspects

The legal aspects considered at the Outline Business Case stage are largely unchanged since that time. The updated text from the Outline Business Case has been noted below.

Options 3 to 7 would require varying degrees of legal involvement to ensure that the delivery organisation is properly constituted and governed effectively. Provision for these costs has been incorporated into the cash flows.

Establishing a wholly owned Housing Company (Option 6) or a Newly Created Social Landlord (Option 7) would require conveyance of the stock to the new organisation. Option 6 would also require a Transfer Agreement between States of Jersey and the new organisation.

Option 7 would also require development of a transfer agreement, setting out the terms of the transfer, legally binding obligations on both the new Landlord and States of Jersey (including guarantees, warranties and rights that form part of the agreement).

3.7 Sensitivity analysis

The options have been assessed against the Critical Success Factors on a consistent basis. Sensitivity analysis has not been performed as part of the Economic Case because variables (such as proposed rent policy implementation, stock development plans and

inflation rates) would impact all relevant options equally and therefore not impact relative rankings.

A full sensitivity analysis, including “worst case scenario”, has been conducted for the preferred option and is documented in section 5.7 of the Financial Case.

3.8 Summary and conclusions

3.8.1 Summary of analysis

The assessment of each of the options at the Outline Business Case stage against the Critical Success Factors identified at the outset of the Housing Transformation Programme have been updated. The Critical Success Factors have also been reconsidered and are still considered to be an appropriate basis for the assessment.

The Economic Case summarises the assessment and produces a relative ranking for each option. Taken together, these rankings take into account a broad range of considerations linked to the business models and financing of each option.

The following table provides a summary of the updated assessment for each Critical Success Factor, along with an overall ranking for each of the 7 options.

| Critical Success Factor | Status Quo | States Dept | Arms Length Mgmt Org. | Trading Operation | Hybrid Company | Wholly Owned Housing Company | Sale |
|---|------------|-------------|-----------------------|-------------------|----------------|------------------------------|---------------|
| | Option 1 | Option 2 | Option 3 | Option 4 | Option 5 | Option 6 | Option 7 |
| Ability to deliver a self-sustaining social housing services provider | 7 | 5 | 5 | 2 | 2 | 1 | 4 |
| Flexible delivery organisation | 7 | 6 | 5 | 3 | 2 | 1 | 3 |
| Income stream | 7 | 5 | 6 | 2 | 2 | 1 | 4 |
| Regulatory, policy & service functions | 6 | 6 | 4 | 5 | 3 | 2 | 1 |
| Overall ranking at FBC stage | 7 | 6 | 5 | 3 | 2 | 1 | 4 |
| Overall Risk | High | High | Medium to High | Medium | Low to Medium | Low | Low to Medium |

3.8.2 Conclusions

Option 6 ranks highly against all Critical Success Factors and offers the lowest risk. Stock development plans can be delivered as can the expected return to States of Jersey. A separate landlord function and the availability of finance provide the required independence and autonomy. Option 6 is, therefore, the preferred option.

Options 4 and 5 are ranked third and second respectively. They are viable options because they have viable business models that enable them to deliver the stock development plans and return surpluses to States of Jersey. They are not as preferable as options 6 because the income stream to States of Jersey is lower than States of Jersey expectations and they have a lower degree of separation from States of Jersey and other Housing functions.

Option 7 is ranked fourth overall. The return option 7 can deliver to States of Jersey is in excess of States of Jersey expectations for the 30 year business model, however, States of

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Jersey would lose all rights to the social housing stock and income streams beyond the initial 30 year plan. Additionally, the risk is higher than option 6 due to increased interest rate risk associated with the high level of borrowing required for the initial purchase. This increased interest rate risk would apply, in the first instance, to the new organisation and not the States of Jersey. However, there is a secondary risk to States of Jersey that, as a result of higher interest rate costs, the new organisation would not be able to deliver the planned investment or ultimately that it would fail and need support from States of Jersey.

Options 2 and 3 are viable in that they can deliver Decent Homes Standard within 10 years and return surpluses to States of Jersey. However, the surpluses returned are lower than States of Jersey expectations and they cannot deliver any significant stock development.

Option 1 is not viable as it cannot deliver Decent Homes Standard within 10 years.

The Commercial Case within this FBC sets out the parameters for the commercial arrangements between the two parties and the Financial Case provides a summary of the projected financial implications for States of Jersey of the preferred option.

4 Commercial case

4.1 Introduction

This section of the business case sets out the commercial case for the preferred option as identified in the Economic Case of this document, a wholly States owned Social Housing Management Organisation. Its purpose is to summarise the commercial, partnering and personnel arrangements that will deliver the identified project benefits and the key success factors for the programme. It therefore considers the services to be transferred and how expected costs and benefits can be controlled through contractual arrangements.

4.1.1 Key Critical Success Factors

The following key Critical Success Factors have been identified for the Programme.

| Critical Success Factor | Assessment questions |
|---|--|
| Self-sustaining social housing services provider | <p>What scope is there to improve housing standards for residents?</p> <p>How accessible is the finance needed to pay for investment and delivery plans?</p> <p>What freedom is there to re-invest efficiency gains and additional income streams?</p> <p>How viable is the business model?</p> |
| Flexible delivery organisation able to adapt to change | <p>What capacity is there to deliver new housing – e.g. ‘housing for life’ (strategic priority no. 14)?</p> <p>How accessible is the finance needed to pay for investment and delivery plans?</p> <p>What autonomy is there to make independent decisions on procurement and service delivery?</p> |
| Continued significant income stream to States of Jersey | <p>What is the level of income stream available to States of Jersey?</p> <p>How does the income stream compare with States of Jersey estimates?</p> <p>What are the external factors that might influence this income stream?</p> |
| Fully separate Regulatory, Policy and Service functions | <p>How separate are the service, regulatory and policy functions?</p> <p>How independent is governance of the delivery organisation?</p> |

4.1.2 Further objectives

Furthermore in developing the new organisation, it has been identified that the Programme should endeavour to:

- ✚ Provide increased “housing for life” accommodation
- ✚ Improve housing standards for residents
- ✚ Determine the appropriate level that will set fair rents at a sustainable subsidised level
- ✚ Deliver a modernising transformation that offers best value for Tenants and the States of Jersey

4.1.3 Summary

The commercial arrangements between the two parties are important to achieve these success factors and to protect the interests of both the States of Jersey and the Wholly States owned Social Housing Management Organisation. They need to strike an appropriate balance between the transfer of risk to the new organisation and the certainty of delivery of items such as the requirement for an ongoing annual revenue contribution to the States of Jersey. This will be particularly important when arranging the required external borrowing.

This section of the Full Business Case identifies the key risk areas and includes, at Appendix E, a matrix setting out what key risks are being transferred to the new company, which are retained by States of Jersey and those shared.

The commercial arrangements are also key to ensuring that there are good ongoing partnership arrangements to the benefit of the two parties and the current tenants of the States of Jersey and potential future tenants. It is critical to identify what and who is transferring to the new landlord both in terms of properties, land, assets and liabilities and staff.

All these arrangements are eventually contained within a Transfer Agreement which will need to be negotiated and agreed between the two parties.

4.2 Transfer Agreement

The heads of terms for the Housing Company enabling law are noted below.

4.2.1 The Company

4.2.1.1 Corporate form

- ✚ Company limited by guarantee
- ✚ Exercise of the States of Jersey powers in relation to its interest and rights in the Housing Company

4.2.1.2 States of Jersey interest in the Housing Company

- ✚ Variable representation for the States of Jersey on the board of the Housing Company
- ✚ States of Jersey sole membership of the Housing Company (as guarantor)

4.2.1.3 Loans etc. to the Housing Company

- ✚ States of Jersey entitlement to make loans and grants, subject to any conditions it sees fit
- ✚ States of Jersey entitlement to guarantee loans made to the Housing Company (or a subsidiary/group entity) by a third party
- ✚ States of Jersey entitlement to guarantee, discharge and/or assume liabilities of the Housing Company

4.2.1.4 Annual return to States of Jersey

- ✚ The Housing Company shall make an annual return as set out in the Transfer Agreement or otherwise as agreed/stipulated from time to time
- ✚ The initial and any subsequent stipulated/agreed annual return may be secured against the Housing Company's assets

4.2.2 Transfer of assets and liabilities

4.2.2.1 Transfer date

- ✚ One transfer date only
- ✚ Date is prescribed in Regulations

4.2.2.2 Transfer of movables

- ✚ Assets, rights and liabilities as described in Regulations shall be transferred to the Housing Company in accordance with those Regulations
- ✚ The transfer may be made on terms and conditions prescribed in the Regulations
- ✚ The extent of any existing assets, rights or liabilities may be specified in Regulations to remove difficulties or uncertainties

4.2.2.3 Transfer of immovables

- ✚ Assets specified in the Regulations shall be transferred to the Housing Company in accordance with those Regulations
- ✚ The transfer may be made on such terms and conditions as are prescribed in Regulations
- ✚ The extent of any existing assets, rights or liabilities may be specified in Regulations to remove difficulties or uncertainties

4.2.2.4 Vesting in the Housing Company

- ✚ Assets vest without need for further conveyance etc
- ✚ Rights and liabilities transfer automatically (in accordance with Jersey Telecom precedent)
- ✚ Current proceedings are taken to be proceedings against the Housing Company
- ✚ Acts or omissions by the States of Jersey are deemed to be acts or omissions by the Housing Company
- ✚ Exclusion of contractual and other claims by third parties
- ✚ No compensation (except as provided in Regulations)

4.2.2.5 Evidence, registration and treatment of transfer

- ✚ A signed copy of the Regulations is conclusive evidence of transfer/vesting of movables
- ✚ A signed copy of the Regulations specifying immovable property transferred to the Housing Company is to be registered in the Public Registry of Contracts
- ✚ Valuation of assets, rights and liabilities and accounting for them by the States and for other purposes – but no 'purchase price' for the stock etc

4.2.2.6 Stamp duty

- ✚ Not chargeable on the transfer to the Housing Company; or
- ✚ Following transfer, as prescribed in Regulations

4.2.2.7 Future disposals

- ✚ Control of disposals (including any grant of security to lenders) by the Social Housing Regulator
- ✚ General/initial consents for disposals to meet third party funding obligations and yearly consents to permit sales as agreed as part of the business plan approval process

4.2.3 Tenancies

4.2.3.1 Existing tenancies

- ✚ Existing tenants will be transferred under regulation to new tenancies with equivalent terms
- ✚ The tenancies will remain contractual

4.2.3.2 Future tenancies

- ✚ Conversion of existing form (into Island-wide standard, tied to Regulation and exemption from the rent control law of 1946)

4.2.4 Staff

4.2.4.1 Transfer of staff

- ✚ Employees of the Housing Department (save as specified) will become employees of the Housing Company

- ✚ Contracts of employment will take effect as if they had been made between the employees and the Housing Company
- ✚ All rights, powers, duties and liabilities will be enforceable or exercisable as if the contracts had originally been made between the employees and the Housing Company
- ✚ Acts done prior to transfer by the States of Jersey (through the Housing Department) will be taken to have been done by the Housing Company
- ✚ Collective agreements will continue to have effect
- ✚ Assumed that all staff will transfer or be subject to redeployment

4.2.4.2 Saving of rights under retirement schemes

- ✚ Retirement scheme rights for Public Employees are unaffected
- ✚ The Company becomes an Admitted Body to the Pension Scheme and the employer of those Public Employees
- ✚ Pensions deficit (currently £2.135m) transfers to the Company

4.2.4.3 New employees to join retirement scheme

- ✚ New employees will be entitled to the same pension
- ✚ The Housing Company is to be registered with and subject to regulation by the Social Housing Regulator

4.3 Procurement, Legislative and Organisational Arrangements

4.3.1 Procurement Arrangements

The new Housing Company will inherit various service level agreements with other States' departments. These will need to be converted into contracts, but the terms contained therein will be honoured. The new Housing Company will still be able to access services currently provided by the States to the Department, where it can be shown that in not doing so, this would increase costs to the Housing Company and thereby affect the ability of the Company to meet its commitments in terms of the return to the States. Detailed arrangement for each of these activities will be worked through in the coming months.

The new Housing Company will set targets to generate operating efficiencies which will be used to repay borrowing early. It will do so through being able to take a more commercial and focused approach in providing landlord functions and through measures such as investment in achieving the Decent Homes Standard thereby reducing the annual cost of reactive maintenance.

There will undoubtedly be further efficiencies derived from a move to Company status and enhanced focus on business objectives. However, it would be inappropriate to constrain the Board and the Treasury Minister through setting binding efficiency requirements beyond these commitments in advance of the new Housing Company being established and the Board setting out its objectives.

Failing to adequately maintain States social housing is fundamentally inefficient, as it inevitably results in the need for large scale capital investment over a short term period, or homes which are not fit to be let with a potential loss of significant rental income. Homes which fail to meet appropriate standards for thermal efficiency impact on Tenants very directly in respect of how expensive they are to run.

Further efficiencies can be achieved in the use of existing land resources. The ability to access additional capital funding will allow decisions to be made about the appropriate intensification of some existing sites rather than only carrying out refurbishments to achieve the Decent Homes Standard. The new homes created will provide new rental streams which will be sufficient to service the borrowing.

4.3.2 Legislative Arrangements

The legislative requirements for the achievement of the new social housing framework anticipated by the business case can be broadly divided into two main areas of enabling legislation.

Firstly, those related to the introduction of regulation for social housing providers (to ensure the separation of policy making, regulatory and landlord delivery functions established within section 3.6 of the Economic Case) are captured within the draft Social Housing (Jersey) Law 201_. This sets out the basis for establishment of an independent Social Housing Regulator together with provisions for the licensing of Social Housing Providers, of which the proposed new wholly States owned Housing Company will be one. Should this enabling law obtain States Assembly and Privy Council assent it will then permit the bringing forwards of regulations, namely those formalising a near market rent policy, decent homes standards and good governance and financial probity requirements for Social Housing Providers.

Secondly, those requirements related to the establishment of the proposed new, wholly States-owned Housing Company, which are captured within the draft Social Housing (Transfer) (Jersey) Law 201_. This enabling law will establish the principles for the transfer of tenants, existing staff of the Housing Department performing landlord functions and the 4,500 stock to the proposed new Company, together with the Governance arrangements of the Company. If the enabling Law obtains States and Privy Council consent, it will permit the bringing forwards of detailed regulations to the States Assembly enabling the transfer to take place.

4.3.3 Tax Arrangements

The tax position of the Housing Company in relation to the Income Tax (Jersey) Law 1961 has been discussed with the Income Tax Department. Representatives of the Income Tax Department have stated that as long as the Company was wholly owned by the States, it would benefit from a miscellaneous exemption under the Law as detailed in Article 115 (c), namely "Exemption from income tax shall be granted in respect of any income derived by the States from their own property". This exemption would apply to both rental income and other associated income generated from the ownership of the properties.

In addition, the new Company would need to register for G.S.T. and would become a "taxable person" in its own right (as opposed to being part of the States of Jersey's registration). The Company would then be required to pay and collect G.S.T. on taxable supplies as now, but would be able to claim a credit back from the Comptroller on a three monthly basis.

4.3.4 Organisational Arrangements

The Housing Department 2013 MTFP allows for a total of 47.6 Full Time Equivalent ("FTEs") staff. Additionally, 2.6 Full Time Equivalent Customer Service staff transferred to the Housing Department during 2012 (as the customer service function moved from Cyril Le Marquand House to the Housing Department). Total staff at 2013 is as follows:

| | No. of FTEs |
|---------------------------------------|-------------|
| Chief Officer & Personal Assistant | 2 |
| Strategic Development Directorate | 13 |
| Operations Directorate | 24.6 |
| Finance Directorate | 10.6 |
| Total Housing Department Staff | 50.2 |

As already noted in the Strategic Case section 2.2.2, this represents a very lean establishment compared to local authority housing departments in the UK.

In preparation for the proposed move to the new Housing Company, the Housing Department has undertaken a number of service reviews to establish the appropriate organisational arrangements that will need to be put in place in order to affect a successful move to the new Housing Company. In addition, a number of site visits have been

arranged to other incorporated bodies and social housing providers to establish appropriate governance and financial management arrangements.

These reviews have been identified that a number of improvements / changes are required in the areas of asset management, customer services, governance and financial management to ensure that the new Housing Company is ready to act in an efficient flexible and commercial manner to provide tenants with the improved services expected.

These changes can be summarised in the following 8 themes:-

- ✚ Ensure processes are fair and accountable to Tenants
- ✚ Ensure resources remain focussed on those most in need
- ✚ Improve understanding of the standards Tenants can expect
- ✚ Ensure policies are in place to meet the needs of vulnerable customers
- ✚ Improve customer care and ensure customers are treated with dignity
- ✚ Ensure all Staff are motivated and accountable for their performance
- ✚ Identify new systems required to improve the business for customers
- ✚ Manage assets optimally for the customer

The overall effect of these changes identified above is summarised in the table below:-

| | No. of FTEs |
|--------------------------------------|-------------|
| Chief Executive & Personal Assistant | 2 |
| Strategic Development Business | 13 |
| Operations Business | 26.6 |
| Finance and Resources Business | 14.6 |
| Total Housing Company Staff | 56.2 |

The increase in staff numbers is partially due to the increased programme in order to meet Decent Homes Standard and a number of these posts are either confirmation of temporary positions or result in efficiency savings and hence do add cost pressure to the Housing Company's business plan.

The additional staff in the Strategic Development Business relate to the appointment of an Asset Management Team, which were confirmed as necessary by Ridge and Partners LLP to manage the implementation of the refurbishment and new build programmes envisaged within the Company Business Case, amounting to approximately £20 million per year over the next 10 years. The additional roles within the Operations Business relate to a capital management trainee to assist oversight of the enhanced maintenance required to achieve the Decent Homes Standards. These roles are considered essential if the States accepts that investment to achieve and maintain Decent Homes Standards is to be made.

In addition, the Finance and Resource Business includes increased staff compliment to provide Board Support, Human Resource and Liquidity Management roles that are necessary if the States accepts that a new Company at arm's length from the States is required.

4.3.5 Implications for existing States Services

The States services whose workloads could be affected by the proposed Company include the Chief Minister's Department, Treasury and Resources Department, Law Officers and Conveyancing Services.

The establishment of a separate Company and associated Board will mean the Human Resource support to the Housing Department, currently paid for by the Department will be replaced by a role within the proposed Company.

Within the Treasury and Resources Department, the financial and treasury management functions currently supporting the Housing Department will have a change in reporting arrangements but as the new Company will remain a Strategic Investment and will be reported within the State's finances this is not considered material. As the Company plans to retain Information technology systems following transfer, the impact of this change cannot be fully quantified at present. Within the Property Holdings Department, there will be a marginal reduction from the number of sold property transactions no longer requiring Standing Order approvals, but this is not expected to be material.

The new Company will be required to seek its own legal advice on property matters and to conduct its own conveyancing. During the transformation process, external consultancy advice has been procured by both the Law Officers and Conveyancing Services to facilitate transformation and so no material reduction in work volumes is anticipated in these areas that would result in direct savings.

4.4 Asset Management Arrangements

The current make up of the States' housing stock is set out in the table below.

| Property type | No. of units |
|---------------|--------------|
| Bedsit | 306 |
| 1 bedroom | 1,732 |
| 2 bedrooms | 1,514 |
| 3 bedrooms | 858 |
| 4 bedrooms | 120 |
| 5 bedrooms | 7 |
| 6 bedrooms | 2 |
| Total | 4,539 |

Additionally, the Housing Department presently administers 7 assets which are occupied by charities who provide inter alia housing services. These properties are fundamentally residential in nature and provide housing for vulnerable people as a core function. The operating charities are all key partners of the present Housing Department with clients of these organisations regularly transferring on to be housed by the Housing Department. It is proposed that these assets will also be transferred to the new Housing Company and provision for their long term maintenance has been made within the business plan of the new Company.

The Housing Company plans to instigate the following stock changes:-

- ✚ Build on new sites with a net gain of 434 units (20 of which will be sold for lifetime enjoyment)
- ✚ Refurbish 578 units
- ✚ Sell 300 units (projected at 15 per annum in years 1-20 of the business model)

See Appendix B for further details on new builds and refurbishments.

Additionally, the social housing Trusts plan to develop 3 sites projected to generate 203 additional units

Projected movements in social housing units are summarised as follows:

| | Units | Units |
|---|-------|--------------|
| Current social housing stock | | 4,539 |
| Gained through new build projects | 598 | |
| Lost through demolition | -164 | |
| Sold as part of a new build project | -20 | 414 |
| Units sold* | | -330 |
| Units held by the Company at year 30 | | 4,623 |
| Gained by Social Housing Trusts | | 203 |

*The sale of 330 properties includes 30 sales prior to the commencement of the new Housing Company on 1 July 2014. The proceeds from the sale of properties part fund the stock development and associated borrowing until repaid in year 16). No properties are sold after year 20

The proposed sales throughout the 20 year period and those that will take place prior to 2014 will all be classified as 'Affordable' in perpetuity and this will mean that the stock of affordable homes is actually increased by 414 units albeit that 330 homes will be targeted at affordable home ownership. Overall the Islands' stock of Affordable Housing will be augmented further by the addition of 203 units to the Housing Trusts.

Non-property assets administered by the Housing Department will also be transferred to the Housing Company and these will be set out in a schedule under regulation.

4.5 Commercial Risk Allocation

The allocation of risks between the States as owner and shareholder of the proposed new Company and the Board of the new Company will need to be formalised through a Transfer Agreement.

To understand the basis of risk allocation, a risk allocation matrix (Attached as Appendix E) was commissioned to enable all parties to understand the level of risk proposed for the new Company, those risks that remain shared between the Company and the States, and finally those that remain with the States of Jersey as guarantor.

The development of the risk allocation matrix also enabled consideration and quantification of appropriate sensitivities to address the risks to ensure that the business case would remain robust in the event that risks or combinations of risks crystallise.

Risks should be allocated on a value for money basis to the party best able to manage them throughout their life-cycle. This requires a thorough understanding of:

- ✚ The nature of the risks
- ✚ The way in which these risks affect the ability of the Company to deliver the service
- ✚ The degree of control that each party has of the risks
- ✚ The cost to the States of retaining the risk
- ✚ The way in which the new Company can manage those risks allocated to it

The risk categories identified conform to the PESTLE model set out within H.M Treasury Guidance on the Management of Risk Principles and Concepts (The Orange Book. H.M. Treasury 2004).

The risk allocation matrix was developed by Trowers and Hamlins LLP on behalf of the Housing Transformation Programme with the support of officers from the Chief Minister's Department, Treasury and Resources, the Law Officers Department and the Housing Department and supported by Sector Treasury Services Limited.

Sensitivities on the risks identified for the Housing Company have been undertaken within section 5 Financial Case.

4.6 Human Resource Implications

4.6.1 Personnel Implications

Following a review of best practice organisational structures amongst newly created social landlords in England and Wales, it has been established that the current Housing Department performs very well in relation to its service output for the resource input applied. The best practice organisations benchmarked against have similar organisational roles, but due to the greater resource applied to meet Decent Homes Standards, the number of staff employed is significantly higher than in Jersey.

A fundamental review of business and financial systems has been undertaken together with an 'Audit Commission' Key Lines of Enquiry based external review to identify the areas of the current housing delivery function which are not fully customer focussed. This has identified areas of efficiency where resources could be better applied. However, given the investment needed in the stock and the desire to move to a more business-like delivery, it has also identified areas of the business, for example in asset management, which need additional resourcing following the transfer, in order to invest to save and ensure optimal value for money for the investment made.

It is therefore envisaged that all members of current Housing Department staff, (excluding those administering the Affordable Housing Gateway), would transfer to the proposed Company on their prevailing terms and conditions, in accordance with the States policy on alternative service provision which provide for the following:

- ✚ That the States of Jersey will incorporate adequate "business transfer" protections
- ✚ That the States of Jersey will seek to ensure that transferring staff enjoy terms and conditions not less favourable than those prevailing prior to transfer
- ✚ That employees within the existing Public Employees' Contributory Retirement Scheme will retain pension rights and liabilities unaffected when transferring to the proposed Company and that new starters post-transfer will be offered the same prevailing pension scheme
- ✚ That any necessary restructuring of staff roles in readiness for the new Company will be undertaken prior to the transfer taking place
- ✚ Transferring employees would not be subject to probationary periods, although they would be subject to the proposed Company's performance management processes
- ✚ That the proposed Company would recognise bona fide Trade Unions including Unite and Prospect which represent transferring staff at present

While re-organisation of reporting lines and the overall efficiency review is likely to result in some change to all roles, it is not envisaged at this stage that job roles will be materially different under the new Company. Instead, a skills-matching exercise is proposed to match current staff to the new roles required within the Company.

4.6.2 Pension Issues

To protect the pension rights of the transferring staff, it is proposed that the proposed Company become an "Admitted Body" in the States Public Employees' Contributory Retirement Scheme (PECRS) and the retention of existing allowances. Consultations with the Employer, the States Employment Board and representatives of the Committee of Management of PECRS have provided 'in-principal' support for the proposals.

However, it will be necessary for the pre-1987 pension liabilities at the point of transfer to resolve the portion of that deficit in relation to the Housing Department staff. In order to establish the extent of the relevant deficit, an indicative actuarial valuation has been carried out. A further actuarial valuation of the pension fund as it relates to those staff will be carried out immediately prior to transfer to fix the deficit sum due.

The responsibility for meeting that deficit will then rest with the Company and it is envisaged that this would be achieved by means of a lump sum payment at the point of transfer. The actuarial valuation will also provide the proposed Company with information about its ongoing contribution rates. Provision for the purchase of pension debt of £2.135 million has therefore been included in the new Company's business model and the draft Social Housing (Transfer) (Jersey) Law 201_ therefore reflects this position.

4.7 External Funding Sources

Preparation of the Business Case required an understanding of prospective external funders' views before finalising the new social housing regime. Meetings with four potential funders were arranged on 11 May 2012 for this purpose.

The discussion was facilitated by Trowers and Hamlins LLP supported by Sector Treasury Services Limited who are both experienced advisers with expertise in understanding the requirements of funders in relation to large scale voluntary transfers in the UK.

4.7.1 Matters discussed with potential funders

The discussion with potential funders considered the following questions amongst other matters:

- ✚ What maximum loan facility might be considered (whether singly or as part of a consortium)
- ✚ What asset cover/security value requirements might there be
- ✚ Whether the loan facility should be a conventional development and any likely drawdown requirements
- ✚ Assuming sufficient security value was available on the transferred property, the level of comfort with proposed loan repayment and annual return obligations assumed
- ✚ Whether 'two pools of debt' (and security trust deed) approach was favoured
- ✚ Whether there were any concerns over the Regulator's control over disposals (which would include charging)
- ✚ Whether usual due diligence processes (including certification of title) and not warranties could be assumed
- ✚ Whether funders had any suggestions about the nature and extent of the warranties on title and other matters proposed
- ✚ Whether funders had any views of the staff transfer, pensions and other liabilities to be assumed by the Housing Company
- ✚ Whether the proposed transfer terms and Housing Company covenants give rise to any issues from a prospective funder's perspective
- ✚ Whether the States of Jersey's role in the Housing Company's governance gave rise to any concerns
- ✚ Whether the proposed Regulator and the legal powers and constraints proposed would generate the required confidence in the social housing sector on the Island
- ✚ Whether the Regulator's proposed powers would strike the right balance between control over the sector and freedom for social housing providers to operate within the regulated framework

4.7.2 Results of discussions with potential funders

All four funders were broadly supportive of the proposals, but there were naturally caveats about further assessment and legal reviews. Funders questioned whether the proposals could be better addressed in terms of pricing benefits by the States of Jersey assuming direct responsibility for the required funding.

There was also a general expectation or suggestion that funding for the Housing Company could or should be approached as part of wider States of Jersey funding requirements.

The most productive discussions about funding structures concerned short term development funding being taken out through a bond on a rolling basis every 5 years or less.

The meetings confirmed that no facility would be committed for more than 5 years and that no single bank would take on the entire lending portfolio. Lenders would consider lending in smaller packages in consortia.

There appeared to be no need from funders for the States of Jersey to reconsider the annual return or £40m internal borrowing investment nor was there any need to revisit the proposed charging arrangements which were generally thought to be acceptable/workable.

It was, however, clear that there needs to continue to be a discussion about whether a guarantee or collateral warranties could be offered as this might have pricing benefits.

As far as the draft laws are concerned, the new regulatory system appeared to be acceptable. Nevertheless there was a concern to ensure that the regulator was at arm's length and able to exercise his/her powers without ministerial 'interference'.

As to the proposed Social Housing (Transfer) Law 201_, funders considered there was sufficient flexibility behind it to accommodate funders' identified requirements.

All the funders invited a continuing dialogue, recognising care will need to be taken to ensure that this does not compromise a future procurement process or otherwise is deemed to be unfair or anti-competitive.

As a result of the funder meetings, the Treasury was approached to decide whether it wished to take advantage of the pricing benefits which might be derived from a different approach. This is further discussed in section 3.3.4.

4.8 Financial reporting and financial protocols

This section describes the proposed:

- ✚ Legal structure of the wholly owned Housing Company (the "Housing Company")
- ✚ Financial reporting and accounting policies to be adopted by the Housing Company in accordance with Companies (Jersey) Law 1991
- ✚ Financial reporting protocols to be observed by the Housing Company when reporting to States of Jersey

4.8.1 Legal structure of the Housing Company

Following a review of alternative company forms for the proposed Housing Company, supported by Trowers and Hamlins LLP (a leading legal adviser on housing matters), it is proposed to proceed by way of Company Limited by Guarantee. This underlines the fact that there is no intent to sell or trade the ownership of the proposed Housing Company, whilst preserving flexibility for the Company.

The annual return currently made by the Housing Department would be replaced by a contractual payment made by the Housing Company to the States of Jersey (as sole Member and guarantor) acting through the Minister for Treasury and Resources, rather than for example by way of share dividend. The role of the Member would be set out within the draft Articles of Association for the Housing Company which will be lodged for approval by the States, and within the proposed Transfer Agreement.

4.8.2 Financial reporting and accounting policies

In accordance with Companies (Jersey) Law 1991, the Housing Company will:

- ✚ Keep accounting records which are sufficient to show and explain its transactions at any time
- ✚ Prepare annual accounts in accordance with International Financial Reporting Standards (“IFRS”)
- ✚ Obtain an audit opinion for the annual accounts

With the exception of the method of returning funds to the States of Jersey, the accounting policies will remain materially consistent with those followed as a States of Jersey department. The more significant accounting treatments are noted below:

- ✚ Rental income, other income and expenditure will be recognised on an accruals basis
- ✚ Social housing land and buildings:
 - ✚ Will be classified as fixed assets on the balance sheet
 - ✚ Will be held at fair value. The fair value will be calculated based on the value in use method. A full valuation will be performed every 5 years with an interim valuation in the third year
 - ✚ Land will not be depreciated; buildings will be depreciated on a straight line basis over a 50 year period
- ✚ The return to treasury will be made by a contractual payment on 31 December each year. The distribution will be settled by quarterly payments during the year in which the distribution is declared

4.8.3 Financial reporting protocols

This section describes the way in which the new Housing Company will communicate financial matters to the States of Jersey in accordance with the proposed Transfer Agreement between the States of Jersey and the Housing Company (see section 4.2 for further explanation of the Transfer Agreement).

The aim of the Transfer Agreement is to foster sound working relationships between the States of Jersey and the Housing Company, based on a mutual understanding of expectations for the sharing of information, regular dialogue on key issues as they emerge and develop, and most importantly, the operation of a “no surprises” policy so that the States of Jersey is kept fully informed as to key business decisions which have the potential to impact on the States of Jersey’s interests as guarantor.

4.8.3.1 Key requirements

The Housing Company will provide the States of Jersey with the following information:

- ✚ An annual business plan and report, at such time as may be reasonably required, setting out the objectives, policies and programmes of the Housing Company and reporting on progress compared to the previously agreed business plan. The report will include review of the key performance indicators measure by the Housing Company
- ✚ An annual report to be provided within 6 months of end of each financial year. The report will include audited financial statements, auditor’s report and a comparison of the figures contained in the business plan with actual results received
- ✚ A half yearly report of operations to be provided within 2 months after the end of the first half year. The report will include a comparison of the figures contained within the business plan with actual results achieved in the period and a report concerning the key performance indicators measured by the Housing Company
- ✚ Ad hoc reporting as required for the purpose of preparing the financial statements of the States of Jersey and information required to assist with the financial planning of the States of Jersey

In the spirit of open dialogue and a “no surprises” policy, it is expected that the Housing Company will, unless specifically contemplated in the Business Plan, seek the consent of the States of Jersey before it makes any material changes to its Business Plan. For example, if the Housing Company:

- ✚ Makes any material change in the nature of its business or commences any new business
- ✚ Sells, transfers, leases, licences or in any way disposes of all or a material part of its business or assets
- ✚ Creates any material mortgage or security interest
- ✚ Changes the financial year end

4.8.3.2 Ongoing communications

The following minimum communications will take place each year:

- ✚ The Chairman, Chief Executive and Finance Director of the Housing Company will meet on a 6 monthly basis with the Minister for Treasury & Resources (the “Minister”) to discuss matters generally covered by the Transfer Agreement
- ✚ Officers on behalf of the Minister will meet on a 6 monthly basis with senior management of the company to discuss matters generally covered by the Transfer Agreement
- ✚ Following the formal AGM each year, the Board will meet with the Minister to consider performance in the previous year
- ✚ A record of matters discussed at such meetings will be made

4.9 Contractual Milestones

The full Programme Project Implementation Plan and anticipated timings for the implementation of the proposed new Company has been set by the Political Steering Group. This sets out the individual projects required for implementation of the programme and establishment of the Housing Company. Individual project timings are likely to change during programme delivery but an approved programme plan will be maintained throughout.

The following high level plan for the programme shows the principle tasks that must be completed to achieve the delivery of the preferred option. To ensure project outputs are progressing as planned throughout its delivery cycle the Programme Board, and subsequently if approval is forthcoming the Company Shadow Board, will review progress against key targets on a monthly basis. The key contractual milestones, approvals and delivery dates can be summarised as follows:

| Reference | Milestone | Delivery Date |
|-----------|---|--------------------------|
| 1.3 | Council of Ministers consideration of Incorporation of States Housing Report and Proposition and Full Business Case. Report and Propositions lodged. | February / March 2013 |
| 1.7 | Health, Social Services and Housing Scrutiny Panel review Report and Proposition and Full Business Case | March 2013 |
| 1.3 | States consideration of Incorporation of States Housing Report and Proposition | April 2013 |
| 1.3 | Council of Ministers consideration of Enabling Laws. Commencement of Strategic Housing Unit in agreed setting. | May 2013 |
| 1.7 | Health, Social Services and Housing Scrutiny Panel review of Enabling Laws | May - July 2013 |
| 1.3 | States Assembly consideration of Social Housing and Social Housing (Transfer) (Jersey) Laws within Reports and Propositions. | July 2013 |
| 1.3 | States Assembly consideration of Shadow Board appointments and | September 2013 |

Friday, 01 March 2013

| Reference | Milestone | Delivery Date |
|-----------|---|---------------|
| | terms of reference. | |
| 1.3 | Lodging of Enabling Laws in the Royal Court, Appointed Day Act considered by States Assembly. | November 2013 |
| 1.3 | States Assembly consideration of Enacting Regulations (for Regulatory, Transfer and Social Security arrangements). | January 2014 |
| 11.7 | Company registration completed. Tenancies, Staff and Stock transfers completed. Company operation commenced. Social Housing Regulator appointed. | July 2014 |
| 2.8 | Rent for new tenancies set at near market level. | April 2014 |

5 Financial case

5.1 Introduction

As noted in the Economic Case in section 3, the preferred solution is option 6, to set up a wholly owned Housing Company (the "Housing Company") to manage the social housing service. The Housing Company is described in detail on Appendix C.

The freehold social housing assets will be transferred from States of Jersey to the new Housing Company on inception. The assets will be transferred at their book value for nil proceeds. This option is further described in section 3.4.3.

The financial implications are noted in the Economic Case in section 3 and summarised below in section 5.4.

The purpose of this section is to summarise the financial case and test the robustness of the preferred option by performing sensitivity analysis on identified risks (see section 5.5, 5.6 and 5.7).

In addition, as noted in the Financial Case of the Outline Business Case, for States of Jersey a number of interrelated issues arise from this option as follows:

- ✚ The implications of changing the link between States' sector rents and the income support payable to tenants of private rented dwellings. This is the subject of a separate report by the Social Security Department
- ✚ The capacity of the new Housing Company to continue to deliver the agreed income stream to States of Jersey and the impact of increased income support costs payable to States' tenants as a result of implementing the proposed rent policy (see section 5.2 and 5.3)
- ✚ The capacity within Housing Trust business plans to contribute to States of Jersey priorities and the impact of increased income support costs payable to Housing Trust tenants as a result of implementing the proposed rent policy. This will be the subject of a separate report

The Housing Transformation Programme has wider benefits including the delivery of new social housing and the attainment of the decent homes standard for existing States' sector housing. Section 5.4 summarises the impact of stock development plans of the Housing Company and the Housing Trusts.

5.2 Proposed Rents Policy and its implications

This section summarises the proposed rent policy and the impact of this policy on:

- ✚ The States of Jersey
- ✚ States' tenants receiving Income Support
- ✚ States' tenants not in receipt of Income Support

5.2.1 Proposed rent policy

The proposed rent policy sees a return of social housing rents to fair rent levels for any tenancy that commences on or after 1 April 2014. Fair rent levels are set at 90% of market rents to track but not inflate market rents in the private sector.

New tenancies (and existing tenancies that are at 90% of market rents) will be adjusted annually by RPI plus average earnings inflation of 0.75% in excess of RPI (which represents half of the long term expectation). However, where this would take the rent above 90% of market rent, the rent will only be increased to 90% of market rent.

For existing tenancies that are above 90% of market rent (approximately 450 properties), rent will be frozen until it matches 90% of market rent. Thereafter, it will be adjusted annually as noted above.

5.2.2 Additional cost to States of Jersey

The annual return made by the Housing Company to the States of Jersey will be maintained in real terms from 2016 (i.e. adjusted annually by RPI). Therefore, increases in rental income above RPI will be retained by the Housing Company. Where increases in rental income are below RPI, i.e. in a weak rental market, the Housing Company will absorb this in to its operations.

The States of Jersey is responsible for additional Income Support costs as a result of the proposed rent policy. The table below quantifies the likely additional cost and includes forecasts for:

- ✚ The additional rental income received by the Housing Company as a result of the proposed rent policy being implemented (compared to the existing rent policy)
- ✚ The amount of the additional rent that will be paid by the Social Security Department. This is expected to be 67% of the additional rent because approximately 67% of the tenants of the Housing Department are entitled to an element of the housing component of Income Support
- ✚ This additional cost for Income Support will need to be funded by the Treasury by means of an additional budget allocation to the Social Security Department

| Year | Year | Amounts in real terms* | |
|-----------|------------------------|--------------------------|--|
| | | Additional rental income | Additional rent paid by Income Support |
| | | £m | £m |
| 2014 | 1 | 0.5 | 0.3 |
| 2015 | 2 | 1.1 | 0.7 |
| 2016 | 3 | 1.1 | 0.7 |
| 2017 | 4 | 1.5 | 1.0 |
| 2018 | 5 | 1.6 | 1.1 |
| 2019 | 6 | 1.9 | 1.3 |
| 2020 | 7 | 2.2 | 1.5 |
| 2021 | 8 | 2.2 | 1.5 |
| 2022 | 9 | 2.2 | 1.5 |
| 2023 | 10 | 2.4 | 1.6 |
| 2024-2028 | 11-15 (annual average) | 2.5 | 1.7 |
| 2029-2033 | 16-20 (annual average) | 2.8 | 1.9 |
| 2034-2043 | 21-30 (annual average) | 3.0 | 2.0 |

*The amounts shown in the above table are in real terms, therefore, the impact of inflation has been removed

It is expected that approximately 55% of new tenancies will be to tenants from the waiting list. Therefore, the Income Support paid for these tenancies replaces Income Support paid in the private sector.

The additional units built by the Housing Company will provide growth to the social housing sector. This will change the proportion of Income Support payments made to social housing landlords (relative to private landlords) but the overall cost would be the same.

5.2.3 Convergence to 90% of market rents

The table below illustrates the modelled convergence of current rents to 90% of market under the proposed rent policy.

| | No. of units at 90% of market rent | No. of units below 90% of market rent | No. of units in stock | % of units at 90% of market rent | No. of units at below 90% of market value not in receipt of Income Support |
|----------------|------------------------------------|---------------------------------------|-----------------------|----------------------------------|--|
| Year 1 - 2014 | 865 | 3,637 | 4,502 | 19% | 1,218 |
| Year 5 - 2018 | 2,449 | 2,324 | 4,773 | 51% | 597 |
| Year 10 - 2023 | 3,485 | 1,288 | 4,773 | 73% | 328 |
| Year 15 - 2028 | 3,869 | 829 | 4,698 | 82% | 219 |
| Year 20 - 2033 | 4,114 | 509 | 4,623 | 89% | 134 |
| Year 25 - 2038 | 4,269 | 354 | 4,623 | 92% | 97 |
| Year 30 - 2043 | 4,377 | 246 | 4,623 | 95% | 61 |

In 2014, business modelling estimates that there will be 3,637 units for which rent is charged at below 90% (1,288 units at year 10). Of those units:

- 2,419 units are forecast to be occupied by tenants in receipt of the housing component of Income Support, reducing to 960 at year 10. Therefore any increases in rent would be paid by additional Income Support
- 1,218 units are forecast to be occupied by tenants who are not in receipt of the housing component of Income Support, reducing to 328 at year 10. This is analysed further below

The forecast units where the rent is below 90% of market rent and the tenant is not in receipt of the housing component of Income Support at year 1 and year 10 of the business model are noted below.

| Property size | Year 1 | Year 10 |
|------------------|--------|---------|
| | 2012 | 2023 |
| Bedsit | 58 | 16 |
| 1 Bedroom | 361 | 97 |
| 2 Bedroom | 490 | 132 |
| 3 Bedroom | 277 | 75 |
| 4 Bedroom | 31 | 8 |
| 5 Bedroom | 1 | - |
| Total | 1,218 | 328 |
| % of total stock | 27% | 7% |

It should be noted that this modelling is only an approximation based on previous years' averages. No account has been taken of increased mobility of those with higher incomes nor has any account been taken of opportunities to purchase properties contained within this business plan. The sales of 15 properties per annum that are forecast throughout the first twenty years of this business plan are likely to be targeted at those higher incomes within the social sector.

Work undertaken jointly between the Housing and Social Security Departments has looked at the income distribution of those tenants not receiving income support. This analysis is given in the table below.

| Income in bands | Total |
|-----------------|-------|
| £0k-£5k | 58 |

| Income in bands | Total |
|-----------------|--------------|
| £5k-£10k | 74 |
| £10k-£15k | 77 |
| £15k-£20k | 167 |
| £20k-£25k | 200 |
| £25k-£30k | 215 |
| £30k-£35k | 163 |
| £35k-£40k | 92 |
| £40k-£45k | 73 |
| £45k-£50k | 33 |
| £50k plus | 72 |
| Total | 1,224 |

This table clearly indicates that even those States' tenants who do not claim income support, most have modest incomes, with only 178 tenants having a household income of over £40,000 per annum.

5.2.4 States' tenants receiving Income Support

This applies to the two thirds of tenants who receive any amount of the housing component of Income Support. This figure is not surprising as one of the eligibility criteria for acceptance onto the Affordable Housing Gateway is a low income.

Rents charged for properties held by the Housing Company will continue to be at a level that would be covered by the housing component of Income Support. Therefore:

- ✚ Tenants entitled to the full housing component of Income Support will continue to have the full amount of their rent paid whilst they are a tenant of the Housing Company
- ✚ Tenants entitled to any lower amount of the housing component of Income Support will continue to receive the level of Income Support appropriate to their circumstances

In other words, tenants in receipt of any amount of the housing component of Income Support will not be financially impacted by the proposed rent policy in their current tenancies nor if they transfer to another property within the Housing Company's stock provided their circumstances do not change.

Given that States' tenants in receipt of the housing component of income support will be fully protected from the proposed rents policy, there is no adverse economic or social impact on these tenants. It should be recognised, however, that following the introduction of the proposed rents policy, tenants' earnings would need to increase to a greater extent in order to escape from income support.

5.2.5 States' tenants not in receipt of Income Support

Existing tenants not in receipt of the housing component of Income Support (approximately one third of tenants) will not be required to pay additional rent as a result of the proposed rent policy (other than annual increases explained in section 5.2.1) whilst they remain in their current properties.

Should those tenants transfer to another property within the Housing Company's stock (thus creating a new tenancy), rent will be charged at 90% of market rent for the new property. Transferring tenants will be made aware of the rental of the new property before deciding whether to sign the tenancy, so will be fully aware of any impact that this may have on their financial circumstance. Tenants transfer for a variety of reasons, but over half of tenants transfer to smaller properties, which would generally command a lower rental than the larger property from which they are moving. Where Tenants are moving to properties that have been refurbished to Decent Homes Standards, there will be compensatory savings in energy costs that will also offset the return to fair rent levels.

Work undertaken jointly between the Housing and Social Security Departments has looked at the Social and Economic Impact Assessment of the proposed rent policy. Given that the proposed rent policy will only be implemented on new tenancies, the impact is considered to be very small. In addition, analysis of those States' tenants who do not receive the housing component of income support has concluded that 74% of tenants have income in excess of any income support criteria to pay the new proposed rent. This means that at their current income level, it is considered that they could afford the new rental level and would not be entitled to any income support when charged rents under the proposed policy.

This analysis has also shown that only 35 States' tenants would become entitled to income support under the proposed rents policy should they move to a new property. These tenants would probably be entitled to approximately £19 per week per tenant in housing component of income support.

Finally, the analysis undertaken has also indicated that 167 States' tenants do not have a household income above the current income support level, but do not to claim income support. It is unclear whether this is by choice or highlights a limitation of the analysis. Whatever the reason, it appears a fair assumption that many of these tenants will continue not to claim income support in the future. The increase in income support due to this change of policy is estimated to be £31 per week per tenant for any of those tenants that do actually claim in future, but only if and when they move to a property with a higher rental.

5.3 Contribution from the wholly owned Housing Company

As noted in the Economic Case in section 3 and summarised in section 5.4.2.3 below, the wholly owned Housing Company (the "Housing Company") will return the agreed annual amount to the States of Jersey.

Sensitivity analysis has been performed in section 5.7 to assess the risk of the agreed return not being delivered to the States of Jersey.

5.4 Summary financial case

The net cost to the States of Jersey for the preferred option is noted in section 5.2.

The summary financial case for the Housing Company is noted below.

5.4.1 Key financial and stock development objectives

The key financial objectives of the Housing Company are as follows:

| Objective |
|--|
| To achieve Decent Homes Standard within 10 years and maintain the standard thereafter |
| To develop the current social housing stock to better meet the needs of Jersey's changing population by: <ul style="list-style-type: none">• Making more homes more lifelong compatible by refurbishing existing stock and building on new sites• To realign the current social housing stock and provide affordable housing solutions to those in a position to buy. This will be achieved through the sales of current social housing stock |
| To provide the agreed annual return to States of Jersey |

5.4.2 Key financial projections

The Housing Company will manage the social housing service including maintaining the 90% of market rent policy on new tenancies described in section 3.4.1 and summarised in section 5.2.1 above. A 30 year business model has been prepared and the key financial projections are noted in the following sections.

5.4.2.1 Stock development

The Housing Company plans to invest £201.4m (in real terms) in stock development and obtain proceeds from sales of £96.1m (in real terms) as follows:

- ✚ Build on new sites with a net gain of 434 units (20 of which will be sold for lifetime enjoyment as affordable homes for proceeds of £4.4m (which is a pilot scheme)) at a projected cost of £147.1m
- ✚ Refurbish 578 units at a projected cost of £54.3m
- ✚ Sell 300 units (projected at 15 per annum for 20 years with proceeds of £366k per property, with a 25% bond provided on half of sales)

Additionally, the Housing Company plans to invest £300.0m (in real terms) in maintenance to bring all properties up to Decent Homes Standard and maintain it thereafter (this is £19.0m more than that allowed for in the Medium Term Financial Plan).

See Appendix B for further details on new builds and refurbishments.

Additionally, the social housing Trusts plan to develop 3 sites projected to generate 203 additional units at an estimated cost of £33.0m (in real terms).

Projected movements in social housing units are summarised as follows:

| | Units | Units |
|---|-------|--------------|
| Current social housing stock | | 4,539 |
| Gained through new build projects | 598 | |
| Lost through demolition | -164 | |
| Sold as part of a new build project | -20 | 414 |
| Units sold* | | -330 |
| Units held by the Company at year 30 | | 4,623 |
| Gained by Social Housing Trusts | | 203 |

*The sale of 330 properties includes 30 sales prior to the commencement of the new Housing Company on 1 July 2014. The proceeds from the sale of properties part fund the stock development and associated borrowing until repaid in year 16). No properties are assumed to be sold after year 20

The proposed sales throughout the 20 year period and those that will take place prior to 2014 will all be classified as 'Affordable' in perpetuity and this will mean that the stock of affordable homes is actually increased by 414 units albeit that 330 homes will be targeted at affordable home ownership. Overall the Islands' stock of Affordable Housing will be augmented further by the addition of 203 units to the Housing Trusts.

5.4.2.2 Borrowing

The Housing Company will obtain borrowing as follows:

- ✚ **Internal borrowing:** As noted in section 3.5.1.2, the States of Jersey have confirmed that an internal borrowing facility will be made available. This is set out in R132/2011 States Investment Strategies which was presented to the States of Jersey on 1 November 2011 by the Treasury and Resources Minister. The Treasury Department has indicated that this will be a £40m facility attracting fixed interest of 4% per annum, this will be formalised in the transfer agreement between States of Jersey and the new organisation
- ✚ **External borrowing:** As noted in section 3.3.4, work is underway to appoint a financial advisor initially to recommend options for the best financing options. Once a workable solution is identified, a proposition will be taken to the States to seek their approval for the proposed funding strategy, in compliance with Article

21 of the Public Finances (Jersey) Law 2005. The Treasury Department have indicated that borrowing of up to £200m over a 20 year period is proposed to be made available to the Housing Company at a fixed interest rate of 5% per annum

The financial modelling indicates that the following borrowing will be required:

| | Peak borrowing | Year repaid |
|--------------------|-------------------|----------------|
| Internal borrowing | £40m | 18 |
| External borrowing | £160m | 16 |

5.4.2.3 Return to States of Jersey

The return to States of Jersey will be maintained in real terms from 1 January 2016. This is after delivering the returns set out in the Medium Term Financial Plan including Comprehensive Spending Review savings. In years 2013 to 2015 the return will be adjusted to reflect agreed transitional costs.

The table below illustrates the returns up to 2015, thereafter the return will be adjusted annually by RPI.

| | 2012 £000s | 2013 £000s | 2014 £000s | 2015 £000s |
|---|---------------|---------------|---------------|---------------|
| Near cash return per MTFP | 24,559 | 26,798 | 27,972 | 29,339 |
| One off set up costs of the new organisation | - | (706) | - | - |
| Transfer of costs to Chief Ministers Department | - | - | 182 | 182 |
| Agreed return | 24,559 | 26,092 | 28,154 | 29,521 |

5.4.2.4 Cash

Cash will be generated from operations and social housing sales. This cash will be used to:

- ✚ Fund the annual return to the States of Jersey and the stock development costs to the extent that it is available (to the extent that it is not available, borrowing is taken out as noted in section 5.4.2.2)
- ✚ Repay the borrowing noted in section 5.4.2.2

Cash surpluses are not generated until year 18 of the business model when all borrowing is repaid. The net present value* of cash surpluses generated at year 30 of the business model is £63.7m.

When cash surpluses are generated, the Housing Company and the States of Jersey will agree the best use for those surpluses.

*Net present value ("NPV") is calculated using the inflated discount rate of 7.12% which is recommended by States of Jersey for this type of financial modelling. The NPV calculation estimates the cash surplus after taking in to account the time value of money. It is an estimate of the cash surplus as though it were received immediately and not in the future, giving a 'real' indication of the amounts that will be generated

5.4.2.5 Summary financial projections for Housing Company

The projected financial position of the Housing Company, which incorporates inflation, is summarised below.

Friday, 01 March 2013

| Income statement | Years | | | | | | | Total |
|---|-------|------|-------|-------|-------|-------|--------|-------|
| | 1-5 | 6-10 | 11-15 | 16-20 | 21-25 | 26-30 | | |
| | £m | £m | £m | £m | £m | £m | | |
| Rental income | 240 | 340 | 430 | 530 | 655 | 812 | 3,007 | |
| Expenditure including depreciation | -183 | -188 | -221 | -255 | -335 | -390 | 1,572 | |
| Net profit before finance costs | 57 | 152 | 209 | 275 | 320 | 422 | 1,435 | |
| Interest on borrowing | -20 | -46 | -30 | -6 | - | - | -102 | |
| Profit after finance costs | 37 | 106 | 179 | 269 | 320 | 422 | 1,333 | |
| Depreciation charge included in the above | 89 | 116 | 129 | 142 | 157 | 175 | 808 | |
| Profit excluding depreciation charge | 126 | 222 | 308 | 411 | 477 | 597 | 2,141 | |
| Return to States of Jersey | -153 | -182 | -216 | -256 | -304 | -361 | -1,472 | |
| Net profit excluding depreciation charge | -27 | 40 | 92 | 155 | 173 | 236 | 669 | |

| Balance sheet | At year end | | | | | | |
|-----------------------|-------------|-------|-------|-------|-------|-------|-------|
| | 1 | 5 | 10 | 15 | 20 | 25 | 30 |
| | £m | £m | £m | £m | £m | £m | £m |
| Social Housing stock | 896 | 1,084 | 1,226 | 1,349 | 1,482 | 1,650 | 1,838 |
| Debtors and creditors | 15 | 22 | 33 | 47 | 63 | 70 | 76 |
| Cash | - | - | - | - | 109 | 291 | 537 |
| Internal loan due | -40 | -40 | -40 | -40 | - | - | - |
| External loan due* | -21 | -144 | -126 | -23 | - | - | - |
| Net assets | 850 | 922 | 1,093 | 1,333 | 1,654 | 2,010 | 2,452 |

*Peak external debt is forecast to be £160m at year 7

5.5 Risks

The proposed rent policy and external borrowing are required to be in place prior to the formation of the Housing Company, as is the Transfer Agreement containing the basis of the annual return to Treasury (and this would be negotiated between the Shadow Board for the Housing Company and the Treasury on behalf of the States as owner).

The identified ongoing risks to the Housing Company of not achieving the objectives noted in section 5.4.1 are noted below.

1. Change to basis of proposed rent policy
2. Change to basis of proposed return to the States of Jersey
3. Change to basis of external borrowing
4. Failure to receive required capital proceeds from the sale of social housing stock
5. Fluctuations in RPI
6. Rental income is lower than expected because:
 - a. Rental market growth is lower than expected
 - b. Re-lets are lower than expected
7. Ability to repay external borrowing if stock development plans not achieved
8. Failure to collect rents due and/or failure to manage the implementation of the proposed rent policy
9. Increased interest rates on borrowing
10. Unexpected costs incurred

Sensitivity analysis has been performed to assess the impact each risk could have on the success of the programme. The results are noted in the section 5.7.

5.6 Risk assessment criteria

The risk will be assessed on the following 3 criteria:

1. Potential financial impact of risk
2. Probability that the financial impact of the risk will occur
3. The extent to which the risk is influenced by external factors

These are explained in 5.6.1 below.

5.6.1 Potential financial impact of risk

Risks are assessed as having a low, medium or high financial impact on the following basis.

| External loan requirements | Explanation of assessment | Low financial impact | Medium financial impact | High financial impact |
|---|--|----------------------|-------------------------|-----------------------|
| Peak debt of less than £200m repaid within 20 years | External loan requirements are in line with terms indicated by the Treasury Department noted in section 5.4.2.2 | x | | |
| Peak debt of £200m to £225m repaid within 25 years. The level of debt | The extent to which external loan requirements exceed those indicated by the Treasury Department are considered to be manageable either by obtaining additional external finance of up to £25m over up to 5 years or by absorbing additional costs in to the business model. The level of potential further borrowing is considered to be achievable given the assets available for security | | x | |
| Peak debt of more than £225m repaid after 25 years | The extent to which external loan requirements exceed those indicated by the Treasury Department are considered to be significant | | | x |

5.6.2 Probability that the financial impact of risk will occur

The probability that the financial impact of each of the risks will occur is assessed as low, medium or high. This assessment will include consideration of the controls in place to mitigate the risks (assuming the proposals contained within this Full Business Case are adopted).

5.6.3 The extent to which the risk is influenced by external factors

The extent to which the risk is influenced by external factors is assessed as low, medium or high which indicates the extent to which the Housing Company can directly control the risk.

5.7 Sensitivity analysis

Sensitivity analysis has been performed to evaluate the robustness of the business model for the new Housing Company for each of the identified risks.

In order to demonstrate the financial impact of each risk, sensitivity analysis has assumed:

- ✚ Objectives noted in section 5.4.1 are fully met in line with the financial modelling summarised in section 5.4.2, with the exception of external borrowing
- ✚ External borrowing would be taken out to the extent that it is required

In other words, the impact on external loan requirements is used to demonstrate the magnitude of the risk when performing sensitivity analysis.

5.7.1 Risk 1: Change to basis of proposed rent policy

5.7.1.1 Potential financial impact of risk

It is recognised that the current rent policy results in rent levels at significantly below equivalent market rents and does not provide sufficient rental income to enable the Housing Company to be financially self-sustainable.

The proposed rent policy is to charge 90% of market rents on new tenancies from 1 April 2014. The adoption of the proposed rent policy is dependent upon regulation being passed by the States in April 2013. The Housing Company would be incorporated after the adoption of the rent policy and so it is assumed for the purposes of this risk assessment that the proposed rent policy has been adopted.

Therefore, the risk for the Housing Company is that the basis of the rent policy is changed at some point during the business modelling period.

If the rent policy is changed, the potential financial impact is high, dependent upon the change to the proposed rent policy. For example, as noted in section 3.3, an 80% of market rent policy would result in an unviable business model due to the inability to repay debt. The 80% of market rent policy was also modelled with a reduced return, however, it was concluded that the return would need to be reduced to an unacceptable level in order for the Housing Company to be financially self-sustainable.

5.7.1.2 Probability that the financial impact of risk will occur

The probability that this risk will occur to the extent that the financial impact would be high is considered to be low because the proposed rents policy, if adopted, can only be changed by a States Decision. The implications of that decision will be transparent and understood and the proposed social housing regulator will monitor the application of the policy.

If the rent policy was amended and this caused the Housing Company to become financial unviable, this would need to be accompanied by other changes, such as a reduction to the return to the States of Jersey. Therefore, the resulting financial impact would be low.

5.7.1.3 The extent to which the risk is influenced by external factors

The extent to which this risk is influenced by external factors is considered to be low on the basis that the policy will be agreed by a States Decision as noted above.

5.7.1.4 Summary assessment

| Assessment for risk 1: Change to basis of proposed rent policy | |
|---|------|
| Potential financial impact of risk | High |
| Probability that risk will occur | Low |
| The extent to which the risk is influenced by external factors | Low |
| Overall risk assessment | Low |

This business case proposes that the rent policy of 90% of market rent for new tenancies is adopted by a States Decision. On the assumption that this occurs, there is low probability that the risk will impact the Housing Company's business model and low risk that this will be influenced by external factors. Therefore, the overall risk assessment is low. However, the high potential financial impact of this risk demonstrates the importance of the proposed rent policy being adopted and maintained for the duration of the business model.

5.7.2 Risk 2: Change to basis of proposed return to the States of Jersey

5.7.2.1 Potential financial impact of risk

The proposed agreed return to the States of Jersey will be formalised in the Transfer Agreement. If the agreed return differs to the return assumed in the business modelling, the business model would need to be re-evaluated on that basis.

The business model assumes that all cash generated (through operations and property sales) would be used to fund stock development and repayment of debt. Therefore, the Housing Company is forecast to have no cash surpluses until debt is repaid in year 18. Any increase in the return to the States of Jersey would have a direct impact on the level and duration of borrowing required.

The potential financial impact of this risk is high, dependent upon the change to the proposed agreed return to the States of Jersey.

5.7.2.2 Probability that the financial impact of risk will occur

The probability that this risk will occur is considered to be low as the basis of the return will be agreed in the Transfer Agreement as noted above.

5.7.2.3 The extent to which the risk is influenced by external factors

This extent to which this risk is influenced by external factors is considered to be low on the basis that the policy will be agreed in the Transfer Agreement as noted above.

5.7.2.4 Summary assessment

| Assessment for risk 2: Change to basis of proposed return to the States of Jersey | |
|---|------|
| Potential financial impact of risk | High |
| Probability that risk will occur | Low |
| The extent to which the risk is influenced by external factors | Low |
| Overall risk assessment | Low |

The potential financial impact of this risk is high but, on the assumption that the basis of the return proposed in this document is included in the Transfer Agreement, there is low probability that the risk will occur and low risk that this will be influenced by external factors. Therefore, the overall risk assessment is low.

5.7.3 Risk 3: Change to basis of external borrowing

5.7.3.1 Potential financial impact of risk

As noted in section 5.4.2.2, the Treasury department is currently considering options for external borrowing and have indicated that borrowing of up to £200m over a 20 year period is proposed to be made available at a fixed interest rate of 5%.

If external finance is not available to the Housing Company then none of the new build plans noted in Appendix B could be achieved and some of the refurbishment projects noted in Appendix B could not be achieved.

It is assumed that the Housing Company would only be incorporated with its current stock development plans if the external finance has been secured as planned. If the borrowing facility is significantly different to that modelled, the business case would need to be re-evaluated.

Therefore, the financial impact of this risk to the incorporated Housing Company is low.

5.7.3.2 Probability that the financial impact of risk will occur

The probability that the basis of external finance would be changed is low. This is on the assumption that the borrowing is secured, as anticipated, prior to the incorporation of the Housing Company.

5.7.3.3 The extent to which the risk is influenced by external factors

The extent to which the risk is influenced by external factors is low. This is on the assumption that the borrowing is secured, as anticipated, prior to the incorporation of the Housing Company.

5.7.3.4 Summary assessment

| Assessment for risk 3: Change to the basis of external borrowing | |
|--|-----|
| Potential financial impact of risk | Low |
| Probability that risk will occur | Low |
| The extent to which the risk is influenced by external factors | Low |
| Overall risk assessment | Low |

On the assumption that the borrowing is secured, as anticipated, prior to the incorporation of the Housing Company, the overall ongoing risk to the Housing Company is low.

5.7.4 Risk 4: Failure to receive required capital proceeds from the sale of social housing stock

5.7.4.1 Potential financial impact of risk

A reduction in expected capital proceeds because sale proceeds and/or sale quantities are lower than expected would result in lower cash inflows than expected. In order for new build projects to proceed as planned, further financing would be required.

The following scenarios have been modelled for sensitivity analysis with the resulting external borrowing implications noted.

| | Sensitivities performed | Peak external borrowing | Year repaid |
|---|---|-------------------------|-------------|
| Assumptions per business model | States of Jersey Statistics Unit "central" House Price Index ("HPI") projections. Long term projections are 5% growth per annum 300 properties sold at a rate of 15 per annum in years 1 to 20 | £160m | Year 16 |
| Decrease in House Price Index ("HPI") assumptions | States of Jersey Statistics Unit "pessimistic" HPI projections. Long term projections are negative 1% per annum. All other assumptions per business model | £175m | Year 20 |
| Decrease in number of properties sold | 200 properties sold at a rate of 10 per annum. All other assumptions per business model | £174m | Year 18 |
| Decrease in HPI and number of properties sold | States of Jersey Statistics Unit "pessimistic" HPI projections. Long term projections are negative 1% per annum 200 properties sold at a rate of 10 per annum in years 1 to 20 | £185m | Year 21 |

The sensitivities modelled above assume RPI at States of Jersey Statistics Unit "central" projections of 3.5% and market rental increases of 4.25%. If the worst case scenario noted above is modelled with differing RPI and market rent levels, the result is as follows:

| | Sensitivities performed | Peak external borrowing | Year repaid |
|---|---|-------------------------|-------------|
| Decrease in HPI and number of properties sold | As modelled in table above which incorporates States of Jersey Statistics Unit "central" RPI projections. Long term projections are 3.5% growth. Rental increases estimated to be 4.25% | £185m | Year 21 |
| Low RPI scenario | As above except with States of Jersey Statistics Unit "pessimistic" RPI projections. Long term projections are 2.5%. Rental increases estimated to be 3.25% | £183m | Year 22 |
| High RPI scenario | As above except with States of Jersey Statistics Unit "pessimistic" RPI projections. Long term projections are 4.5%. Rental increases estimated to be 3.25% | £195m | Year 20 |

If either house prices are pessimistic or fewer properties are sold than expected, this would have a low financial impact on the Housing Company.

If both house prices are pessimistic and fewer properties are sold than expected, the financial impact would be medium in most cases modelled above. However, it is considered unlikely that both of these risks will occur simultaneously for the entire duration of the loan period. If this were to occur the peak borrowing is within the States of Jersey requirements and the longest loan requirement is 22 years (2 years in excess of States of Jersey requirements). In reality the Housing Company could manage this risk in order to repay the loan within 20 years.

The financial impact of this risk is assessed as low.

5.7.4.2 Probability that the financial impact of risk will occur

Given the uncertainty in the housing market at present, the probability that this risk will occur, to the extent that the financial impact is low, is assessed as medium.

5.7.4.3 The extent to which the risk is influenced by external factors

Although this risk can be mitigated by reviewing the type and volume of properties available for sale, the probability that this risk will occur is subject to house price movements. This is assessed as high for this risk.

5.7.4.4 Summary assessment

| Assessment for risk 4: Failure to receive required capital proceeds from the sale | |
|---|--------|
| Potential financial impact of risk | Low |
| Probability that risk will occur | Medium |
| The extent to which the risk is influenced by external factors | High |
| Overall risk assessment | Low |

The overall risk is assessed as low as this is the potential financial impact.

This risk will be a key focus for the Housing Company until stock development plans are completed and external debt has been repaid.

5.7.5 Risk 5: Fluctuations in RPI

5.7.5.1 Potential financial impact of risk

Sensitivity analysis has been performed on the potential financial impact of increased or decreased RPI as follows:

| | Sensitivities performed | Peak external borrowing | Year repaid |
|--------------------------------|--|-------------------------|-------------|
| Assumptions per business model | States of Jersey Statistics Unit "central" RPI projections. Long term projections are 3.5% growth per annum | £159m | 16 |
| Increase in RPI | States of Jersey Statistics Unit "optimistic" RPI projections for the duration of the business model. Long term projections are 4.5% growth per annum | £165m | 16 |
| Decrease in RPI | States of Jersey Statistics Unit "pessimistic" RPI projections for the duration of the business model. Long term projections are 2.5% growth per annum | £153m | 17 |

Within the sensitivities set out above, the Housing Company can meet its objectives of external borrowing being up to £200m and repaid within 20 years.

For completeness, larger fluctuations in RPI have been modelled using long term RPI of 0% and long term inflation of 6%. In both of these scenarios the financial impact of the risk is low.

A key reason for this risk having a low financial impact on the Housing Company is the expectation that rental income will rise at RPI plus an average earnings adjustment of 0.75%. Sensitivity analysis on this expectation is performed in risk 3 below.

5.7.5.2 Probability that the financial impact of risk will occur

The probability that this risk will occur in the short term is high due to the current economic uncertainties. Over the 30 year business model the probability is considered to be low as it is expected that RPI would even out to a reasonable level over the longer term. On balance, the probability that the financial impact of the risk will occur is assessed as medium.

5.7.5.3 The extent to which the risk is influenced by external factors

This risk is highly influenced by external factors.

5.7.5.4 Summary assessment

| Assessment for risk 5: Fluctuations in RPI | |
|--|--------|
| Potential financial impact of risk | Low |
| Probability that risk will occur | Medium |
| The extent to which the risk is influenced by external factors | High |
| Overall risk assessment | Low |

Although the probability that this risk will occur is medium and it is highly influenced by external factors, on the assumption that the proposals contained within this document are adopted, there is a low financial impact to the Housing Company. This is therefore assessed as posing a low overall risk to the Housing Company because even if it were to occur it would have a low financial impact on the Housing Company.

5.7.6 Risk 6: Rental income is lower than expected

5.7.6.1 Potential financial impact of risk

This is the risk that rental income is lower than expected because:

- ✚ Rental market growth is lower than expected
- ✚ Re-lets are lower than expected

It is assumed in the business model that the rental market will increase by RPI plus 0.75%. If market rent increases are less than RPI plus 0.75%, the Housing Company would receive less rent than expected from:

- ✚ Existing tenancies or re-let properties where rent is charged at 90% of market rent (as the rent for these properties would increase by market rent inflation)
- ✚ Existing tenancies where rent is above 90% of market rent as they would be frozen for longer than expected

The modelling assumes that expenditure, including the return to the States of Jersey and building costs, would increase by RPI. Where the expenditure is labour intensive it is assumed to increase by a further 0.75%.

To assess the financial impact of this risk, sensitivity analysis has been performed for the following scenarios:

1. Pessimistic rental market: A pessimistic rental market assumes that market rental increases will be 1% lower than forecast in the business model i.e. RPI plus 0.75% minus 1%. The sensitivity modelled assumes that the rental market will be pessimistic each year for the duration of the business model
2. Reduced re-let rate: Reduced re-lets assumes that re-lets will be 3.5% per annum each year for the duration of the model. This is half of the current and expected re-let rate of 7%
3. Pessimistic rental market and a reduced re-let rate: This is the combined impact of points 1 and 2 above

The forecast impact on the borrowing is noted in the table below. It is assumed when performing the sensitivity analysis that property sale of 15 units per annum will continue until the debt is repaid.

| | Per business modelling* | Pessimistic rental market | Reduced re-let rate | Pessimistic rental market and reduced re-let rate |
|---------------------------|-------------------------|---------------------------|---------------------|---|
| Peak external debt | £160m | £168m | £177m | £184m |
| Year external debt repaid | Year 16 | Year 21 | Year 23 | Year 26 |

*Business modelling assumes long term RPI of 3.5%, market rental increases of 4.25% and annual re-lets of 7%.

In addition to the above, the combined impact of a pessimistic rental market and a reduced re-let rate has been modelled using pessimistic and optimistic RPI forecasts and the results are in the table below. Long term pessimistic RPI is forecast to be 2.5% and long term optimistic RPI is forecast to be 4.5%. These projections are taken from the States of Jersey Statistics Unit.

| | Per business modelling | Pessimistic RPI | Optimistic RPI |
|---------------------------|------------------------|-----------------|----------------|
| Peak external debt | £160m | £170m | £184m |
| Year external debt repaid | Year 16 | Year 24 | Year 23 |

The financial impact of this risk is medium due to the extended borrowing period. This demonstrates the worst case scenario for this risk. However, it is unlikely that the rental market will rise at a lower rate than RPI for the entire duration of the model.

5.7.6.2 Probability that the financial impact of risk will occur

Given the current uncertainty in the rental market, the probability that this risk will occur is assessed as medium in the short term. It is, however, unlikely that this risk will occur for the entire duration of the business model period. On balance, the probability that this risk will occur is assessed as medium.

5.7.6.3 The extent to which the risk is influenced by external factors

This risk is influenced by external factors as it is impacted by the rental market as a whole. The extent to which the risk is influenced by external factors is assessed as medium as the Housing Company can influence rent levels by managing the condition of its properties.

5.7.6.4 Summary assessment

| Assessment for risk 6: Rental income is lower than expected | |
|--|--------|
| Potential financial impact of risk | Medium |
| Probability that risk will occur | Medium |
| The extent to which the risk is influenced by external factors | Medium |
| Overall risk assessment | Medium |

This risk will be a key focus for the Housing Company and overall has been assessed as medium risk.

5.7.7 Risk 7: Ability to repay external borrowing if stock development plans not achieved

5.7.7.1 Potential financial impact of risk

The financial modelling incorporates projected new build and refurbishment costs. External borrowing is drawn down in line with the projected costs and repaid partly by additional income from new builds and increased income from refurbished properties.

There are two risks identified:

1. The terms of the external borrowing draw downs have not yet been determined. If the terms of the draw down are fixed there is a risk that, if new build and refurbishment projects are delayed, cash could be drawn down which is not utilised
2. New build and refurbishment projects take longer to complete than forecast (for example, due to a planning delay) therefore delaying the expected additional rental income

The implications of the above risks are that cash would be drawn from the external borrowing facility, therefore incurring interest charges, with lower than forecast rental income to repay the debt.

The risks are quantified by assuming that all new units are brought in to use 1 year later than forecast and all refurbishment projects are completed 1 year later than forecast whilst costs of the development remain in line with the financial modelling. This includes allowance for further lost rent for refurbishment projects that require properties to be vacated. If this were to occur, the implications on the external borrowing are as follows:

| | Per business modelling | If new units delayed by 1 year |
|--------------------------------|------------------------|--------------------------------|
| Peak external borrowing | £160m | £173m |
| Year external borrowing repaid | Year 16 | Year 17 |

The Housing Company would meet the requirement to repay external borrowing within 20 years if all projects were delayed by 1 year. This scenario is considered to be "worst case" and no account has been taken of claims made against subcontractors and insurers.

Therefore, this risk is considered to have a low financial impact on the Housing Company's business model.

5.7.7.2 Probability that the financial impact of risk will occur

The business model includes prudent assumptions with regard to the cost and timing of the development plans. The probability that this risk will occur is therefore assessed as low.

5.7.7.3 The extent to which the risk is influenced by external factors

This risk is influenced by external factors to some extent due to the stock development work being performed by third party contractors. However, the management of this process will be controlled by the Housing Company and insurances will be in place. Therefore, the extent to which the risk is influenced by external factors is considered to be low.

5.7.7.4 Summary assessment

| Assessment for risk 7: Ability to repay external borrowing if stock development plans | |
|---|-----|
| Potential financial impact of risk | Low |
| Probability that risk will occur | Low |
| The extent to which the risk is influenced by external factors | Low |
| Overall risk assessment | Low |

As all elements of this risk are assessed as low, the overall risk assessment is assessed as low.

5.7.8 Risk 8: Failure to collect rents due and/or failure to manage the implementation of the proposed rent policy

5.7.8.1 Potential financial impact of risk

This risk could result in increased rent arrears and lower rent levels than expected.

Administration costs could also increase due to, for example, additional staff requirements and costs of increased correspondence with tenants, £200k is considered to be a prudent sensitivity for this risk.

The risk is analysed below.

| Risk | Sensitivities performed | Peak external borrowing | Year repaid |
|--------------------------------|--|-------------------------|-------------|
| Increased rent arrears | Bad debts increased by 2.5% of rental income per annum for years 1, 2 and 3 of the business model* | £164m | 17 |
| Lower rent levels | Market rents implemented are 5% lower than assumed in the business model. This reduction in base rents reduces rental income each year of the business model | £168m | 18 |
| Increased administration costs | Administration costs are £200k more than expected over years 1 and 2 of the business model | £160m | 16 |

*The Housing Department's bad debts are currently 0.26% of rental income. A key reason for this low level of bad debts is the direct payment of Income Support from the Social Security Department. Business modelling assumes that this arrangement will continue. This sensitivity modelled is therefore worst case

In the worst case scenario that all of these risks occurred, and assuming stock maintenance and development and the return to States of Jersey are in line with objectives, the resulting peak external borrowing would be £173m repaid by year 18. Therefore, this risk is considered to have a low impact on the viability of the Housing Company's business model.

5.7.8.2 Probability that the financial impact of risk will occur

The business model includes prudent assumptions. Additionally, plans will be implemented to reduce the probability that this risk will occur. The probability that this risk will occur is therefore assessed as low.

5.7.8.3 The extent to which the risk is influenced by external factors

This risk is influenced by external factors to some extent because rent is paid by third parties. However, the management of this process will be controlled by the Housing Company and so the extent to which the risk is influenced by external factors is considered to be low.

5.7.8.4 Summary assessment

| Assessment for risk 8: Failure to collect rents due and/or failure to manage the transition to new rents policy efficiently not achieved | |
|--|-----|
| Potential financial impact of risk | Low |
| Probability that risk will occur | Low |
| The extent to which the risk is influenced by external factors | Low |
| Overall risk assessment | Low |

This risk is not likely to occur as procedures will be put in place to manage this process effectively, and there are limited external factors influencing this risk. The overall risk assessment is assessed as low.

5.7.9 Risk 9: Increased interest rates on borrowing

5.7.9.1 Potential financial impact of risk

Increased borrowing costs would result in higher than expected finance costs and, therefore, higher than expected cash outflows.

As described in section 3.5.1.2, the interest rate on the internal borrowing facility of £40m is fixed and so sensitivity analysis is not required. From the perspective of the States of Jersey, the Treasury and Resources Minister considered any forgone opportunity costs to the States of Jersey as a result of providing this finance to the Housing Company prior to presenting R132/2011 States Investment Strategies to the States of Jersey on 1 November 2011. It was concluded that the 4% return from the Housing Company exceeds the current and anticipated return from the currency fund (where the funds would otherwise be retained).

As described in section 3.3.4, the Treasury Department have indicated that external borrowing will attract fixed interest at 5% and they believe this is sufficient to attract investors.

As the external borrowing facility has not yet been finalised, sensitivity analysis has been performed for fixed interest at 5.5% as this a potential scenario advised by the States of Jersey.

Assuming stock maintenance and development and the return to States of Jersey are in line with objectives, the resulting external borrowing would be £163m repaid by year 17. Therefore, the Housing Company would meet its borrowing requirements and the financial impact would be low.

If the interest rate was 9% then the financial impact would be medium (peak borrowing of £190m repaid by year 21). Until the terms of the loan are established (including whether interest is fixed or variable) it is considered prudent to assess the financial impact of this risk as medium.

5.7.9.2 Probability that the financial impact of risk will occur

As the terms of the external financing have not yet been agreed, the probability that this risk will occur is assessed as medium.

5.7.9.3 The extent to which the risk is influenced by external factors

This risk is influenced by external factors because the financing is external and the terms have not yet been agreed. This is therefore assessed as high.

5.7.9.4 Summary assessment

| Assessment for risk 9: Increased interest rates on borrowing | |
|---|--------|
| Potential financial impact of risk | Medium |
| Probability that risk will occur | Medium |
| The extent to which the risk is influenced by external factors | High |
| Overall risk assessment | Medium |

Overall, this risk is assessed as medium. When the terms of the external borrowing have been finalised, this will be revisited and will probably be assessed as lower risk, particularly if interest is fixed for the term of the loan as anticipated.

5.7.10 Other risk 10: Unexpected costs incurred

5.7.10.1 Potential financial impact of risk

This could be unexpected stock condition, utility, pension deficit and other unexpected costs. An increase in costs would result in higher than expected cash outflows.

The business model contains prudent assumptions and so it is not anticipated that there will be significant additional costs and so the financial impact is assessed as low.

As the peak external borrowing per the business modelling is £160m over 16 years, the level of additional costs incurred would need to be significant in order for this risk to have a medium financial impact.

In the event that there is a fundamental change to States of Jersey policies (for example in relation to planning regulations and utility costs), it is appropriate for the Housing Company to discuss the implications of such changes with the States of Jersey and how

that may impact upon the business model of the Housing Company including the annual return to the States of Jersey.

Therefore, this risk is considered to have a low impact upon the viability of the Housing Company's business model.

5.7.10.2 Probability that the financial impact of risk will occur

As the business model incorporates prudent assumptions, the probability of this risk occurring is considered to be low.

5.7.10.3 The extent to which the risk is influenced by external factors

This risk is influenced by external factors because additional costs could be incurred due to changes in regulation. This is assessed as medium.

5.7.10.4 Summary assessment

| Assessment for risk 10: Unexpected costs incurred | |
|--|--------|
| Potential financial impact of risk | Low |
| Probability that risk will occur | Low |
| The extent to which the risk is influenced by external factors | Medium |
| Overall risk assessment | Low |

The potential financial impact of this risk is low and it is not likely to occur. The extent to which the risk is influenced by external factors is medium. On balance the risk is assessed as low.

5.8 Summary financial risk assessment

| Risk | Potential financial impact | Probability | Extent to which influenced by external factors | Overall risk assessment | Risk owner |
|---|----------------------------|-------------|--|-------------------------|------------------|
| 1 Change to the basis of proposed rent policy | High | Low | Low | Low | Shared |
| <p>The potential financial impact of this risk is high but, on the assumption that the proposed return to the 90% of market rent for new tenancies policy contained within this document is adopted, there is low probability that the risk will impact the Housing Company's business model and low risk that this will be influenced by external factors. Therefore, the overall risk assessment is low.</p> <p>The risk is shared between the States of Jersey and the Housing Company as follows:</p> <ul style="list-style-type: none"> ✚ The States of Jersey will bear the financial impact of a change to the rent policy by, for example, accepting a lower return ✚ The Housing Company is responsible for implementing and maintaining the proposed policy and so will bear the financial impact if this is done inefficiently | | | | | |
| 2 Change to the basis of proposed return to the States of Jersey | High | Low | Low | Low | States of Jersey |
| <p>The potential financial impact of this risk is high but, on the assumption that the basis of the return proposed in this document is included in the Transfer Agreement, there is low probability that the risk will occur and low risk that this will be influenced by external factors. Therefore, the overall risk assessment is low.</p> <p>If the basis of the return changes, the States of Jersey bears the risk that the return may not be delivered. In practice, the Housing Company will work with the States of Jersey to discuss potential options which would enable the Housing Company to still deliver the return. This could include changing stock development plans (including re-profiling maintenance costs), overhead cost reductions, alternative income sources from widened activities, further property sales, delaying repayment of the internal loan and obtaining further external financing. The Housing Company will keep its operating practices under continuous review, with a view to minimising costs and maximising flexibility within its business model.</p> | | | | | |
| 3 Change to basis of external borrowing | Low | Low | Low | Low | Housing Company |
| <p>It is anticipated that a borrowing facility of up to £200m for up to 20 years will be made available to the Housing Company which can be repaid by additional income generated from new properties and when other cash surpluses are available. On the assumption that the borrowing is secured, as anticipated, prior to the incorporation of the Housing Company, the overall ongoing risk to the Housing Company is low.</p> <p>The risk of any change to the basis of the borrowing is owned by the Housing Company as they will be responsible for meeting the debt requirements.</p> <p>If the borrowing facility is not made available as anticipated, then this risk (including the risk owner) would need to be re-evaluated.</p> | | | | | |

| Risk | Potential financial impact | Probability | Extent to which influenced by external factors | Overall risk assessment | Risk owner | |
|--|--|-------------|--|-------------------------|------------|-----------------|
| 4 | Failure to receive required capital proceeds from the sale of social housing stock | Low | Medium | High | Low | Shared |
| <p>The overall risk is assessed as low as this is the potential financial impact.</p> <p>The risk is shared between the States of Jersey and the Housing Company because it is influenced by the housing market which is not under the control of the Housing Company. As the sensitivity analysis indicates that the potential financial impact is low, the Housing Company expects to be able to absorb the financial impact of this risk in to its operations and would, therefore, not require additional support from the States of Jersey. This could include changing stock development plans (including re-profiling maintenance costs), overhead cost reductions, alternative income sources from widened activities, further property sales in some years, delaying repayment of the internal loan and obtaining further external financing. The Housing Company will keep its operating practices under continuous review, with a view to minimising costs and maximising flexibility within its business model.</p> <p>Property sales compared to forecasts will be monitored closely by the Housing Company and statistics will be provided to the States of Jersey (in line with the agreed financial reporting protocols). Therefore, in practice, the States of Jersey and the Housing Company will work together to monitor the financial impact of this risk and to discuss potential solutions.</p> | | | | | | |
| 5 | Fluctuations in RPI | Low | Medium | High | Low | Housing Company |
| <p>Although the probability that this risk will occur is medium and it is highly influenced by external factors, on the assumption that the proposals contained within this document are adopted, there is a low financial impact to the Housing Company. This is therefore assessed as posing a low overall risk to the Housing Company.</p> <p>The Housing Company bears the financial impact of this risk.</p> | | | | | | |
| 6 | Rental income is lower than expected | Medium | Medium | Medium | Medium | Housing Company |
| <p>This risk will be a key focus for the Housing Company and overall has been assessed as medium risk.</p> <p>The Housing Company bears the financial impact of this risk. As the sensitivity analysis indicates that the potential financial impact is medium, the Housing Company expects to be able to absorb the financial impact in to its operations (as noted in part 1 of this table) and/or obtain suitable further financing and would, therefore, not require additional support from the States of Jersey.</p> <p>Rental income compared to forecasts will be monitored closely by the Housing Company and statistics will be provided to the States of Jersey (in line with the agreed financial reporting protocols). Therefore, in practice, the States of Jersey and the Housing Company will work together to monitor the financial impact of this risk and to discuss potential solutions.</p> | | | | | | |
| 7 | Ability to repay external borrowing if stock development plans not achieved | Low | Low | Low | Low | Housing Company |

| Risk | Potential financial impact | Probability | Extent to which influenced by external factors | Overall risk assessment | Risk owner |
|---|--|-------------|--|-------------------------|-----------------|
| <p>As all elements of this risk are assessed as low, the overall risk assessment is assessed as low.</p> <p>The Housing Company bears the financial impact of this risk. As the sensitivity analysis indicates that the potential financial impact is low, it is not anticipated that this risk will have a material effect on the Housing Company business model.</p> | | | | | |
| 8 | Failure to collect rents due and/or failure to manage the implementation of the proposed rent policy | Low | Low | Low | Housing Company |
| <p>The financial impact of this risk is low and it is not likely to occur as procedures will be put in place to manage this process effectively, and there are limited external factors influencing this risk. The overall risk assessment is assessed as low.</p> <p>The Housing Company bears the financial impact of this risk. As the sensitivity analysis indicates that the potential financial impact is low, it is not anticipated that this risk will have a material effect on the Housing Company business model.</p> | | | | | |
| 9 | Increased interest rates on borrowing | Medium | Medium | High | Shared |
| <p>Overall, this risk is assessed as medium. When the terms of the external borrowing have been finalised, this will be revisited and will probably be assessed as lower risk, particularly if interest is fixed for the term of the loan as anticipated.</p> <p>The risk is shared between the States of Jersey and the Housing Company until the terms of external financing are agreed. Once agreed, this will be revisited and, if the terms are as anticipated, the risk will become the responsibility of the Housing Company only.</p> | | | | | |
| 10 | Unexpected costs incurred | Low | Low | Medium | Shared |
| <p>The potential financial impact of this risk is low and it is not likely to occur. The extent to which the risk is influenced by external factors is medium. On balance the risk is assessed as low.</p> <p>The risk is shared between the States of Jersey and the Housing Company depending upon the nature and extent of the unexpected costs. It is anticipated that the States of Jersey will be responsible for any significant costs arising from legislative changes and that the Housing Company will be responsible for any other unexpected costs.</p> | | | | | |

5.9 Conclusion

The following is required prior to inception of the Housing Company:

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- ✚ External finance and terms thereof are to be finalised
- ✚ The proposed rent policy is to be adopted by a States Decision
- ✚ The basis of the return is to be agreed (in the Transfer Agreement)

If the above matters are dealt with as anticipated, the Housing Company is considered to be viable.

6 Management case

6.1 Introduction

This section of the business case sets out the project management and delivery considerations for the preferred option as identified in the Economic Case of this document, a States' owned housing organisation (the "Housing Company").

6.2 Project Management

The Housing Transformation Programme was established to address the Strategic Objectives and Critical Success Factors identified within the Strategic Case 2.2.10.

As such, the intent for the Programme was to deliver the capabilities required to enable transformation outcomes to happen.

The Housing Transformation Programme does not therefore deal with the detailed change management arrangements necessary within the new structures and organisations created by transformation. These will be set out during the development of the business change processes below.

The Housing Transformation Programme has been developed through a series of inter-connected projects organised into work streams.

The Governance of the Programme consists of a Ministerial Political Steering Group, a Programme Board of senior civil servants and a Delivery Team of officers supported by professional advisers.

The programme approach follows that recommended as best practice by the Office of Government Commerce:

http://www.ogc.gov.uk/programmes_and_projects.asp

The programme approach is formalised within a Programme Brief.

This structure and governance has enabled the coordinated development of integrated capability prior to an investment decision being sought by the States of Jersey to the transformation.

If an investment approval is achieved, the programme management arrangements will need to change to facilitate the coordinated implementation of business change within the new structures created by the transformation approvals.

It is envisaged that the Programme's Political Steering Group and Programme Board should be retained throughout the business implementation period to ensure continuity of governance, communication and complimentary coordination of activities against the original programme objectives and Critical Success Factors.

6.2.1 Shadow activity and delivery teams

Separate Delivery Teams will need to be established to implement the business change activity within the new organisations to enable their formal commencement – this will be termed the "Shadow" activity phase.

It is proposed that separate Shadow Delivery Teams should be established for the following functions:

- ✚ Strategic Housing Unit, Affordable Housing Regulator and readiness for transformation of Housing Trusts
- ✚ Housing Company Board
- ✚ Housing Company Delivery Organisation

Each Shadow Delivery Team shall appoint a Senior Responsible Owner who shall be responsible for the business change activity within their organisation's remit as defined by investment approval and qualified by the Political Steering Group and Programme Board.

It is proposed that the Senior Responsible Owners for the 3 delivery teams should be as follows:

| Shadow delivery team | Senior Responsible Owner |
|---|--|
| Strategic Housing Unit, Affordable Housing Regulator and readiness for transformation of Housing Trusts | Director of Corporate Policy – Chief Minister's Department |
| Housing Company Board | Shadow Chair of the Housing Company |
| Housing Company Delivery Organisation | Shadow Chief Executive of the Housing Company |

Each Delivery Team shall be allocated responsibility from the Political Steering Group for the transformation projects necessary to achieve the desired operational state of the relevant organisation.

The allocation of these projects by Delivery Team has been agreed. The Senior Responsible Owner of each Delivery Team shall be tasked with developing project plans for each project that enable the coordinated achievement of all necessary capabilities for the desired operational state of the organisation by the proposed commencement date of 1st July 2014.

The programme's detailed organisation arrangements proposed for the Shadow phase will be set out within a revised Programme Brief for the Political Steering Group's approval during the consideration period for the States investment decision in anticipation of a favourable outcome, but will only be implemented in the event of an approval being forthcoming.

6.3 Business Change Management

6.3.1 Business Change Management Arrangements

The business change management arrangements for the Programme during the shadow phase will be in accordance with the Office of Government Commerce best practice guidance.

Each Shadow Delivery Team will appoint a Business Change Manager or Managers to be responsible for implementing the necessary change, whilst retaining existing operational capability. The role of the Business Change Manager will be that set out within the Office of Government Commerce guidance. The change management approach adopted within each delivery team will be a matter for the Senior Responsible Owner to agree with the Programme Board and relevant stakeholders.

The proposed Business Change Managers for the three Shadow Phase Delivery Teams are as follows:

| Shadow delivery team | Senior Responsible Owner |
|---|---|
| Strategic Housing Unit, Affordable Housing Regulator and readiness for transformation of Housing Trusts | Head of Strategic Housing Unit |
| Housing Company Board | Finance Director of the Housing Company |
| Housing Company Delivery Organisation | Directors of Strategic Development, Operations and Finance of the Housing Company |

Funding for the business change management process has been identified and will be funded from a restructuring provision request in 2013. This request has been allowed for in the Medium Term Financial Plan.

6.3.2 Business Change Programme

The transformational projects anticipated for the business change programme required for each Shadow Delivery Team are summarised within the Programme Plan.

The transformational capability required is set out in output terms to enable the Senior Responsible Owner and Shadow Delivery Team latitude to adopt the most appropriate delivery approach given the setting and stakeholders.

In summary, the outputs required from each shadow Delivery Team by January 2014 are as follows:

Strategic Housing Unit, Affordable Housing Regulator and readiness for transformation of Housing Trusts

For establishment of the Strategic Housing Unit:

- ✚ Privy Council approved Enabling Laws to establish the Strategic Housing Unit, Affordable Housing Regulator and Housing Company
- ✚ States approved Enacting Regulations setting out the requirements for Providers to be enforced by the Affordable Housing Regulator
- ✚ A confirmed scope of cross tenure Housing Strategy for the Strategic Housing Unit
- ✚ A confirmed and resourced scope of activity, reporting structure and setting for the Strategic Housing Unit
- ✚ Appointed and transferred staff for the Strategic Housing Unit activity
- ✚ Service Level Agreements with any agency providing Strategic Housing Unit activity
- ✚ Service Level Agreements with providers concerning the Affordable Housing Gateway
- ✚ Establishment of a Tenant Focus Group

For establishment of the Affordable Housing Regulator:

- ✚ A confirmed and resourced scope of activity, reporting structure and setting for the Affordable Housing Regulator
- ✚ An appointed Affordable Housing Regulator(initially in shadow phase operation)

For Provider readiness of Regulation:

- ✚ Development of all codes of practice for Providers required for commencement
- ✚ Agreed initial business models and funding agreements for Providers
- ✚ An initial set of agreed performance reporting requirements for Providers

Housing Company Board

- ✚ An appointed Chair of the shadow Company via the Appointments Commission
- ✚ Strategic Housing Unit/Treasury and Resources approval of a finalised Transfer Agreement (including Funding Agreement)
- ✚ Appointment of other non-executive, Tenant and Treasury and Resources Board members
- ✚ Any necessary training and development of Board members delivered
- ✚ Approval of Memoranda and Articles of Association for the Company
- ✚ Establishment of approved governance arrangements for the Company
- ✚ Establishment of a shadow operating budget for the Company
- ✚ Registration of the Company
- ✚ Establishment of a shadow remuneration and accounts committees
- ✚ Establishment of shadow operations and strategic development committees

Housing Company Delivery Organisation

- ✚ Appointment of shadow Company staff through skills matching and recruitment of new roles as necessary
- ✚ Establishment of systems required for Board and Company reporting
- ✚ Establishment of new financial, IT and performance management systems required for transformed company operation
- ✚ Establishment of operational policies and procedures for the new Company
- ✚ Establishment of reporting procedures required for the Transfer Agreement
- ✚ Establishment of revised business processes required for Regulation
- ✚ Establishment of corporate branding and stakeholder engagement processes
- ✚ Establishment of revised business processes required for transformed company operation
- ✚ Establishment of Service Level Agreements where services are retained

Each element above will form a project or work stream of projects delivered by the Shadow Delivery Team to the Programme Board and Political Steering Group, the outputs and capabilities from which will be transferred to the new organisations on formation. The Programme Manager will continue to perform an overall oversight role for the programme which will ensure that the Delivery Teams deliver their outputs in a co-ordinated manner.

6.3.3 Business Change Assurance

During the development of the Housing Transformation Programme assurance has been provided by Professor Whitehead. This was necessary to ensure that the White Paper policy development proposed addressed the Green Paper challenges presented by the Professor.

During the business change programme, assurance for the delivery teams shall come from the retention of Michael Jones as Governance Adviser (CCHPR). This shall ensure consistency of the Delivery Team capabilities with the Programme outcome objectives. In addition:

- ✚ Sector Treasury Services Limited have provided quality assurance of this Full Business Case and the supporting business models
- ✚ BDO Limited, Chartered Accountants, as outsource service providers reporting to the Chief Internal Auditor have provided an agreed limited scope review in relation to the Housing Transformation Programme

6.3.4 Stakeholder Engagement Arrangements

During the development of the Housing Transformation Programme and through the issue of the "Achieving Decent Homes" White Paper, a stakeholder engagement and communications strategy has been maintained.

In the run up to the submission of the investment decision for approval, maintaining this engagement and communication strategy will be crucial to retaining stakeholder support for the transformation recommended.

Key stakeholders during the investment decision phase are known to be:

- ✚ Tenants (both of States of Jersey and Housing Trust housing)
- ✚ Residents of Victoria and George V Cottage Homes (on behalf of whom a separate approval is sought)
- ✚ States Members
- ✚ Housing Trusts (Both the 4 falling under regulation and those not)
- ✚ Other providers of social housing (Parishes and Charities)
- ✚ Interested Groups (Age Concern, Citizen Advice Bureau, etc.)
- ✚ Staff of the Housing Department
- ✚ The General Public

Following any investment decision approval, it is proposed that the Shadow Delivery Teams will operate their own stakeholder engagement plans as follows

Strategic Housing Unit, Affordable Housing Regulator and readiness for transformation of Housing Trusts

- ✚ Housing Company and Housing Trusts
- ✚ Tenants (through a Focus Group)
- ✚ Housing Company Board
- ✚ Parties to the Transfer Agreement (Chief Minister and Treasury and Resources)
- ✚ Shadow Strategic Housing Unit

Shadow Affordable Housing Regulator

- ✚ Housing Department Staff
- ✚ Housing Department Tenants

Housing Company Organisation

- ✚ Shadow Strategic Housing Unit
- ✚ Shadow Affordable Housing Regulator
- ✚ Housing Department Staff
- ✚ Housing Department Tenants

6.3.5 Stakeholder and Commissioning Approvals

The following approvals have been identified for the phases of the Housing Transformation Programme through to commencement of the new organisations.

6.3.5.1 Investment Decision Approval – States approval sought for Report and Proposition – April and July 2013

Approval will comprise review of this Full Business Case and the Enabling Laws for the framework proposed for transformation.

Stakeholder approvals proposed include:

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- ✚ Chief Minister's Department
- ✚ Treasury and Resources Department
- ✚ Social Security Department
- ✚ States Economist
- ✚ Law Officers and Law Draughtsman
- ✚ HTP Programme Board
- ✚ HTP Political Steering Group
- ✚ Corporate Management Board
- ✚ Council of Ministers
- ✚ States Employment Board

Consultations proposed include:

- ✚ Tenant's Forum and Resident's Associations and Panels
- ✚ States and Housing Trust Tenants
- ✚ Private sector Recipients of housing component of Income Support
- ✚ Housing Trusts
- ✚ Housing Department staff
- ✚ States Members
- ✚ Comité des Connétables Health, Social Security and Housing Scrutiny Panel
- ✚ Planning and Environment Department
- ✚ Health and Social Services Department
- ✚ Interested Groups

6.3.5.2 Shadow Strategic Housing Unit Establishment – May 2013

Approvals proposed:

- ✚ States of Jersey (Enacting Regulations)
- ✚ Chief Minister (assuming the setting for the Strategic Housing Unit is the Chief Minister's Department)
- ✚ Chief Executive of the States of Jersey

Consultations proposed:

- ✚ Regulated providers (Housing Company and Housing Trusts)
- ✚ Tenants Focus Group
- ✚ Affected Housing Department staff

6.3.5.3 Shadow Affordable Housing Regulator Establishment – March 2014

Approvals proposed:

- ✚ States of Jersey (Enacting Regulations)
- ✚ Chief Minister (assuming the setting for the Strategic Housing Unit is the Chief Minister's Department)
- ✚ Appointments Commission
- ✚ States Employment Board
- ✚ Attorney General / Law Officers Department

Consultations proposed:

- ✚ Regulated providers (Housing Company and Housing Trusts)
- ✚ Tenants Focus Group

6.3.5.4 Shadow Housing Company Board Established – September 2013

Approvals Proposed:

- ✚ States of Jersey (Enacting Regulations)
- ✚ Appointments Commission
- ✚ States Employment Board
- ✚ Parties to the Transfer Agreement
- ✚ Chief Minister (assuming the setting for the STRATEGIC HOUSING UNIT is the Chief Minister's Department)
- ✚ Treasury and Resources Minister

Consultations proposed:

- ✚ Housing Department staff

6.3.5.5 Formal commencement of Strategic Housing Unit operation – March 2014

Approvals proposed:

- ✚ Chief Minister (assuming the setting for the Strategic Housing Unit is the Chief Minister's Department)
- ✚ Chief Executive of the States of Jersey

Consultations proposed:

- ✚ Regulated providers (Housing Company and Housing Trusts)
- ✚ Tenants Focus Group
- ✚ Affected Staff

6.3.5.6 Formal commencement of Affordable Housing Regulator operation – March 2014

Approvals proposed:

- ✚ Chief Minister (assuming the setting for the Strategic Housing Unit is the Chief Minister's Department)
- ✚ Attorney General / Law Officers Department

Consultations proposed:




- ✚ Regulated providers (Housing Company and Housing Trusts)
- ✚ Tenants Focus Group

6.3.5.7 Formal commencement of Housing Company operation – July 2014

Approvals Proposed:

- ✚ States of Jersey (Enacting Regulations)
- ✚ Appointments Commission
- ✚ States Employment Board
- ✚ Parties to the Transfer Agreement
- ✚ Chief Minister (assuming the setting for the Strategic Housing Unit is the Chief Minister's Department)
- ✚ Treasury and Resources Minister
- ✚ Jersey Company Registration

Consultations proposed:

-  Affected staff
-  The Affordable Housing Regulator
-  Comptroller and Auditor General

6.4 Benefits Realisation Arrangements

The Achieving Decent Homes White Paper set out the key benefits from the proposed transformation. These were divided into benefits to Tenants, to the States of Jersey and to Providers of social housing.

To realise these benefits, a formal benefit management approach will be followed, broadly aligning with that identified as best practice by the Office of Government Commerce.

A Benefits Register has been prepared setting out (for each of the benefits) the desired outcome, the capability required to achieve the outcome and the project outputs necessary to build the necessary capability.

Each benefit has been allocated to a Business Change Manager within one of the Shadow Delivery Teams to oversee the delivery of the capability required to realise the benefit. An anticipated timing for delivery of the benefit capability has been indicated within the Plan. Any associated disadvantages will also be monitored and managed in the same way.

The Political Steering Group and Programme Board will monitor the delivery of the benefit capabilities by the Shadow Delivery Teams and review whether the anticipated benefit has been realised.

The benefits plan is summarised below.

| Reference | Benefit | Business change manager |
|------------------------|---|--|
| 1A | All social Housing Tenants benefit from 100% rolling compliance with DHS achieved and maintained | Company Director of Finance and Resources |
| 1B | All social housing tenants in decent homes benefit from reduced heating bills | Company Director of Finance and Resources |
| 1C | All social housing tenants in decent homes benefit from more planned and less responsive repairs | Company Director of Operations |
| 1D | All social housing tenants in decent homes benefit from having to make less complaints | Company Director of Operations |
| 1E | All social housing tenants in decent homes benefit from improved health | Company Director of Strategic Development |
| 1F | All social housing tenants in decent homes benefit from reduced fuel poverty | Company Director of Finance and Resources |
| Potential Dis-benefit. | Increased awareness of Tenants to DHS means higher expectations leading to lower customer satisfaction levels | Company Director of Operations |
| 2A | Improved opportunity for those prospective tenants most in need to be prioritised by Providers | Strategic Housing Unit |
| 2B | Improved transparency of allocation to those most in need (prospective tenants) | Strategic Housing Unit |
| Potential Dis-benefit. | Proportion of Tenants on Income Support increases to unsustainable levels for business models | Strategic Housing Unit |
| 3A | Better match for all Company Tenants to the right home for their needs | Company Director of Operations |
| 3B | An increasing proportion of Life Long and Sheltered Homes are made available for those social housing Tenants who need them | Company Director of Strategic Development / Housing Trusts |

| Reference | Benefit | Business change manager |
|------------------------|--|---|
| Potential Dis-benefit. | Perceived reduced security of Tenure results in reduced transfers | Strategic Housing Unit |
| 4A | Tenants on Income Support are fully protected from the adverse effect of the proposed rent policy | Company Director of Finance and Resources / Social Security |
| 4B | All Tenants in social housing have hidden rental subsidy removed | Company Director of Finance and Resources / Social Security |
| Potential Dis-benefit. | Unacceptable adverse effects on those asked to pay more | Company Director of Finance and Resources / Social Security |
| 5A | Tenants in social housing can appeal to the Social Housing Regulator about infringement of regulations. | Strategic Housing Unit |
| 6A | Company Tenants benefit from continual improvement in services | Social Housing Regulator |
| 7A | All social housing Tenants benefit from greater engagement | Social Housing Regulator |
| 8A | Chief / Housing Minister benefit from focussing on long term policy | Strategic Housing Unit |
| 9A | The States and all social housing Tenants benefit from defined performance standards | Social Housing Regulator |
| 10A | Accountability for social housing regulation is clearly defined | Strategic Housing Unit |
| 11A | Accountability for prioritising social housing resources is clearly defined. | Strategic Housing Unit |
| 12A | Tenants, Providers and Lenders benefit from a robust regulatory structure | Strategic Housing Unit |
| 13A | Social Housing Providers and developers benefit from the improved viability of social housing | Strategic Housing Unit |
| 14A | Improved transparency of the costs of social housing provision is achieved for the States | Social Housing Regulator |
| 15A | Social Housing Providers generate income that increases investment in social housing | Social Housing Regulator |
| 16A | Social Housing Providers become more financially independent | Strategic Housing Unit |
| 17A | The commercial viability of private development of social housing is enhanced | Strategic Housing Unit |
| 18A | The Housing Company does not require additional capital funding from the States for housing maintenance | Company Director of Finance and Resources |
| 19A | Responsibilities for setting policy, regulation and delivery of social housing are clearly delineated removing Ministerial conflicts of interest | Strategic Housing Unit |
| 20A | The delivery of social housing is more closely aligned with social policy objectives | Strategic Housing Unit |
| 21A | Social Housing Providers manage the social housing stock more efficiently due to rent policy certainty | Strategic Housing Unit |
| 22A | The Affordable Housing Gateway provides clear indication of demand and removes allocation duplication | Strategic Housing Unit |
| 23A | The Company demonstrates greater focus on providing excellent customer services | Company Director of Operations |

6.5 Risk Management

All significant and material risks to the effective delivery of the Housing Transformation Programme desired outcomes have been identified, analysed, monitored and mitigated against. This is being achieved through the maintenance of a risk register. The risk register is a "live" document and is reviewed on an ongoing basis as an integral part of the project governance meetings. Risks can be generated by any member of the Programme Governance and are then assessed by the Delivery Team. Those risks that score less than 10 are managed within the Delivery Team. Those that are 10 or more are brought to the Programme Board for consideration. Risks with scores exceeding 15 are taken by the Senior Responsible Owner to Corporate Strategy Group for consideration.

In May 2012, the Housing Department reviewed the risk register by holding a risk assessment workshop (facilitated by a risk management professional from Moody's Risk Management Services Limited). The risk register has also been reviewed and updated by the Housing Department senior management team in September 2012.

The following table summarises the high level risks identified for this project from the detailed risk analysis.

| Risk Descriptions | Residual Risk Score | Controls Currently in Place | Risk Owner |
|---|---------------------|---|-----------------------------------|
| Stakeholder Support: The risk the Housing Department does not gain widespread stakeholder support to achieve the transformation objectives | 8.9 | A communication strategy is in place; Programme Board oversees progress; Supported by Ministerial oversight and Tenants Groups | Programme Manager |
| Errors and Omissions: The risk of errors and omissions in our submissions including the enabling laws, full business case, report and propositions, conveyancing arrangements or change programme | 8.4 | Programme management controls are in place; Quality Assurance Processes are in place; Weekly progress meetings are held | Chief Officer |
| Milestones: The risk we fail to achieve all planned milestones including joint review output, FBC and other general programme slippage | 8.1 | Programme management controls are in place; Quality Assurance Processes are in place; Weekly progress meetings are held. Fortnightly meetings with workstream leaders are in place; Concentration of transformation work is at a senior level | Programme Manager |
| Borrowing: Failure to secure borrowing at rates assumed within the business plan | 7.8 | Potential funder meetings have taken place. Options are being developed in conjunction with the Treasury | Director of Finance and Resources |
| Political Support: Failure to attract Political support to regulatory model | 4.7 | A Political Steering Group is in place Regular briefings and individual meetings with Politicians and Housing Minister take place; External legal and governance advisors are being used to inform decision making | Director of Strategic Development |

| Risk Descriptions | Residual Risk Score | Controls Currently in Place | Risk Owner |
|---|---------------------|---|-----------------------------------|
| The risk we lack the human resources to achieve our objectives - having the right people | 9 | An organisational development review has been undertaken which has defined change needed from the existing human resources to those required in the Housing Company | Chief Officer |
| Underlying Assumptions: The risk the underlying assumptions in our business case are found to be incorrect | 6 | Stress testing of all assumptions made in the business case are undertaken with financial advisers and Treasury | Director of Finance and Resources |
| Key Staff: The risk we lose key staff during the transformation process | 7.1 | Quarterly staff briefings are taking place; Contingency emergency plans are in place; Succession planning will need to be formalised | Chief Officer |
| Pension Funding: The risk we are unable to fund pensions in respect of HA staff or the pension fund places an unsustainable future burden on the business | 6.2 | Pension liabilities are fully understood, quantified and built into the financial plans | Director of Finance and Resources |
| Service Disruption: The risk normal business as usual services are disrupted as part of the transformation process | 8.3 | Complaints monitoring from Tenants, stakeholders and States Members is in place; Weekly programme delivery team meetings are in place to address arising issues | Director of Finance and Resources |
| MIS: The risk we lack the Management Information Systems (MIS) (financial and operational) to achieve our objectives - having the right systems | 9 | The majority of existing financial and information technology systems will be retained for the transformation period and funded plans are in place to replace them from the second year of operation onwards. Existing KPI's have been supplemented with best UK Housing experience. A performance dashboard is in place | Director of Finance and Resources |
| Staff Culture: The risk our staff fail to make the transition, in terms of behaviours, to the Housing Company. - having the right culture | 8.3 | Quarterly staff briefings are in place; Transformation outcomes were included in the staff appraisal process for 2011; On-going dialogue with staff over a number of years - means a "no surprises" policy is maintained | Director of Operations |
| Board: The risk the Housing Company does not have a strong Board which is focused on Social Housing and which cannot make hard commercial decisions | 11.6 | The services of a leading Housing governance expert is being used to advise on best practice | Chief Officer |
| States of Jersey Interventions: The risk of States of Jersey interventions into the running of the HA | 9.8 | The Political Steering Group is conscious of this risk. The proposed Transfer Agreement will be informed by experienced advisers | Chief Officer |
| Borrowing: The risk we cannot affordably borrow capital to fund the outcomes of the business plan | 7.3 | Options being developed in conjunction with the Treasury - estimates are a facility of £160M will be required | Director of Finance and Resources |

| Risk Descriptions | Residual Risk Score | Controls Currently in Place | Risk Owner |
|--|---------------------|--|-----------------------------------|
| Partner: The risk we cannot find suitable partners to complete all necessary work to achieve the Jersey Standard | 6.9 | An annual programme of works is developed to ensure there is a good and competent partner base; | Director of Operations |
| Project Failure: The risk Jersey HA loses the confidence of its stakeholders due to a major project failure or series of systemic failures | 9.2 | Key Lines of Enquiry reviews of services have been undertaken to identify best customer practice; | Chief Officer |
| Surplus Retention: The risk States of Jersey calls in surpluses to avoid cutting key States of Jersey services (pre transfer) which undermines our business activity | 6.3 | All Comprehensive Spending Review savings have been achieved by the Department; A "carry over" facility has been allowed to ensure maintenance levels do not fall; A thorough and robust Departmental and proposed Company business plan is in place | Chief Officer |
| Economic Climate: The risk our business plan would become unviable if there is continuing low inflation rates | 8.8 | Specific sensitivities have been undertaken within the Full Business Case | Director of Finance and Resources |
| Transfer Agreement: Entering into the transfer agreement may result in the HA being unable to fulfil its obligations or being bound by adverse contractual terms | 7.2 | Experienced Legal advisors are assisting with the Transfer Agreement; Oversight is provided by the Chief Minister's Department. and Treasury | Director of Strategic Development |
| H&S: We fail in our health and safety obligations leading to penalties and damage to reputation | 8 | Appointment of an Health and Safety Manager is enabling continuing improvements | Director of Operations |
| Borrowing: We fail to invest wisely or to borrow utilising the best financial products caused by inadequate management information resulting in financial loss | 5.9 | Experienced financial and legal advisers are assisting in the development process and quality assuring the Full Business Case approach | Director of Finance and Resources |
| New Systems: New systems are not project managed efficiently resulting in higher costs and loss of business | 6 | The Housing team are increasingly experienced in change management. Proven programme management methodologies are employed and dedicated programme and project management capability is deployed | Director of Finance and Resources |
| Inflation: Price and cost inflation accelerate to such a degree that we are unable to meet our savings plan or target margin | 6.5 | Appropriate sensitivity analyses for inflation are included within the Full Business Case | Director of Finance and Resources |
| Partnership: The risks key partnership arrangements (JDC and TTS) fail | 5.2 | Existing client/contractor proven relationships are in place; An issues escalation and resolution process is in place | Director of Strategic Development |

6.6 Contract Management

The following contract management arrangements are necessary for successful completion of the transformation.

Strategic Housing Unit

It is proposed that the Strategic Housing Unit setting should be the Chief Minister's Department. This Department is concerned with cross-departmental policy resources and therefore is not an appropriate setting for operational delivery.

Therefore, it is proposed that the Affordable Housing Gateway should be operated under agency through a Service Level Agreement with another States Department – probably the Department for Social Security. This will enable the Gateway to benefit from enhanced staff resources to ensure business continuity and management with experience of dealing with issues arising from means testing.

Once the setting and policy scope of the Strategic Housing Unit is defined there may be other elements of operational work that would be better operated under agency.

Affordable Housing Regulator

The Affordable Housing Regulator is anticipated to be a part time post at outset, due to the limited size of the social housing sector. The appointed Regulator may require some administrative support from the States of Jersey at key times in the assessment and reporting cycle, and therefore it is anticipated that a Service Level Agreement with the Strategic Housing Unit will be necessary.

Housing Company

The new Housing Company will commission a number of new services upon commencement.

These will include contracted arrangements for provision of:

- ✚ Search consultancy (for appointment of Board members)
- ✚ Remuneration advice (for the Remuneration Committee)
- ✚ Treasury services
- ✚ Legal advice (for the stock transfer and transfer agreement confirmations)
- ✚ Human resources and organisational development advice

The following retained services are proposed to be the subject of contracts for defined periods following establishment of the new Housing Company:

- ✚ Insurance (it is anticipated that the Company will be able to employ the States Insurance policy)
- ✚ Information technology (including J D Edwards financial management and Saffron housing management packages)
- ✚ Pension advice (it is proposed that the new Company will be an admitted body within the States of Jersey PECS pension scheme)
- ✚ Cashier and payroll services
- ✚ Facility management services (It is yet to be decided if the new Company will lease its current States office accommodation or whether this will be transferred to the Housing Company on inception). An appropriate adjustment will be made to the annual return if the accommodation is transferred

The arrangement for these services will be developed during the shadow Company phase.

6.7 Post Project Evaluation

Following establishment of the framework proposed by the transformation programme, a formal review of the Programme will be undertaken. Before commencing the review all Programme information (concerning the Programme budget, planning, risk and benefit management etc.) will be updated and finalized.

The Programme Review will consider whether:

- ✚ The Programme governance has been successful
- ✚ The Programme budget and plan have been achieved
- ✚ Programme risk and benefit management arrangements have been successful
- ✚ Business case assumptions remain valid and what activity to manage any necessary change has occurred
- ✚ Identified benefits have been realised and to what extent
- ✚ Any disadvantages have arisen and how these should be addressed
- ✚ Any ongoing support required from the States of Jersey for the framework
- ✚ There are any key lessons learned for the States of Jersey from the Programme

The Review will also identify the Programme closure arrangements required.

Elements of the Review will be produced by the Senior Responsible Owners of each of the Shadow Delivery Teams and presented to the Programme Board and Political Steering Group for approval.

Once the review has been completed, the Political Steering Group will formally feedback the Review findings to the States of Jersey and confirm the Programme closure arrangements.

Appendices

Appendix A Risk analysis

Section 3.6.1 of the Economic Case summarises the assessment of inherent risks for each option. The reasons for this assessment are noted in the tables below.

Status Quo – Option 1

| Key risk | Likelihood & reasons |
|---|---|
| Delivery vehicle is not self-sustaining | High – business model is not viable and no finance is available |
| Delivery vehicle is not flexible and able to change | High – no finance provided, limited autonomy |
| Required income stream is not delivered | High – business model is not viable and so the surpluses (which are lower than States of Jersey expectations) could not be returned |
| Regulatory, policy and service delivery functions not separated | High – no change from the existing arrangements |
| Overall risk rating: | High |

States Department – Option 2

| Key risk | Likelihood & reasons |
|---|---|
| Delivery vehicle is not self-sustaining | High – the vehicle could deliver Decent Homes Standard within 10 years but has insufficient sources of finance to deliver investment plans |
| Delivery vehicle is not flexible and able to change | High – limited sources of finance, limited autonomy |
| Required income stream is not delivered | High – surpluses could be returned with Decent Homes Standard being met but they are lower than States of Jersey expectations. Surpluses could not be returned if stock is developed beyond Decent Homes Standard |
| Regulatory, policy and service delivery functions not separated | High – no change from existing arrangements |
| Overall risk rating: | High |

Arms Length Management Organisation – Option 3

| Key risk | Likelihood & reasons |
|---|---|
| Delivery vehicle is not self-sustaining | High – the vehicle could deliver Decent Homes Standard within 10 years but has insufficient sources of finance to deliver investment plans |
| Delivery vehicle is not flexible and able to change | Medium – limited sources of finance but enhanced autonomy and governance |
| Required income stream is not delivered | High – surpluses could be returned with Decent Homes Standard being met but they are lower than States of Jersey expectations. Surpluses could not be returned if stock is developed beyond Decent Homes Standard |
| Regulatory, policy and service delivery functions not separated | Medium – the nature of appointments to the Board could compromise independence and the separation of functions |
| Overall risk rating: | Medium to High |

Trading Operation – Option 4

| Key risk | Likelihood & reasons |
|---|--|
| Delivery vehicle is not self-sustaining | Low – Funding available to deliver stock investment plans. Business model is viable |
| Delivery vehicle is not flexible and able to change | Medium – sufficient sources of finance but limited autonomy and governance |
| Required income stream is not delivered | Medium – stock could be developed and surpluses could be returned but surpluses are lower than States of Jersey expectations |
| Regulatory, policy and service delivery functions not separated | Medium to High – no independent board but management is separate from regulation |
| Overall risk rating: | Medium |

Hybrid Trading Company – Option 5

| Key risk | Likelihood & reasons |
|---|---|
| Delivery vehicle is not self-sustaining | Low – Funding available to deliver stock investment plans. Business model is viable |
| Delivery vehicle is not flexible and able to change | Low – Enhanced autonomy and governance. Sufficient sources of finance to deliver stock development plans |
| Required income stream is not delivered | Medium – stock could be developed and surpluses could be returned but surpluses are lower than States of Jersey expectations |
| Regulatory, policy and service delivery functions not separated | Low to Medium – functions will be separated but the extent of separation could be compromised by a lower level of independence at board level than some options |
| Overall risk rating: | Low to Medium |

Wholly Owned Housing Company – Option 6

| Key risk | Likelihood & reasons |
|---|---|
| Delivery vehicle is not self-sustaining | Low – Funding available to deliver stock investment plans. Business model is viable |
| Delivery vehicle is not flexible and able to change | Low – Enhanced autonomy and governance. Sufficient sources of finance to deliver stock development plans |
| Required income stream is not delivered | Low – stock could be developed and the return to States of Jersey delivered. The return is in line with States of Jersey expectations |
| Regulatory, policy and service delivery functions not separated | Low – service delivery by an outside body results in a separation of functions |
| Overall risk rating: | Low |

Newly Created Social Landlord – Option 7

| Key risk | Likelihood & reasons |
|---|---|
| Delivery vehicle is not self-sustaining | Medium– Funding available to deliver stock investment plans. Business model is viable. Scale of borrowing required increases the risk of interest rate exposure |
| Delivery vehicle is not flexible and able to change | Low – Enhanced autonomy and governance. Sufficient sources of finance to deliver stock development plans. |
| Required income stream is not delivered | Low – The majority of the income stream would be delivered in year 1. Subsequent income streams would be based on asset sales |
| Regulatory, policy and service delivery functions not separated | Low – service delivery by an outside body results in a separation of functions |
| Overall risk rating: | Low to Medium |

Appendix B Refurbishment and new build projects

Section 3.4 of the Economic Case refers to refurbishment and new build projects. These are listed below along with the estimated total costs. For comparison purposes, the projects included at Outline Business Case stage are also included. Individual project costs are not shown as this is considered to be commercially sensitive. Costs are indicative and are subject to change, particularly for projects for which feasibility studies have not yet been performed. Costs will be managed by the Housing Company as each of the projects is progressed.

| | OBC stage | FBC stage |
|---|----------------|----------------|
| Refurbishment Costs | £000s | £000s |
| Repayment for Pomme D'or scheme | | |
| Le Squez - Phase 3b | | |
| Victoria Cottage Homes (new build project at OBC stage) | | |
| Jardin des Carreaux | | |
| La Collette | | |
| Journeaux Street Intensification | | |
| Hampshire Gardens | | |
| Convent Court | | |
| Caesarea Court | | |
| De Quetteville Court High Rise | | |
| Hue Court High Rise | | |
| Osborne Court | | |
| Refurbishment Costs | 42,274 | 54,257 |
| New build costs on existing housing sites or sites covered by P40/2012 | £000s | £000s |
| Repayment for Le Squez - phase 2a and 2b | | |
| Le Squez - Phase 2c | | |
| Journeaux Street, 2 - 4 | | |
| Lesquenade 1 | | |
| Ann Court (project being undertaken by a Housing Trust) | | |
| Le Squez - Phase 4 | | |
| Le Squez - Phase 5, 7, 8 | | |
| Le Squez - Phase 6, 9, 10, 11 and 3a | | |
| Victoria Cottage Homes (refurbishment project at FBC stage) | | |
| Lesquenade 2 | | |
| Fields 516, 517 and 518 St Saviour | | |
| La Collette - Block B and C | | |
| La Collette - Blocks C, D and F | | |
| New build costs | 89,664 | 116,060 |
| Total refurbishments and new build costs | 131,938 | 170,317 |
| New build costs on other social housing sites | £000s | £000s |
| Former Le Coin Site | | |
| Summerland Site | | |
| Ambulance Station Site | | |
| Pine Ridge | | |
| Additional new build costs | - | 31,055 |
| Overall total | 131,938 | 201,372 |

Appendix C Description of delivery options

Section 3.4.3 refers to the delivery options which are described below.

Option 1 – Status Quo

Under this option the provision of the housing service would continue to be provided by the Housing Department.

- ✚ There is no change to the implementation of the rents policy ie rents increase at RPI plus wage inflation annually
- ✚ Management and ownership remains with States of Jersey
- ✚ No borrowing permitted either internally from States of Jersey reserves or externally from institutional lenders
- ✚ Sale receipts are retained within the housing department business model to finance capital expenditure
- ✚ Projected surpluses are treated as a contribution to States of Jersey. See section 3.4.3 for definition of surpluses
- ✚ There are no changes to the way that governance, policy and regulation is currently delivered

Option 2 – States Department (with internal borrowing)*

This option is a variation on the Status Quo option with implementation of the proposed rent policy (as described in section 3.4.1) and additional support for capital expenditure available in the form of internal borrowing from States of Jersey reserves.

- ✚ Management and ownership remains with States of Jersey
- ✚ Internal borrowing from States of Jersey resources is permitted at a rate of 4% up to £40m
- ✚ Sale receipts are retained within the housing department business model to finance capital expenditure
- ✚ Projected surpluses are treated as a contribution to States of Jersey. See section 3.4.3 for definition of surpluses

* Although the option of a States Department with access to external borrowing has not been separately considered as an option, the results and performance of this alternative option is considered to be very similar to option 4 below.

Option 3 – Arms Length Management Organisation

The rationale for this approach is that it provides independence for the management while maintaining the ownership of communal assets by States of Jersey.

- ✦ Wholly owned by States of Jersey
- ✦ Management to move arms length from States of Jersey, governance being provided by a Board drawn from members of the community who may be tenants or leaseholders and people with specific skills which would be of benefit to the Governing Board; the constitution of the Arms Length Management Organisation specifying the constituent groups
- ✦ Internal borrowing from States of Jersey resources is permitted at a rate of 4% up to £40m
- ✦ Sale receipts are retained within the housing department business model to finance capital expenditure
- ✦ Projected surpluses are treated as a contribution to States of Jersey. See section 3.4.3 for definition of surpluses
- ✦ This approach would result in additional costs estimated at:
 - ✦ Purchasing the pension debt from States of Jersey of £2,135k
 - ✦ Setting up costs for transferring staff, establishing the Board and the operating framework and communications with the tenants of £284k
 - ✦ Enhanced governance of £300k
 - ✦ Central support costs of £1m
 - ✦ An allowance for the regulator of £120k

Option 4 – Trading Operation

Under this option the Housing Department would be designated as a Trading Operation in accordance with section 23 of Public Finances (Jersey) Law 2005 and would be subject to Financial Direction 3.1 'Financial Administration of Trading Operations'.

Internal borrowing from States of Jersey resources is permitted at a rate of 4% up to £40m.

This option differs from the arms length management option because in addition to internal borrowing, available to Trading Operations in accordance with sections 5.10 and 5.11 of the direction, there would also be scope to access borrowing taken out on its behalf by States of Jersey. Sections 5.23 to 5.27 of the financial direction specify that the Minister of Treasury and Resources may approve external borrowing by States of Jersey on behalf of trading operations. In this case the trading operation would need to submit a business case for the borrowing identifying the funding sources for the costs of servicing and repaying the loan; capital projects would continue to require States approval.

The Trading Operation would operate as a discrete trading department that is directly accountable to States of Jersey. It would not have a separate Board of management. This is consistent with the approach taken to other States of Jersey trading operations, and provides another key difference between the Arms Length Management Organisation and Trading operation options.

As a trading operation the housing department would have to agree its business model with the Minister for Treasury and Resources and its revenue and capital budget would require States approval.

In summary, this option has the following characteristics:

- ✚ A trading operation that is wholly owned by States of Jersey
- ✚ Management to move to arms length but still under the direction of a Minister
- ✚ Sale receipts are retained within the housing department business model to finance capital expenditure
- ✚ Funding for capital expenditure comes from sale receipts, States of Jersey reserves (internal) or external borrowing taken out by States of Jersey on behalf of the Trading Operation
- ✚ Projected surpluses are treated as a contribution to States of Jersey. See section 3.4.3 for definition of surpluses
- ✚ This approach would result in setting up costs associated with establishing the Trading Operation, the operating framework and communications with tenants. £185k has been allowed for these costs

Option 5 – Hybrid Trading Company

This option is similar to the Trading Operation option in that the stock remains wholly owned by States of Jersey. However, it would be managed at arm's length from States of Jersey by a management board. Under this option the trading company would be established as a separate legal entity, which is controlled by States of Jersey and able to borrow on the private market with government support. The Trading Company's day to day operations would therefore be subject to direct influence from States of Jersey, although to a lesser extent than under options 1, 2 and 4.

- ✚ Wholly owned by States of Jersey.
- ✚ Management to move arms length from States of Jersey. Governance being provided by a Board comprising Ministers and members of the community (who may be tenants or leaseholders and people with specific skills which would be of benefit to the Governing Board– as with the Arms Length Management Organisation option).
- ✚ Internal borrowing from States of Jersey resources is permitted at a rate of 4% up to £40m
- ✚ External borrowing with government support permitted. This is assumed to require a States of Jersey guarantee
- ✚ Sale receipts are retained within the housing department business model to finance capital expenditure
- ✚ Projected surpluses are treated as a contribution to States of Jersey. See section 3.4.3 for definition of surpluses
- ✚ This approach would result in additional costs estimated at:
 - ✚ Purchasing the pension debt from States of Jersey of £2,135k
 - ✚ Setting up costs for transferring staff, establishing the Board and the operating framework and communications with the tenants of £314k
 - ✚ Enhanced governance of £300k
 - ✚ Central support costs of £1m
 - ✚ An allowance for the regulator of £120k

Option 6 – Transfer to a States of Jersey wholly owned Housing Company

Under this option a new housing company, wholly owned by States of Jersey, would be set up to manage the housing service.

Two funding scenarios have been considered:

- ✚ a) A freehold transfer with a licence to borrow against the collateral of the housing stock
- ✚ b) A leasehold transfer with borrowing against the value of rental streams. This option is assessed at the end of this Appendix

Option 6b is not considered to be a preferred option for the reasons stated below. Therefore, the assessment of option 6 in the Economic Case is based on a freehold transfer (option 6a).

In summary for this option, the assumptions are:

- ✚ Management to move arms length from States of Jersey. Governance to be provided by a Board of Management as with the Hybrid Trading Company option.
- ✚ Internal borrowing from States of Jersey resources is permitted at a rate of 4% up to £40m
- ✚ External borrowing with government support permitted.
- ✚ An agreed annual return is made to States of Jersey annually. The remaining surplus/deficit is retained by the new housing company
- ✚ This approach would result in a more autonomous organisation than under options 1 to 5
- ✚ This approach would result in additional costs estimated at:
 - ✚ Purchasing the pension debt from States of Jersey of £2,135k
 - ✚ Setting up costs for transferring staff, establishing the Board and the operating framework and communications with the tenants of £685k
 - ✚ Enhanced governance of £300k
 - ✚ Central support costs of £1m
 - ✚ An allowance for the regulator of £120k

Option 6 freehold or leasehold consideration

As described above, under option 6, 2 options are being considered.

The key advantage for States of Jersey in transferring its housing assets to the Housing Company on a leasehold basis is that it retains more direct control over those assets. The States of Jersey retains the freehold assets, which could be used as collateral independently of the Housing Company.

A leasehold transfer reduces the Housing Company's flexibility to use the assets at its disposal and the Housing Company would have less certainty as to its entitlement to sales proceeds. This may result in reductions and/or delays to stock development plans.

Lenders consider leasehold interests to offer a much lower level of security than freehold interests. A leasehold transfer may, therefore, result in the Housing Company experiencing difficulties in obtaining external finance. Independent financial advisors, Sector Group, advise that the perceived reduction in security can be so significant that lenders refuse to lend. Sector Group further advises that this is likely in the current economic circumstances, which have deteriorated since the Outline Business Case stage. Sector Group believes that this represents a significant risk of the Housing Company being unable to raise the required level of borrowing, unless States of Jersey offers additional guarantees or security to lenders. They advise that this adds a layer of complexity which may not be attractive to potential lenders.

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On balance, a freehold transfer offers greater security to funders and provides the Housing Company with greater flexibility in its use of the assets. States of Jersey would no longer have direct control over the housing assets. However, it would be able to protect its interests through its ownership of the Housing Company, as well as through regulatory requirements and the terms of the Transfer Agreement.

Option 6b: leasehold transfer, is therefore not the preferred option of options 6a and 6b.

Option 7 – Sale of freehold to a new social landlord

This is the most radical option, involving the freehold sale of the housing stock to a single social landlord which could be an existing Trust, a newly set-up landlord, probably based on the existing management as with the majority of stock transfers in the UK, or an existing social landlord from the UK, France or the Netherlands.

- ✚ Under this option the freehold of the housing stock would be sold by States of Jersey in return for a capital receipt. The capital receipt has been estimated using the 'Tenanted Market Value' method as used for stock transfers in the UK
- ✚ Management (and staff) would move from States of Jersey to the new social landlord. Governance being provided by a Board drawn from members of the community who may be tenants or leaseholders and people with specific skills which would be of benefit to the Governing Board (as with options 3, 5 and 6), the constitution of the Company specifying the constituent groups
- ✚ The new landlord would be free to borrow on the private market to fund the purchase price and any investment costs and would have no borrowing facility with States of Jersey
- ✚ For the purpose of this appraisal it is assumed that the new landlord would pay the proceeds of sales back to States of Jersey and it has been compensated for 15 sales per annum through the Tenanted Market Value in the business model. It is assumed there would be a sharing agreement between States of Jersey and the new landlord for the present value of foregone net rent income (after management, maintenance and improvement costs are deducted). Should the level of sales differ from the projected 15 per annum, the landlord would be compensated for this. Thus, sales would have a neutral impact on the new landlord's business model. The balance of the receipt from sales would be returned to States of Jersey. This method of sharing sales receipts is used in respect of most transfers in the UK
- ✚ There would be no transfer of surpluses or deficits to States of Jersey (other than a share of sales receipts as set out above). Instead the new landlord would pay a purchase price to States of Jersey. In this appraisal the purchase price has been estimated based on the tenanted market value approach, as used in stock transfers in the UK
- ✚ This approach would result in additional costs estimated at:
 - ✚ Purchasing the pension debt from States of Jersey of £2,135k
 - ✚ Setting up costs for transferring staff, establishing the Board and the operating framework and communications with the tenants of £1,312k
 - ✚ Enhanced governance of £370k
 - ✚ Central support costs of £1m
 - ✚ An allowance for the regulator of £120k

Appendix D External factors that might influence income stream

Section 3.5.3.3 deals with the assessment question “What are the external factors that might influence the income stream?” This appendix summarises the risk assessment for each option against each of the risks identified in section 3.5.3.3.

Option 1 – Status Quo

| External factor | Potential impact | Likelihood |
|---|------------------|---|
| Increases in cost of finance | None | Low - no finance provided |
| Additional costs caused by delays in delivery of investment | High | High, as the business model cannot afford to deliver both the investment and income stream required |
| External restrictions on achieving efficiencies | Medium | Medium, where efficiencies are requested from other States departments. The income stream projections don't assume efficiencies |
| Changes to social rent policy | High | Low, Status Quo assumption is no change |
| Lower sales of properties than forecast | Medium | Low, prudent view of potential sales taken, so variations are more likely to be beneficial. Affects options 1 to 6 equally |
| Market value of properties sold falls | Medium | Medium, as current estimates of market value taken and prices could fall in the short term. Affects options 1 to 6 equally |
| Income stream risk rating | | Medium |

Option 2 – States Department (with internal borrowing)

| External factor | Potential impact | Likelihood |
|---|------------------|---|
| Increases in cost of finance | Medium | Medium – could rise if costs to States of Jersey increase, or there is competition for funds from other States departments |
| Additional costs caused by delays in delivery of investment | High | High, as the business model cannot afford to deliver both the investment and income stream required |
| External restrictions on achieving efficiencies | Medium | Medium, where efficiencies are requested from other States departments. The income stream projections don't assume efficiencies |
| Changes to social rent policy | High | Low, would affect options 2 to 7 equally |
| Lower sales of properties than forecast | Low | Low, prudent view of potential sales taken, so variations are more likely to be beneficial. Affects options 1 to 6 equally |
| Market value of properties sold falls | Medium | Medium, as current estimates of market value taken and prices could fall in the short term. Affects options 1 to 6 equally |
| Income stream risk rating | | Medium |

Option 3 – ALMO

| External factor | Potential impact | Likelihood |
|---|------------------|---|
| Increases in cost of finance | Medium | Medium – could rise if costs to States of Jersey increase, or there is competition for funds from other States departments |
| Additional costs caused by delays in delivery of investment | High | High, as the business model cannot afford to deliver both the investment and income stream required |
| External restrictions on achieving efficiencies | Medium | Medium, where efficiencies are requested from other States departments. The income stream projections don't assume efficiencies |
| Changes to social rent policy | High | Low, would affect options 2 to 7 equally |
| Lower sales of properties than forecast | Low | Low, prudent view of potential sales taken, so variations are more likely to be beneficial. Affects options 1 to 6 equally |
| Market value of properties sold falls | Medium | Medium, as current estimates of market value taken and prices could fall in the short term. Affects options 1 to 6 equally |
| Income stream risk rating | | Medium |

Option 4 – Trading Operation

| External factor | Potential impact | Likelihood |
|---|------------------|---|
| Increases in cost of finance | Medium | Medium – prudent assumptions made, but costs of borrowing could be higher than allowed for |
| Additional costs caused by delays in delivery of investment | High | Medium – avoids the risk of States of Jersey having to ration its internal resources, but States sanction still required |
| External restrictions on achieving efficiencies | Medium | Medium, where efficiencies are requested from other States departments. The income stream projections don't assume efficiencies |
| Changes to social rent policy | High | Low, would affect options 2 to 7 equally |
| Lower sales of properties than forecast | Low | Low, prudent view of potential sales taken, so variations are more likely to be beneficial. Affects options 1 to 6 equally |
| Market value of properties sold falls | Medium | Medium, as current estimates of market value taken and prices could fall in the short term. Affects options 1 to 6 equally |
| Income stream risk rating | | Medium |

Option 5 – Hybrid Trading Company

| External factor | Potential impact | Likelihood |
|---|------------------|---|
| Increases in cost of finance | Medium | Medium – prudent assumptions made, but costs of borrowing could be higher than allowed for |
| Additional costs caused by delays in delivery of investment | High | Low – availability of resources not affected by States of Jersey decisions |
| External restrictions on achieving efficiencies | Medium | Medium, where efficiencies are requested from other States departments. The income stream projections don't assume efficiencies |
| Changes to social rent policy | High | Low, would affect options 2 to 7 equally |
| Lower sales of properties than forecast | Low | Low, prudent view of potential sales taken, so variations are more likely to be beneficial. Affects options 1 to 6 equally |
| Market value of properties sold falls | Medium | Medium, as current estimates of market value taken and prices could fall in the short term. Affects options 1 to 6 equally |
| Income stream risk rating | | Low to medium |

Option 6 – Transfer to a States of Jersey wholly owned Housing Company

| External factor | Potential impact | Likelihood |
|---|------------------|---|
| Increases in cost of finance | Medium | Medium – prudent assumptions made, but costs of borrowing could be higher than allowed for |
| Additional costs caused by delays in delivery of investment | High | Low – availability of resources not affected by States of Jersey decisions |
| External restrictions on achieving efficiencies | Medium | Medium, where efficiencies are requested from other States departments. The income stream projections don't assume efficiencies |
| Changes to social rent policy | High | Low, would affect options 2 to 7 equally |
| Lower sales of properties than forecast | Low | Low, prudent view of potential sales taken, so variations are more likely to be beneficial. Affects options 1 to 6 equally |
| Market value of properties sold falls | Medium | Medium, as current estimates of market value taken and prices could fall in the short term. Affects options 1 to 6 equally |
| Income stream risk rating | | Mostly Low |

Option 7 – Sale of freehold to a new social landlord

| External factor | Potential impact | Likelihood |
|---|------------------|--|
| Increases in cost of finance | High | Medium to high – prudent assumptions made, but any increases in the cost of borrowing would have a significant impact on the business model due to the high level of borrowing required for the initial purchase of social housing stock |
| Additional costs caused by delays in delivery of investment | High | Low – availability of resources not affected by States of Jersey decisions |
| External restrictions on achieving efficiencies | Medium | Low, as surpluses retained |
| Changes to social rent policy | High | Low, would affect options 2 to 7 equally |
| Lower sales of properties than forecast | Low | Low – Landlord compensated for net income foregone of properties sold, balance accrues to States of Jersey, prudent view of sales taken |
| Market value of properties sold falls | Medium | Low – Landlord compensated for net income foregone of properties sold, balance accrues to States of Jersey, prudent view of sales taken |
| Income stream risk rating | | Low to medium |

Appendix E Commercial risk allocation matrix

| Ref | Risk Description | States of Jersey | Company | Shared |
|-----|---|------------------|---------|--------|
| P1 | Policy requirement change | X | | |
| P2 | Rent policy change | X | | |
| P3 | Increase in Decent Homes Standard | X | | |
| E1 | Inflationary change | | X | |
| E2 | Interest rate change | | X | |
| E3 | Business rate change | X | | |
| E4 | Business Taxation change | X | | |
| E5 | GST change | X | | |
| E6 | Utility cost change | | | X |
| E7 | Housing price change | | | X |
| E8 | Rental market change | | | X |
| E9 | Demand change for Social Housing | | | X |
| E10 | Unexpected impact on Income Support | X | | |
| E11 | Extra cost of Income Support for Private Rented sector not off-set by HA return | X | | |
| E12 | Housing Trusts not managing the transition to the new rents effectively | X | | |
| E13 | States and HA not managing the transition to new rents effectively | | | X |
| S1 | Demographics of Tenants change | X | | |
| S2 | Age profile of Tenants change | X | | |
| S3 | Resistance to/difficulties with means testing for transitional relief | X | | |
| T1 | Building control standards change | X | | |
| T2 | Unexpected stock condition costs | | | X |
| L1 | Regulatory cost change | X | | |
| L2 | (Initial) difficulties with Regulator/SHU interface | X | | |
| L3 | Requirement for regulatory intervention | | X | |
| L4 | General change in Law | X | | |
| L5 | Discriminatory change in law | X | | |
| L6 | Call on funders' guarantee (if given) | X | | |
| L7 | Annual return covenant not complied with | | X | |
| L8 | Internal loan (i.e. investment) repayments not honoured | | X | |
| L9 | Breach of HA covenants | | X | |
| L10 | Difficulty in getting external loan on acceptable terms | | X | |
| L11 | Challenge to contractual tenancy regime | | X | |
| L12 | Prospective board of HA does not accept proposed obligations | | X | |
| L13 | Title defects | | | X |
| L14 | Difficulties with third party contracts | | X | |
| L15 | Problems with continued 'support' service provision by States, including deferred 'TUPE'? | | X | |
| L16 | Increase in pensions deficit | | X | |
| L17 | States fails to pay expected Income Support | X | | |

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| Ref | Risk Description | States of Jersey | Company | Shared |
|-----|---|------------------|---------|--------|
| L18 | Poor HA Governance | | X | |
| L19 | Misuse of land | | X | |
| L20 | Third party claims at point of transfer | | | X |
| L21 | Difficulties with complex interface between Treasury, Social Security, Chief Minister's (SHU), Planning and other departments | X | | |
| EN1 | Unforeseen liabilities arising from site transfer | | | X |
| EN2 | Unanticipated asbestos liability | | | X |
| O1 | Construction risk | | X | |
| O2 | Asset maintenance cost risk | | X | |
| O3 | Transferring staff performance | | X | |
| O4 | Rent arrears increase | | X | |
| O5 | Gateway system fails | X | | |
| O6 | Replacement IT system fails | | X | |
| O7 | HA's need to find set up costs from efficiencies in first 5 years | | X | |
| O8 | HA's failure to achieve required sales receipts | | X | |

Appendix F Staff structure

