



To: Executive Councillor for Strategy and Transformation
Report by: Fiona Bryant, Strategic Director
Relevant scrutiny committee: Strategy & Resources 9/10/2017
Scrutiny Committee
Wards affected: All

Cambridge Investment Partnership (CIP) Land Transactions

Key Decision

1. Executive summary

- 1.1 In July 2016 Strategy and Resources approved the setting up of the Cambridge Investment Partnership (CIP) which was subsequently established in January 2017.
- 1.2 The use of the CIP in managing property development enhances the Council's capability for delivery of affordable housing and makes the best use of its community assets to provide for the future of Cambridge and its residents. Further information on the CIP establishment and objectives are provided in section 3 of this report.
- 1.3 The report is structured in sections which set out the considerations, options and recommendations for land disposals between the Council and the CIP for General Fund land and Housing Revenue Account land. The Council's decision making process is also set out.
- 1.4 The reasons for the Council's decision to explore the establishment of an Investment Partnership and the process by which Hill Investment Partnership Ltd (HIP) was selected as the investment partner are set out in sections 3. This section also provides an explanation of the benefits the Council will derive from utilising an Investment Partnership route as the mechanism for land development; and an outline of the processes, procedures and governance framework within which the business of the CIP will be conducted.
- 1.5 Section 4 of the report considers the complex legal and financial considerations which relate to the disposal of General Fund land

and internal transfers of land between the General Fund and the HRA. The preferred options for transfer of the land parcels to CIP for development are set out in section 5. Section 6 reflects specific legally enforceable requirements relating to the land disposal in the context of the CIP development and delivery partnership model. Consideration is given to the requirement for payment of Stamp Duty Land Tax (SDLT) and for VAT in Section 7.

- 1.6 In section 8 options are proposed for calculating the payment which will be made to CIP by the Council for social housing delivered on sites developed by CIP.
- 1.7 Section 9 of the report sets out how decisions will be taken through the council's decision making process to the point of land disposal. Further details are provided in the diagram at Appendix 1 which demonstrates the process and decision flow.

2. Recommendations

The Leader is recommended:

1. To approve use of the preferred land disposal routes from the Council to CIP as set out in section 5.
2. To note the considerations relating to the approach to the transfer of land between the General Fund and the Housing Revenue Account as set out in sub section 4.3
3. To note the considerations arising from the Stamp Duty Land Tax (SDLT) and VAT obligations in section 7.
4. To approve the approach for the payment by the HRA to CIP for social rented housing as set out in 8.
5. To delegate a decision to the Exec Cllr for Finance and Resources, Exec Cllr for Housing or Leader (as appropriate) in conjunction with the relevant Strategic Director for the final approval of a Strategic Development Brief and Proposed Land Transfer / Disposal Model to CIP for individual sites. Major sites will be reviewed at a Scrutiny Committee prior to the Executive Councillor decision to transfer the land to CIP.

3. Background

- 3.1 At the Strategy and Resources Scrutiny Committee in January 2016 the Executive Councillor for Finance and Resources approved the General Fund Development Programme. The Development Programme sets out a 10 year programme of potential development and investment opportunities for General Fund (GF) sites. It also

identifies options which can be considered by the Council for the development of its land, including options for the Council to develop the land directly or by working with development partners.

- 3.2 A paper was taken to the Strategy and Resources Committee on the 4th July 2016 with a recommendation sought from the Executive Councillor as follows: “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 Spokesperson.” The paper set out the details of how an Investment Partnership works and provided details of the governance arrangements, legal and financial considerations and the potential benefits to be derived from establishing an Investment Partnership.
- 3.3 The Leader approved setting up an Investment Partnership to optimise the use of the Council’s property through investment in commercial, residential and other uses to achieve both social and financial returns. After an assessment by a panel of external consultants and internal officers from the Council, Hill Investment Partnerships (HIP) was selected from a shortlist of companies to form the Cambridge Investment Partnership (CIP) with the City Council. The Partnership is an equal, 50:50 Limited Liability Partnership (LLP).
- 3.4 This investment partnership model provides an opportunity for the Council to benefit from the experience and additional resource that a development partner can bring. Each partner shares the outputs (financial and social) in proportion to the value of its input, and therefore the model allows the partners to share the development risk and the development uplift arising from a scheme.
- 3.5 The Investment Partnership provides significant advantages to the Council in delivering individual development projects and programmes of work and thereby achieving its aim. With the alternative model of procuring a developer to build out a scheme, the developer retains all profits from uplift in value. The procurement process for individual schemes and larger programmes of delivery tends to be lengthy. The CIP model is robust in its governance and decision making processes and provides a sound model for the more accelerated development and delivery of its Council partner’s assets.

3.6 How the CIP works

The principle of the Members’ Agreement underpinning the partnership is that both partners will share any investment upside and risk equally (or as may be agreed). This potential added value is

calculated after adjustments have been made for the payment of land value, consultants and associated professional fees, site/running costs and business overheads. The partnership is a deadlock partnership, the terms of which allow either partner to exercise its powers under the deadlock to veto any proposals for development of a site. Accordingly the Council is able to veto a scheme that would prejudice the best interests of the Council in the stewardship of its assets and in delivering its strategic and corporate objectives. In circumstances where a deadlock was reached, the veto would provide for the transfer of the land from CIP back to the Council.

3.7 The agreed objectives of CIP as set out in the Members Agreement are:

- Investment in the development of land to create successful new places that meet both the financial objectives (primarily a revenue return) and social objectives of the Cambridge City Council (particularly housing that is affordable and is needed locally), provided always that the individual sites may be developed to meet either financial or social objectives;
- Improve the use of Council assets and those of other Public Sector Bodies in the Cambridge, or Cambridge wide, area;
- Maximise financial return through enhanced asset value, (with reference to the first bullet above)
- Provide a return to the Investment Partners commensurate to their investment and the level of risk in respect to such investment.

3.8 The business of CIP is conducted in accordance with the governance processes and procedures which are set out in the Members Agreement. Cambridge City Council is represented on the CIP Board by Executive Councillor for Finance and Resources and the Executive Councillor for Housing, Hills Investment Partnership is represented by two Directors of Hill Investment Partnership.

3.9 During the period of establishing the CIP, the Council secured £70m Devolution Grant to provide 500 social rented housing units. The completed units will sit within the Housing Revenue Account. The CIP is a potential delivery vehicle for delivery of sites in this programme, alongside other delivery mechanisms.

3.10 In developing sites through CIP, the Council will be transferring land to the Partnership. The rest of this report explores the considerations for the Council in agreeing to land transfer for both General Fund land and Housing Revenue Account land.

4. Considerations arising on Land Transfers

4.1 This section sets out the considerations relating to land transfer for GF land and HRA land, each of which are subject to a different set of regulations.

4.2 Considerations on General Fund land transfers

4.2.1 General Fund (GF) land must be disposed of for best (market) value, to comply with Section 123 of the Local Government Act 1972. If land were transferred at under value this could be deemed to be State Aid. Disposal at less than best value and with a value reduction below best value of greater than £2 million requires approval from the Secretary of State. The implication of this for developing land under the CIP partnership is that land should be transferred at market value; prior to development and uplift in value.

4.2.2 If the GF site value is reduced from best value by less than £2 million then the Council can decide to dispose of the site to a third party without Secretary of State approval; (subject to State Aid issues) provided the transfer meets the social, economic or environmental wellbeing criteria set out in the Local Government Act 1972. Under Section 24 and 25 of the Housing Act 1988 if the land is to be used for rental properties the transaction may require Secretary of State approval in which case a land transfer between the GF and HRA may be a preferable mechanism.

4.2.3 A GF site which delivers more than 15 units will be subject to City Council planning requirements to deliver 40% of “affordable housing”. This housing can be acquired by the HRA. On some sites the Council may wish to increase the affordable housing provision above the 40% required by planning policy. This will be considered on a site by site basis with a decision being informed by the financial viability of the scheme and the Council’s corporate and strategic objectives. A decision to increase the “affordable housing” provision above that required by planning policy may reduce the value of the land and therefore may impact on financial viability considerations.

4.3 Considerations on Transfers from the General Fund to the HRA

4.3.1 The Council accounts for its General Fund (GF) and Housing Revenue Account (HRA) separately. Assets are held in either the GF or HRA depending upon original purpose of acquisition, the historic use of the asset and / or how the asset acquisition or subsequent

expenditure was funded. Assets can be moved between the GF and HRA but such transfers need Exec Councillor Approval and will be accounted for at market value. As an internal accounting transaction, there are no actual financial costs such as Stamp Duty Land Tax; however accounting adjustments will be recorded to provide an audit trail for the transfer.

4.3.2 The most likely transfers will be a transfer of GF assets to the HRA, rather than the other way round; with the intention that the asset will be developed for social rented or affordable housing. Any transfers between the GF and the HRA will need to take account of the Local Government Capital Finance rules.

4.3.3 The value adjustment to be made is a matter for the Council to determine, but it is required to be at market value on the basis of current or intended future use. The Council will normally transfer land at intended use value. The difference between this value and the value the land is recorded at in the Council's accounts or that it could achieve if used for other purposes; will be part of the decision to transfer the land. The view of an independent valuer and the Council's external auditor will be sought on valuations where the transaction is material. Transfers to the HRA will increase the HRA's borrowing (through an accounting mechanism known as the HRA Capital Financing Requirement), which is currently capped at £230m and will therefore count against the remaining borrowing headroom which is currently at £16m. This will limit the ability of the HRA to borrow additional funding to finance the provision of additional social housing or replacement social housing.

4.4 Considerations on HRA Land Transfers

4.4.1 Restrictions are imposed on the disposal of habitable homes by the HRA to an entity in which it has an interest. The HRA is permitted to dispose of 5 or fewer habitable homes to an entity in which it has an interest. Any disposals over this number will require Secretary of State approval.

4.4.2 The Council can dispose of land that is "vacant" - this means that the site is vacant, and/or dwellings are no longer habitable and are due for demolition. Further advice will be sought on a site by site basis to clarify whether it would be preferable to transfer cleared sites to meet these requirements and to understand the risks arising from this approach. It may be appropriate to create a licence relationship to enable CIP to demolish properties prior to any site transfer.

4.4.3 HRA sites could form part of the portfolio of land being developed by the CIP. However, the Council may choose to consider alternative development options which may include developing the sites itself to assist in achieving the delivery targets for the 500 homes which are to be delivered from the Devolution Grant.

4.4.4 The HRA could sell vacant land to a third party and use the receipt to contribute to housing delivery. However, this option is not under consideration here as the report is only considering transfers in relation to the CIP.

5. Preferred Options for General Fund and HRA Land Transfers to CIP

5.1 The preferred options are set out in this section. However these options would need to be considered on a site by site basis taking into consideration the Council's broad objectives for the site. The Council can consider a mix of the options on large sites.

5.2 Proposed Option for General Fund Land Transfers to CIP

5.2.1 On the basis of legal advice for General Fund Sites of 15 units or more, (as set out in section 4.2.3 and assuming land is sold at best value), the preferred disposal option is either under a straightforward long lease or a freehold sale. Sale / purchase of land is expressly excluded from the scope of the Public Contracts Regulations and as such, as long as the Council does not impose enforceable obligations (see section 6), the disposal and re-acquisition of a site should not be regarded as a "public works contract". A long lease which does not allow for freehold sales may have an impact on sale of market housing. DCLG are reviewing the use of leasehold sale by developers and may impose restrictions in future.

5.3 Proposed option for HRA land Transfers to CIP

5.3.1 For HRA Sites where the Council has a broader objective to deliver affordable housing, the legal advice suggests that the preferred option to transfer the land to CIP is an initial Agreement for Lease (AFL), with a break clause in the related lease. The considerations noted in section 6.2, relating to GF land and the requirement not to impose enforceable conditions, also apply to HRA land. Transferring through an Agreement for Lease will have SDLT and VAT implications (explained below), therefore the recommendation is for development of HRA land through CIP to be considered as one of several development options. Other options include access to pre-existing framework agreements; new arrangements for contracts to build; and

an extension of a pilot scheme to use Cambridge City Council estates and facilities team for small sites.

5.3.2 If the Council chooses to develop an HRA site through CIP, the process will be as follows:

- The Council would first enter into an Agreement for Lease (AFL) with CIP and the grant of the Lease in connection with the AFL will be conditional on a planning approval being achieved and any other conditional requirements as appropriate.
- The AFL will contain a licence for CIP to enter the site to carry out surveys, soil investigations, usual due diligence checks as well as enabling works such as demolition as may be required.
- Once the conditional terms of the AFL are satisfied, the Council will grant the Lease as required in the AFL to CIP of, say, 125 years.
- The Lease will require CIP to build out a scheme in accordance with the planning consent that it obtained.
- The Council will have a break clause in the Lease in its favour to terminate the Lease once a development is completed and as a result Council's freehold of the land will then be unencumbered by the Lease and the completed properties will be in the freehold ownership of the Council.
- The lease will require the Council to pay a reverse premium equating to the cost of the development to be effective. The price paid for the lease will be assessed and estimated in advance of transfer and confirmed once a planning permission has been approved.
- CIP will have a requirement to cover the cash flow involved in building the housing units. This would be covered by loans made, on commercial terms via the pre-existing Loan Note arrangements, under which monies are lent to CIP by the Council and Hills to enable it to progress projects within its overall portfolio.

5.3.3 The lease will contain controls in accordance with the CIP Members' Agreement to ensure the land will revert to the Council if planning permission is not achieved, if not developed within an agreed period of time, or where the stated objectives for the site cannot be achieved.

6. Legally Enforceable Obligations

6.1 The principle behind CIP is that the Council will invest land and HIP will invest its development capacity and experience – with either party investing funding. As such transactions between the Council and CIP will be property transactions rather than works and services

transactions so long as there is not a legally enforceable obligation on CIP to deliver works. It is therefore important that the Council only approve an indicative scheme and leave CIP freedom to progress the final scheme for delivery. For this reason the timing of the transfer is important and it is recommended that any transfers to CIP are made for both GF and HRA land **before** planning permission is obtained.

- 6.2 With this in mind, the Council's interests will be safeguarded through the Council representatives on the CIP Board. This is the mechanism by which the Council will ensure the indicative scheme is deliverable within the constraints of the site, is financially viable, and meets the Council's corporate and strategic objectives.
- 6.3 In particular in regard to the valuation of sites on transfer, and the subsequent granting of planning permission it should be noted that the added value to CIP is calculated after adjustments have been made for the payment of land value, consultants and associated professional fees, site/running costs and business overheads.

7. Stamp Duty Land Tax (SDLT) and VAT in relation to land transfers

7.1 Issues for SDLT on GF land transfer

In a purchase of land arrangement there will be an SDLT liability on CIP when it purchases the site.

7.2 Issues for SDLT on the grant of the Agreement for Lease with a break clause in Lease (HRA Land).

- 7.2.1 SDLT will be payable by CIP on the grant of the lease at 50% of the market value (this is because there are special rules for a partner transferring a property in its own name to a partnership / LLP). It should be noted that there is no relief available at this point, so SDLT will actually be payable. So, for example, if the market value of the bare land is £2m, the SDLT will be £39,500 because the chargeable consideration for SDLT will be £1m (50% of the market value).

7.3 SDLT on exercise of the break clause in the lease

- 7.3.1 The exercise of a break clause (such as the one collapsing a lease once a development is completed – see 6.3) is the acquisition of a chargeable interest by the Council, so SDLT is chargeable in respect of it. This will be charged at 50% of the market value again (because of the special rules about transfers between partners and

partnerships) – the concern is the market value will be significantly higher than on the grant of the lease because it will be assessed on the completed units, so the SDLT could be much higher as well.

7.4 Section 61 Finance Act 2003 relief

This section of the Act may be applicable – it allows for exemption of SDLT in certain circumstances. For the purposes of the relief:

- the land transaction must be entered into in order to comply with a planning obligation (planning obligation is defined in s.106 or s.299A(2) of the Town and Country Planning Act 1990;
- the planning obligation must be enforceable against CIP and it must be in place against CIP before the transaction is effected, and must be capable of being enforced for example through the courts etc.
- the purchaser must be a public authority.
- the land transaction must take place within five years of the planning obligation being entered into.

7.5 VAT on Agreement for lease

The Council will need to take detailed VAT advice on any agreement for lease. Generally the sale of property is normally exempt from VAT which impacts on the Council's ability to recover the VAT on costs. It is possible to opt to tax a property to protect against this but any option to tax does not affect residential buildings. The CIP will also need to consider the VAT implications of any projects carefully.

8. Payment by the HRA to CIP for Social Rented Housing Once Units are Developed

8.1 This section sets out the approaches which could be adopted in considering the mechanism for determining the price the HRA should pay CIP for social rented housing.

- A. The market price that a Registered Provider would pay based on a planning policy compliant scheme.
- B. A fixed price negotiated with CIP.
- C. The actual build cost of the social rented housing.

It is recommended the Council utilises either option A or option C to agree a price with CIP for affordable housing on a site by site basis. Option B is not recommended as it takes no account of market fluctuations.

- 8.2 Where there is a planning requirement to provide affordable housing on larger General Fund sites then the HRA will negotiate a price based on the market price that a registered provider would pay. This price will be determined with reference to external advice. The Council will again share the benefit of the up-lift in value through CIP.
- 8.3 For HRA sites and smaller general fund sites which are not subject to planning requirements for the delivery of affordable housing, it is recommended that the Council should pay the actual build cost of the new homes. HRA sites are invested in CIP to deliver a social outcome and no up-lift in value is intended.
- 8.4 Underpinning these options is the requirement for the HRA to gain best value in the new build development of social housing. However, a further consideration is the need to spend Right to Buy receipts within the specified time limits to avoid returning receipts to Government with a 4% above base rate penalty.

9. Council Decision-making Processes

- 9.1 The Council's representatives on the CIP Board are the Executive Councillor for Finance and Resources and the Executive Councillor for Housing.
- 9.2 Both the Council and Hill Investment Partnerships have an equal say in the decision making and governance processes of CIP.
- 9.3 From the Council's perspective, approval of the relevant Executive Councillor or the Leader is required before land is transferred to the CIP. This will be the Executive Councillor for Finance and Resources in respect of General Fund sites and the Executive Councillor for Housing in respect of Housing Revenue Account sites. The Leader will be asked to approve reports where there are implications for both the General Fund and the Housing Revenue Account.
- 9.4 At an early stage, each site will be the subject of a report to either the Strategy and Resources Committee or the Housing Committee for approval for inclusion within a development programme. The projects will be managed through the Council's project management process up until the point of transfer to the CIP to develop out. As stated earlier in

the report, the CIP LLP is a deadlock partnership where the Council and Hill have equal representation on the Board and therefore no scheme can go ahead without both parties agreement.

- 9.5 The early stage report to committee will allow scrutiny of:
- a) The Council's high level objectives for the site
 - b) An indicative scheme for the site that meets the Council's brief
 - c) Consideration of the development options for the site and supporting analysis for a decision to recommend development through CIP
 - d) The viability of the indicative scheme.
 - e) Projected financial returns and cost implications for the Council
 - f) The agreed basis for profit sharing between the Council and HIP on completion of the scheme
 - g) The risks of the scheme for the Council and Hill Investment Partnership
 - h) A clear statement covering the intended further engagement between the partners in the event there is a significant change to the original scheme development proposal
 - i) An indicative date for the transfer of the land to CIP, the process which will be followed for ratifying a decision to transfer the land through the CIP Board governance process and a clear statement around the deadlock provisions for the site as outlined within the Members' agreement
- 9.6 Once a decision to transfer the land has been ratified by the CIP Board the Executive Councillor or Leader will approve the recommendation that the land is transferred to CIP and that CIP will progress the site to achieve a planning approval and delivery of the development. As indicated earlier in the report, major sites will be reviewed at Scrutiny Committee prior to the Exec Cllr approving the transfer. The report to the relevant Committee at this stage will include the CIP Board approval of the proposed plans, and confirmation of the strategic development brief, recommending approval for land transfer by the Exec Cllr.

When CIP was set up it was anticipated that each site would be dealt with on a site-by-site basis following, for example the content of any Option Agreement and the Council's land disposal policies. Commercially it was recognised that land would be transferred at the point that it was necessary for development in connection with the particular project. The detailed process envisages:

- The Investment Partnership Board of CIP determining that a site should be investigated with a view to it being a CIP site.
- A named site valuer is appointed.
- Contracts are exchanged.

On completion of the purchase of a site, CIP would then issue a Loan Note equivalent to the transfer price.

10. Conclusions

10.1 This report has considered the issues relating to land transfer from the Council to the CIP, and between the GF and the HRA. An important conclusion is that these need to be looked at on a site by site basis, owing to the complexity arrangements required. The Council will also seek agreement to the proposed approach on individual schemes with the external auditor.

10.2 For the GF sites, transfer to the CIP would be at market value, on a long lease or outright sale. For this transaction to be considered as an undertaking and not a contract for works the Council must be careful not to impose legally enforceable obligations.

10.3 For the HRA sites, an agreement for lease with a break clause in the lease is the recommended route. The same considerations relating to the imposition of legally enforceable conditions (noted in S11.2 above) will apply to the transaction. However since a transfer of land and consequent buyback may give rise to SDLT, and VAT, it is recommended that CIP is considered as the vehicle for the development of sites on a site by site basis alongside other development and delivery mechanisms. Value for money evaluations will need to take into account purchase price which will be paid by the HRA to CIP, (for which a methodology is proposed in section 9 of this report), together with delivery timescales and the timeframes for spending RTB receipts and other devolution funding.

10.4 The route through the Council's decision making processes up to the point of any land transfer to the CIP, where the Council has 50:50 representation on the board, are set out in Appendices 2 and 3

11 Implications

(a) **Financial Implications**

This report addresses the legal and financial implications relating to the mechanisms for optimising the development of the Council's assets and the delivery of affordable housing through the CIP. Financial implications will be identified and assessed on individual sites.

(b) **Staffing Implications**

There are no staffing implications arising from this report.

(c) **Equality and Poverty Implications**

The delivery of affordable housing is in line with the Council key objectives and therefore aligns with equality and poverty implications.

(d) **Environmental Implications**

There are no direct environmental implications arising from this report. However; the environmental targets which are required to be delivered by or achieved for each site in accordance with the Council's strategic and corporate objectives will be determined on a site by site basis

(e) **Procurement**

Provided that any specific build obligation and the making of build stage payments is avoided, the Council can acquire sites back with housing units in place in due course, without this being construed as entering into "Public Works Contracts" which would require an OJEU Procurement Process.

(e) **Community Safety Implications**

None.

(f) **Consultation and Communication Implications**

None.

(g) **Legal Implications**

The Council was supported in the set-up of CIP as an LLP by Freeths solicitors who have extensive experience of establishing and advising on similar joint venture models. Advice was sought from Savills and Trowers and Hamlin regarding provision of socially rented housing through CIP, including land transfer and procurement considerations. CIP also sought legal advice from Pinsent Masons on development arrangements for affordable

housing. In addition to the legal advice provided on the establishment of the CIP, Freeths have also provided clarification to the Council on consideration and risks relating to procurement, land transfer, internal transfers between the GF and the HRA, SDLT and VAT.

12. Background papers

These background papers were used in the preparation of this report:

- Previous reports on GF Development Programme
- Members' Agreement and other documents from the CIP
- Legal Advice from various sources

13. 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

Diagram flows for Decisions on CIP related projects and transfers

