

**PORTFOLIO SALE OF SITES**

*To:* **Commercial & Investment Committee**

*Meeting Date:* **15 December 2017**

*From:* **Chris Malyon, Deputy Chief Executive**

*Electoral division(s):* **All**

*Forward Plan ref:* **N/a** *Key decision:* **No**

*Purpose:* **To consider the sale of a number of land and property assets to the Council's wholly owned development company (Cambridgeshire Housing and Investment Company) in a single sale process, known as the 'portfolio'.**

*Recommendation:* **It is recommended that the Committee agree:**

**a) To authorise a loan facility to Cambridgeshire Housing and Investment Company for up to £120,000,000 for land acquisition, construction and associated costs.**

**b) Delegate the negotiation of the final terms of the sale and loan agreement to the deputy section 151 officer in consultation with the Chairman of the Committee, including the repayment and interest charging arrangements**

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## 1. BACKGROUND

- 1.1 The Council has established a wholly owned housing company to develop on land primarily owned by the Council in order to derive a financial return. The underlying objective of creating a commercial vehicle of this nature is provide new revenue sources to support the delivery of front line services to Cambridgeshire residents. Commercial & Investment Committee have been considering a pipeline of development opportunities since the establishment of the company in 2016.
- 1.2 The financial model that the Committee have previously agreed should be adopted is that the Council will make loans to Cambridgeshire Housing Investment Company (CHIC) at commercial rates in order to provide the funding to allow CHIC to purchase land from the Council and to finance the costs of construction. As the Council can borrow at less than commercial rates it will derive a financial margin on the loans. This margin has already been included as a revenue benefit within the Council's budget. The Council will receive capital receipts and eventually the Council will also receive dividends from the Company but this will not arise for a number of years given the debt ratios of the Company in the early years of trading.
- 1.3 Unfortunately progress on the sale of sites to CHIC has been slower than originally anticipated resulting in a net revenue shortfall: £750k in the current financial year, which has been forecast within the published monitoring reports throughout the Autumn. In the following years the anticipated net income in interest receivable from CHIC is:

2018/19	£4,346k
2019/20	£5,850k

- 1.4 Given the progress on getting sites transferred to CHIC and the consequential impact this is having on the Council's budget the Managing Director of CHIC outlined a "portfolio sale" approach at a workshop with Members on 20<sup>th</sup> October. This approach would be to bring forward a large proportion of the total pipeline in a single sale (the portfolio) within the current financial year, and secure the significant income expectations associated with the loans going into next year.

## 2. MAIN ISSUES

- 2.1 The Council is, by law, required to achieve best value in the disposal of any asset – even if this is to a company wholly owned by the Council. The Council also needs to ensure that any loan to the company reflects the value of the asset upon which the loan is made.
- 2.2 The portfolio approach would bring forward the proposed sales for 2017/18 and 2018/19 in to a single process. Values are currently being commissioned and will undertake RICS 'Red Book' valuations on all the sites within the portfolio.
- 2.3 If this approach is agreed CHIC will acquire a number of sites without planning approval. The Red Book valuations would therefore be based on current use which will include an element of hope value to reflect the potential uplift if planning consent is obtained. The more certainty of planning approval the higher the hope value will be. The main uplift in value will occur when planning is obtained and the Council will aim to recover this through the use of overage clauses. It is important for both the Council and CHIC to ensure that this

process is both a robust and transparent to ensure that best value is demonstrably achieved. In this way the Council will ensure that its policy that all surplus land and property should be disposed of at 'best consideration', to meet the requirements of s.123 of the Local Government Act 1972 will be adhered to.

- 2.4 CHIC and the County Council have sought legal advice from the solicitors Bevan Brittain LLP about a number of areas surrounding the portfolio sale approach. Bevan's advice was that the best approach to maintain an arm's length relationship, which is important to avoid state aid and procurement issues, is to sell at market value. In reality however the only way to be able to demonstrate market value is sell sites on the open market. Therefore any process other than that will be based on an opinion.
- 2.5 Quotations for carrying out independent valuations are due to be returned by 8<sup>th</sup> December and the work will take around 2 months in total. Valuations will vary in complexity. Those that are straightforward will be carried out first allowing solicitors to be instructed and the sale process to begin as soon as possible. Sales will be completed concurrently with loans being made before the end of March 2018. Specialist advice will be sought on overage clauses.
- 2.6 Valuations on two sites have already been undertaken and a third is imminent and they are now ready to be sold to CHIC:

Site	Units	Valuation
Russell Street, Cambridge	6	£970,000
Queens Street, March	22	£840,000
Milton Rd Library	7 and a library	Awaited.

### 3.0 LOANS AND FINANCING

- 3.1 The original business case for CHIC, as seen by the then Assets and Investment Committee in May 2016, sets out:
- the intention to create a revenue stream from housing development in preference to receiving one-off capital receipts from sale of surplus sites
  - the significant time lag from the point at which sites are identified until the point at which a revenue stream is created
- 3.2 To address the time lag, the business case envisaged that CCC would benefit from a revenue stream much earlier by establishing market loan(s) to CHIC. The Council can borrow at very competitive rates from the Public Works Loan Board, whereas any loans from the Council to CHIC must be at market rate. The difference is retained by the Council, and supports the Council's overall financial position from a relatively early stage in CHIC's development.
- 3.3 The major land acquisitions from the Council by CHIC, this financial year, entail a significant loan financing requirement. Once loan(s) are in place, interest is payable to the Council. As explained above it will not be known exactly what the value of land transfers, and corresponding loans, will be as these are contingent on an external valuation process, however it is expected that the maximum level of loan connected to the portfolio sale will be £120million.

- 3.4 Recommendation (b) in this report will enable the Council to negotiate and agree the detailed terms and timing of the loans related to the portfolio sale. The Council has received and is considering technical advice on a number of issues related to the loan(s), including those set out below.
- 3.5 As well as loan financing, the Council considers that it will be necessary to provide around 5% of the capital funding to CHIC by way of equity investment (i.e. a contribution into the business that is not a loan by the Council as the shareholder). From a taxation perspective, for CHIC, HMRC are unlikely to accept debt-only financing as interest paid is tax deductible for a company.
- 3.6 By its nature equity is “unsecured.” That is to say it is provided to CHIC without absolute guarantee or insurance of performance by the company. It is likely the loan arrangements to CHIC will also involve a degree of unsecured debt (debt without a legal charge on land in case of default) because the company will require construction loans before it can begin building homes (and creating assets). The Council is furthering its investment function by acting in this way. It is assessed that in order to maximise the financial reward from housing investment in Cambridgeshire, the risk is best retained, and mitigated, within a Council owned structure, through CHIC as a wholly owned limited company.
- 3.7 State aid rules prohibit the Council from providing selective financial subsidies to CHIC. Firstly, this is a consideration in relation to the land disposals, however it is anticipated that the market economy operator principle (MEOP) of state aid will be satisfied by the valuation mechanisms to achieve best consideration set out in section 2.4. This means CHIC will not be purchasing the sites on non-commercial terms.
- 3.8 Secondly, in setting the interest rates for lending to CHIC, the Council will need to comply with published reference rates, which vary according to the level of security and credit history of the loan recipient. Providing loans at market value further confirms that CHIC’s operations are “commercial in character” – an important determinant of the procurement regime relevant to the company.
- 3.9 Based on updated modelling and estimates received from CHIC and reviewed by the Council, it is anticipated that a loan facility of up to £120m will be required this financial year. The Council will receive payment from CHIC (using part of the loan) for land transferred as a capital receipt.

#### **4.0 GOVERNANCE**

- 4.1 Once sites are sold governance will be through the Council’s rights as shareholders and through the shareholder representatives that sit on the Board of Directors of the Company.
- 4.2 Given the legal advice that the Council has received it is necessary to maintain an arm’s length relationship with CHIC. As shareholder however the level, and frequency of, reporting will be different from that the Committee has been used to. However the Committee is, to a large extent, able to shape the nature of the reporting that it requires. .
- 4.3 A key issue for Council Members will be that the nature of the relationship with the programme will be different that if sites were being developed directly by the Council. Whilst

we anticipate that the level of engagement will be maintained local member's ability to influence CHIC will be limited.

## **5. ALIGNMENT WITH CORPORATE PRIORITIES**

### **5.1 Developing the local economy for the benefit of all**

Sites developed across the county will undoubtedly contribute to the local economy creating additional jobs in the house building industry. In turn those employed in the industry will create secondary spend in the localities where they work and live.

### **5.2 Helping people live healthy and independent lives**

There are no significant implications for this priority.

### **5.3 Supporting and protecting vulnerable people**

There are no significant implications for this priority.

## **6. SIGNIFICANT IMPLICATIONS**

### **6.1 Resource Implications**

The sale of assets to CHIC are included within the Council's Business Plan. Delays to the original profile of sales is causing an in year pressure and this has already been report to GPC within the IRPR. This reports seeks to ensure that the sale of sites takes place within a portfolio sale within the current financial year thereby mitigating further capital and revenue implications. These are highlighted in the report.

### **6.2 Procurement/Contractual/Council Contract Procedure Rules Implications**

Bevan Britain have advised on procurement, best consideration, lending and security, accelerating implementation and State Aid.

A procurement exercise is currently in hand to commission independent valuers to undertake 'red book' valuations of the sites within the proposed portfolio.

### **6.3 Statutory, Legal and Risk Implications**

Specialist legal advice has been sought jointly from Bevan Brittain on procurement, best consideration, lending and security, accelerating implementation and State Aid. LGSS Law have also advised.

The legal requirement for the Council to achieve best value in the sale of its assets is set out in the report. In addition the legal requirement for the wholly owned commercial company to maintain independence from Council governance processes has been identified.

### **6.4 Equality and Diversity Implications**

There are no significant implications within this category.

### **6.5 Engagement and Communications Implications**

There are no significant implications within this category.

### **6.6 Localism and Local Member Involvement**

Officers will work with CHIC to ensure the protocol of local Member engagement on individual sites is maintained as part of the Company's modus operandi.

## 6.7 Public Health Implications

There are no significant implications within this category.

Implications	Officer Clearance
Have the resource implications been cleared by Finance?	Yes Chris Malyon
Have the procurement/contractual/ Council Contract Procedure Rules implications been cleared by the LGSS Head of Procurement?	Yes Paul White
Has the impact on statutory, legal and risk implications been cleared by LGSS Law?	Yes. Fiona McMillan
Have the equality and diversity implications been cleared by your Service Contact?	Yes John Macmillan
Have any engagement and communication implications been cleared by Communications?	Yes Christine Birchall
Have any localism and Local Member involvement issues been cleared by your Service Contact?	Yes John Macmillan
Have any Public Health implications been cleared by Public Health	Yes Tess Campbell

## 7. SOURCE DOCUMENTS

Source Documents	Location
None	