



To: Leader of the Council
Report by: Alan Carter
Relevant scrutiny committee: Strategy and Resources Committee 4 July 2016
Wards affected: All

Investment Partnership

Key Decision

1. Executive summary

The report recommends the establishment of an Investment Partnership as the best way for the Council to secure its objectives from the redevelopment of many of its sites.

2. Recommendations

The Executive Councillor is recommended:

- 2.1 To delegate authority to a Strategic Director to set up an Investment Partnership subject to legal due diligence and following consultation with the Leader and Opposition Spokespersons.

3. Background

3.1 Following consideration of a report by the Strategy and Resources Committee on 18 January 2016, the Executive Councillor has agreed to the establishment of a General Fund Development Programme to optimise the use of its land and property assets. The report also examined different options for the Council to secure the redevelopment of its land, from selling sites through to the Council acting as developer. Through these reports the Council has set out which sites in its ownership the Council wishes to progress for redevelopment over the short to medium term and;

- that the financial priority is to secure a revenue income as opposed to a capital receipt;

- that the sites can and should primarily be redeveloped for housing that is affordable, addressing the local need for more social housing and other forms of sub-market housing (intermediate housing)
- that the Council is prepared to take more of a share of development risk to secure a greater share of financial and/or social reward.

3.2 It is obviously important too that revenue income is secured as quickly, and as cost-effectively, as possible in view of the wider financial pressures on the Council. A redevelopment scheme can on average take around three years to complete. Finally, despite the current hiatus surrounding the sustainability of the Housing Revenue Account (HRA), there are some HRA sites that have been approved for redevelopment and it would be sensible to consider their redevelopment alongside any approach to the redevelopment of General Fund sites.

3.3 Analysis over the last few months including financial appraisals in respect of the Park Street project and the Council's Housing Company and the appetite of the Council to accept more development risk has led to the consideration of joint venture partnerships to redevelop sites rather than contract based partnerships for works and services. The latter are less sensitive to changing market circumstances and therefore less able to capture up-lifts in value from redevelopment.

3.4 Senior officers from housing; property; legal and finance services have been investigating different forms of joint venture partnerships including running a workshop which involved presentations from an external property consultant; two prominent local developers and from a local authority that has set up a joint venture partnership. Informal soundings have been taken from legal and property advisers and local authorities who have established joint ventures and some of their committee reports in the public domain have been read. Reports have been considered by the Strategic Leadership Team and the conclusion is that a form of joint venture partnership known as an Investment Partnership (IP) is a model that would be the best approach for the Council to secure its objectives from the redevelopment of many of its sites. All other joint venture models explored require the Council to identify the value of the site or programme of sites in advance of procuring a partner to provide works and services. The IP allows for greater flexibility and control by the Council in that it can choose which sites it wishes to take forward through the IP and which sites may lend themselves to different approaches. As the Council is not procuring works and services the establishment of a IP is not deemed to be a procurement.

3.5 In summary, the strengths of the IP model for the Council are as follows;

- Risk and reward is shared with the Council's partner.

- The Council can choose which schemes it inputs into the model and when – it can therefore control the extent of the risk and reward it chooses to take on a scheme by scheme basis.
- The Council can choose the financial (ie capital or revenue or both) and social outputs it requires from a scheme.
- The Council can choose to veto a scheme before it proceeds.
- The IP can be set up quickly and is therefore the best route to progress schemes such as Mill Road and Park Street Car Park.
- Set up costs are low and there are no procurement costs for the Council.

Overview of how an Investment Partnership works

3.6 The Council would agree to set up a joint venture with a partner as a Limited Liability Partnership (LLP). The LLP would be 50:50 controlled by the Council and the partner. Therefore, it would not be a public sector body. The Council invests its land with the IP and the partner invests funding and its knowledge, skills and experience in development. These inputs are valued (eg the Council's land is independently valued) and land can be input on a site by site basis. Once land is input the IP appraises the scheme. The Council and partner approves the scheme and it is developed. Once complete the Council and the partner will share the outputs (financial or social) in proportion to the value of each partners inputs, in other words this model allows the sharing of the development risks and reward between the Council and its partner.

3.7 Under the model the Council can choose which scheme it wishes to invest in the IP. The Council or the partner can veto whether a scheme proceeds or not once it has been appraised. The Council retains control of the freehold of land and its value as it can choose or not whether it requires the freehold to remain with the Council. The Council can offer funding (and staff) as an investment into the IP too.

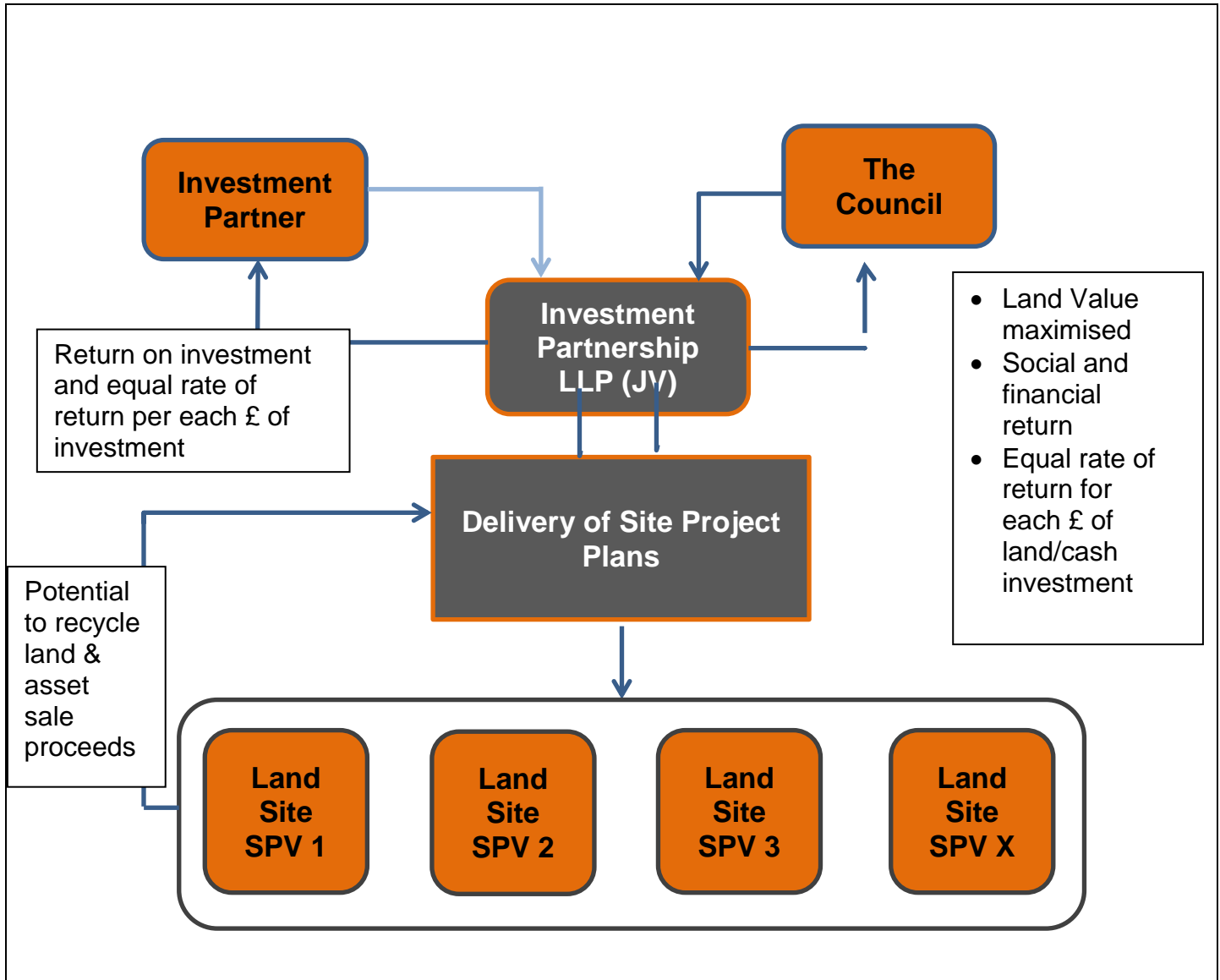
Governance and Structure

3.8 The IP would be overseen by a Board made up of equal representation from the Council and the partner. As an example, an existing IP set up by another local authority has a Board of four – two representatives from the Council and two from its partner. Each Board Member has a single vote. For avoidance of doubt decision-making is on the basis of consensus, this means that if there is not agreement between the parties (or a majority vote – although it is difficult to imagine the circumstances in which one parties representative votes in favour of a proposal and the other votes against), or there are abstentions, then nothing happens. The Chair does not have a casting vote.

3.9 If the establishment of an IP is approved, a process to agree Council representation would need to be agreed.

3.10 The requirements of the Council and the partner as the shareholders would be set out in a shareholder agreement.

3.11 The diagram below summarises the structure of an IP with a partner.



3.12 The IP would be serviced by a small project team that can include Council staff.

3.13 Once a scheme has been appraised and approved by the Council and the partner and the Board, a separate special purpose vehicle (SPV) would be set up to manage the delivery of the scheme (more than one scheme can be delivered through a single SPV if they are small sites). The purpose of setting up the SPVs is to contain any development risks relating to a scheme and to provide transparency in the outputs flowing from the delivery of different schemes bearing in mind that they, of course, will be completed at different times.

Selecting a Partner

- 3.14 Learning from the experience of other local authorities in establishing an IP it is important from the outset to define what the Council is trying to achieve through the model. The proposed purpose and objectives for the IP are set out in Appendix 1.
- 3.15 Senior officers have also been reflecting on the qualities that Cambridge City Council would expect from a partner to an IP. These are set out in Appendix 2 – What does Cambridge City Council want from a partner in an IP.
- 3.16 The establishment of an IP is not subject to public sector procurement rules. Nevertheless the Council will need to be transparent about why it has chosen its partner against the above criteria. A selection methodology has been devised that involves assessment by external parties and a wide range of internal officers. The assessment process would also involve the usual due diligence checks in respect of finance and probity. The selection methodology is shown as Appendix 3.

Legal Matters

- 3.17 The Council has commissioned Freeths following a mini-competition using the EM Lawshare framework. Freeths will provide advice at two stages. Initially they will provide advice on;
- The Council's powers to enter into the proposed arrangement;
 - Any procurement implications involved in the selection of a partner;
 - Any procurement implications in entering into agreement with the partner to develop specific sites, including in circumstances in which the Council would benefit through the delivery of public works;
 - Good practice considerations more generally in selecting a partner;
 - Advice on the methodology of selection;
 - Any state aid implications;
 - Tax implications about what is proposed;
 - Advice generally on the proposed model, including consideration of whether this is the best option.

Should approval be given to proceed, Freeths will act on behalf of the Council to set up the joint venture structure.

Risks

- 3.18 The IP model does not remove any of the usual risks associate with development. For example; site related risks such as contamination;

risks around achievement of planning approval; build cost inflation etc. The IP does allow these risks to be shared with the partner and to be effectively mitigated with the Council benefiting from the development skills, experience, knowledge and staff capacity of the partner.

3.19 In terms of direct risks with the IP model these are as follows;

Legal challenge about the choice of the partner - Freeths advice will confirm but all case studies and secondary legal commentary clearly indicate that a local authority can choose its partner in an IP.

Transparency in that choice – The selection methodology is offered to demonstrate why the Council chose its partner.

That the return generated through the IP does not represent best value – Land invested by the Council into the IP will be valued by an independent valuer. At any time the Council can require the IP to test best value of any of its activities. As the partner is set to share in up-lift in development value it is not in their interest not to work with the Council to jointly manage the efficient delivery of projects.

The Council and its partner does not agree to progress a scheme – The impact of this risk is that the cost of progressing the scheme to-date would be lost and there would be a delay in delivering the scheme. Again, part of the mitigation is that it is not in the interest of either partner to without good reason prevent a scheme from progressing, as any aborted costs would be shared. The Council can of course decide not to invest further sites in the IP if relationships deteriorate.

4. Implications

(a) Financial Implications

Land Value - As mentioned above the Council would invest land into the IP. The land would be independently valued at the point of input and the Council will be issued a 'loan note' to the value of the land. This would therefore satisfy the statutory requirement for the Council to 'dispose' of the land at best value. Once the land has been developed the IP will redeem the loan note from the develop value.

Any other development value above the value of the Council's land at input will be shared between the Council and the partner in proportion to the value of other inputs ie funding and staff costs. In the simplest example if the Council inputs land to the value of £1m and the partner inputs funding and staff costs to the value of £1m and the resulting

value of the new development is £2.4m, the Council will receive 50% of the up-lift in value ie £200,000 as will the partner.

Revenue Return – The Council will be able to require a revenue return as a return on the development value. For example, it can specify that some of the housing will be let at Intermediate Rents and forego any capital receipt should these properties have been sold.

Funding – The Council can choose to provide funding as part of its investment into the IP. It may want to do so if for example it can secure finance at better value than the partner. This would be analysed at scheme appraisal stage and be part of the decision to proceed with a schemes or not.

Reinvesting Returns in the IP – The model would allow the Council to instruct that the IP retain some of the return on a scheme should it be helpful for the IP to have working capital to progress subsequent schemes.

Financial Capacity of Partner – The usual checks of financial capacity and current exposure of a partner would be undertaken as part of the due diligence before setting up an IP.

Corporation Tax – This is not payable by a LLP.

SDLT – Any SDLT liability will be assessed on a scheme by scheme basis.

(b) **Staffing Implications**

Council staff experienced in the development process will be required to act on its behalf to set up the IP and also to manage its interests as sites are input into the IP. This will be led by the Council's shared housing development service the Greater Cambridge Housing Development Agency (H DA).

(c) **Equality and Poverty Implications**

There are no direct equality and poverty implications in establishing an IP, but the redevelopment of individual sites and the effective realisation of the Council's land and property assets will release funding to assist the Council to pursue its equality and poverty policies.

(d) **Environmental Implications**

There are no direct environmental implications in establishing an IP but there will be a specification for each redevelopment that addresses ten required environmental outcomes.

(e) **Procurement**

Initial advice is that the establishment of an IP does not constitute a procurement. Part of Freeths commission is to specifically address this matter.

(f) **Consultation and communication**

There has been no formal external consultation regarding the establishment of an IP.

(g) **Community Safety**

There are no direct Community Safety implications in establishing and IP.

5. Background papers

No background papers were used in the preparation of this report.

6. Appendices

Appendix 1 – Proposed Purpose and Objectives of an Investment Partnership

Appendix 2 - What does Cambridge City Council want from a partner in an IP.

Appendix 3 - Selection of Investment Partner : Methodology

7. Inspection of papers

To inspect the background papers or if you have a query on the report please contact:

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Appendix 1 - Proposed Purpose and Objectives of an Investment Partnership

Purpose

- To provide housing that is affordable to meet local need
- To create successful places

What do we want to achieve (outcomes and outputs)?

- Primarily housing and a range of housing that is affordable including social housing.
- A revenue return for the Council is priority over a capital receipt - but with the flexibility for the Council decide on a scheme by scheme basis.
- A programme approach to deliver the 'double bottom line' of housing that is affordable and a revenue return ie flexibility to look at outcomes over a number of schemes over one, three and five year timescale and potentially longer.
- Sharing risk and return with an investment partner.
- Speedy and timely delivery.
- Developments that create successful places
- Retention of freehold as a priority.

Appendix 2 - What does Cambridge City Council want from a partner in an IP.

The following list is proposed;

A. Alignment with the Council's Vision for Cambridge

- Commitment to the Council's vision for Cambridge ie ".....a united city, 'One Cambridge - Fair for All', in which economic dynamism and prosperity are combined with social justice and equality" (Extract from Cambridge City Council – Our Vision).
- A commitment to quality built form and 'place' design –

"A city which strives to ensure that all local households can secure a suitable, affordable local home, close to jobs and neighbourhood facilities."

"A city which draws inspiration from its unique qualities and environment and its iconic historic centre, and retains its sense of place across the city through positive planning, generous urban open spaces and well-designed buildings, and by providing quality council services."

"A city where getting around is primarily by public transport, bike and on foot."

"A city that takes robust action to tackle the local and global threat of Climate Change, both internally and in partnership with local organisations and residents, and to minimise its environmental impact by cutting carbon, waste and pollution."

(Above are extracts from Cambridge City Council – Our Vision).

B. The Ability to Optimise the Future Investment in Council Land Opportunities

- An understanding of the Cambridge housing market (to optimise sales values and manage rates of sale).
- An understanding of local land supply (to facilitate land assembly) and direct experience of the local construction supply side (to balance cost, quality and timely delivery of new homes).
- The skills and experience to work with the Council to deliver all component parts of the development process ie the flexibility to work with the Council to secure the construction of schemes as well masterplan, design, secure planning and market and sell homes.
- The skills and experience to work with the Council to deliver schemes of 50 to 200 homes plus (likely to be the core purpose of

the Investment Partnership) and the flexibility and appetite to work with the Council if necessary to deliver smaller schemes with say less than ten homes.

- Flexibility to realise both the Council's financial and social outcomes from investment.

C. A lasting partnership

- The commitment to sustain a significant partnership over a medium term timescale.