Cabinet Member for Finance and Resources	Ref No: FR2 19/20
May 2019	**Key Decision: Yes**
Property development arrangements - procurement of a property development enterprise to work in partnership with the County Council	**Part I**
Report by Executive Director of Place Services	**Electoral Divisions: n/a**

Summary

The purpose of this report is to propose arrangements for and procure a joint venture partner to carry out property development on surplus County Council land. The County Council will set up a corporate entity that it wholly owns and which is able to enter into partnership with an established property development enterprise. The enterprise will be a well-resourced and established organisation of standing with a company record of successful residential and commercial developments. The objective is to maximise the financial return from surplus land assets held by the County Council, and to reinvest the profits to support the wider aims of the County Council.

West Sussex Plan: Policy Impact and Context

The primary focus will be in raising value for the County Council through generating additional financial returns from surplus land assets at financial levels above those likely in a straightforward sale of undeveloped land. The funds raised would then be re-invested across West Sussex to support the wider aims of the County Council.

Financial Impact

The costs of gaining the external advice and support necessary for the set up and procurement arrangements are estimated at £700,000 across financial years 2019/20 and 2020/21, with funding being identified from reserves.

Recommendations:

That the Cabinet Member agrees to:-

(1) The commencement of a procurement process to select a suitable commercial enterprise, demonstrating skilled resources in property development, to act as joint venture partner with the County Council in a business arrangement for the commercial development of surplus council land,

(2) Delegate to the Executive Director of Place Services in consultation with the Cabinet Member for Finance and Resources the selection of the initial tranche of suitable sites and the appointment of the preferred bidder;

(3) Delegate to the Director of Law and Assurance the setting up of a County Council wholly owned company as required to progress the joint venture partnership.

(4) Approve set up costs, including the procurement process, up to the value of £700,000, such funds to be drawn from the Council's reserves.

1.0 Background and Context

1.1 The County Council established a policy for strategic land acquisition and development that involves the County Council actively investing and/or carrying out direct development of land for longer term asset management. The policy used the title 'Propco' to distinguish it from routine asset management. A 'Propco' Panel of members was established to advise the Cabinet Member for Finance and Resources on specific schemes in connection with the policy.

1.2 The 'Propco' Panel has been considering options to progress potential development sites and commissioned a report from Savills to consider the development options. A summary of the report, attached as Appendix 1, evaluates the options to progress the sites.

1.3 The Council holds a number of surplus land assets and an area in the region of 96ha has been identified with varying potential for redevelopment over a period of 15 to 20 years.

1.4 Whilst a straightforward sale of land on the open market is appropriate in some circumstances, opportunities exist, supported by an increasingly favourable policy environment nationally, to return higher financial outcomes for the County Council and to reinvest the proceeds across West Sussex.

1.5 Working in partnership with a commercial property development partner will mitigate risks, provide the required skilled resources, introduce innovative ideas and provide commercial pace to maximise the returns from the council's surplus land and the funding invested in its development.

1.6 At its meeting on 28 March 2019 the County Council's PropCo Panel agreed to recommend progressing property development in this way through the procurement of a corporate joint venture arrangement.

2.0 Proposal Details

2.1 The proposed arrangement is a 'Public-Private Partnership' where the Council and the commercial development company are equal 50:50 partners in the partnership. The Council will provide land for development and, if appropriate, funding. The partnering commercial enterprise will provide expertise, resources, risk management, resilience, innovation and funding to deliver developments identified.

2.2 The objective of the partnership is to create an arms-length operating arrangement which is independent from the County Council. This will enable the partnership to operate commercially in a way that maximises the financial returns from surplus land that is held by the County Council. For this arrangement to succeed, the Council needs to behave towards these sites in the same way that it would treat sites that it sold to a third party.

2.3 The partner will be a substantial commercial enterprise with extensive property development expertise and will be selected through a full competitive tender process. This is subject to further detail and will include an initial tranche of suitable sites. It is recommended that the decision on which sites to include in the initial tranche is delegated to the Executive Director in consultation with the Cabinet Member.

2.4 The procurement is expected to involve a competitive dialogue process to ensure full market facing exchange of information. This provides selected bidders with the opportunity to develop alternative proposals in response to the County Council's outline of requirements. This allows the County Council and its advisers to identify the basis of an effective partnership by listening to the views and experiences of all bidders that have operated similar ventures with local authorities and then translate these to meet an agreed list of selection criteria. When the proposals are developed to an acceptable level of detail, the final stage invites formal competitive bids to be submitted. The process is expected to take between 10 and 15 months.

2.5 In addition to an initial tranche of sites, the County Council could offer the partnership options for further land assets to be developed, and which could be exercised on acceptance of the business case. The status of these sites may differ such as with planning consent for redevelopment or with existing buildings to be demolished. Decisions about which future sites would be placed with the partnership will be made through the Council's capital governance arrangements related to the declaration of assets as surplus to service requirements or for the acquisition of new property.

2.6 The partnership will progress planning applications on surplus County Council land made available by the Council through a planned pipeline of surplus assets. In addition, and subject to business cases, new sites may become available or be acquired for re-development. This work will raise the value of land by gaining planning consents for higher value uses. The partnership

arrangements will ensure that the Council secures an appropriate value for its assets that are transferred to the partnership.

2.7 The viability assessment of then progressing individual sites up to carrying out a construction development, to sell or retain as an investment, will be made on the basis of meeting profit return criteria and market viability in the business cases that are considered by the partnership.

2.8 Opportunities to create wider returns to the County Council, such as retaining parts of developments to build an investment portfolio and earn revenue returns, as opposed to capital receipts in a sale, or in acquiring new sites to develop will be investigated further taking specialist corporate, financial and tax advice. These decisions will need to be taken on a commercial basis.

2.9 To operate with the procured commercial enterprise, it will be more straightforward in terms of pace and ease of decision-making for the County Council to create a separate company, which it wholly owns, to operate as the corporate partner with the external commercial enterprise. The details will be developed following legal and financial advice. The purpose of the corporate partnership is to ensure the focus is on financial returns within the overall scope and constraints the County Council wishes to set when establishing the partnership.

2.10 The company arrangement detail will require further specialist expert advice but will broadly comprise directors, management, marketing, project delivery and aftercare staff. It is envisaged that the output of this team will be reported on a quarterly basis both to the County Council and the board of the wholly owned company and, if need be, the partnering commercial enterprise.

2.11 The County Council's receipt of funds from the trading arrangement will be stipulated as part of the partnership agreement, together with any 'overage payment' which may arise during the development as a result of increased values, lower costs or betterment of development assumptions.

2.12 In appropriate circumstances, and with risk managed security, the County Council might consider providing a level of funding at commercially competitive return rates to progress developments.

3.0 Consultation

3.1 PropCo Panel – this partnership proposal was presented to the PropCo Panel in November 2018 and March 2019 and they have recommended the partnering approach being proposed in this report.

3.2 To date, strategic advice has been provided by leading consultants on the principle of the County Council working in similar arrangements already successfully in place and how those had been procured and are operated.

- Savills, the international real estate consultancy is appointed by the County Council as strategic adviser on property development and has reviewed the scale and type of surplus land potentially available for

redevelopment. A report has been provided on the development options that could be appropriate to the County Council and outlined typical trading and contract arrangements.

- External lawyers advised on how the County Council might work in direct contract and company arrangements for property

- Faithful + Gould, the Council's multi-disciplinary consultant was appointed by the County Council to provide property and development advice over five years and has reviewed and reported on the options

- The experience of other county councils such as Hertfordshire and Surrey with similar surplus property and joint venture property development initiatives has been reviewed and direct support from the project director at Hertfordshire has been offered on lessons learned and methods adopted during its partner selection and management of the venture.

3.3 A project board has been set up to be chaired by the Executive Director for Place Services with senior officers from legal, finance, procurement, estates and assets and property to develop the proposals and oversee the procurement arrangements. Sub panels in specialist areas of legal and finance have been set up to feed into the project board. This project board will advise the PropCo Panel and the Cabinet Member.

3.4 A range of specialist expertise will be required to develop the details and structure during the procurement phase. To date, high level advice has been provided on the principle of similar arrangements already successfully in place elsewhere and how they have been procured and operated. The list will include:-

- Faithful + Gould – the Council's multi-disciplinary partner – will provide set up advice and procurement support;

- Savills real estate agency – will provide strategic land advice, valuation and development appraisal advice and assurance;

- Local estate agents across West Sussex – will provide market, land and house sale price information to position the product and programme to meet demand;

- Architects – to outline the design standards for the properties to ensure maximum financial return on the investment;

- Market positioning advisers – to ensure the product is designed to meet sales prices and standards identified by the local estate agents to provide a product that is attractive to sell;

- Promotional and public relations advisers – to develop the image and reflect the offer in market position;

- Legal – external expertise with experience of similar procurements at local authorities which have established similar ventures recently;

- Finance - external expertise with experience of similar procurements, tax, and funding, also corporate set up expertise around arranging the return of funds, payments generated and investment opportunities.

4.0 Financial (revenue and capital) and Resource Implications

4.1 Setting up appropriate governance structures for the proposed public-private joint venture and running the procurement to select a suitable partner is complex and will require significant input from external advisors and specialists, to ensure the Council's interests are protected. Recognising that need, the table below sets out the estimated costs of commissioning such advice. These have been benchmarked with Hertfordshire and Surrey County Councils, as both authorities have run similar procurement programmes over 2017/2018.

Joint Venture set up work	**Estimate £**
Legal advice	220,000
Specialist finance and tax	120,000
Strategic advice on land and running procurement tender	110,000
Market positioning	30,000
Project management and running procurement tender	50,000
Cost assurance for valuing construction	30,000
Construction detailing and specification	30,000
Procurement process/admin/fees	50,000
Design	25,000
Communications and promotional work	35,000
Total Cost of Proposal	**700,000**

4.2 In terms of funding, there is currently no specific budgetary provision for such costs and therefore should the County Council wish to pursue this initiative, then it is proposed to allocate £350k from the Strategic Economic Plan Reserve, and £350k from the Business Infrastructure Reserve. As at 31 March these funds had balances of £1.295m and £0.706m respectively, to help further the economic prospects for the county. Clearly the Council's resources are finite and choices must be made in terms of how best to use them. In essence the Council would be giving priority to this partnership proposal, in recognition of the risks and rewards targeted.

4.3 The resulting budgetary profile for establishing the venture would be as follows:

	Year 1 2019/20 £'000	Year 2 2020/21 £'000	Year 3 2021/22 £000
Estimated Cost of Proposal	500	200	0
Budget (through use of Reserves)	(500)	(200)	
Surplus/Shortfall	0	0	0

4.4 In terms of what the partnership would deliver financially, indicative figures are included within the Savills report of 28 March 2019, together with comparatives for alternative options such as simply selling land, or direct development. The indicative nature of the figures must be appreciated, and the Council's risk appetite must inform decision-making.

4.5 The Savills report appraises three potential pipeline sites and outlines a projected financial uplift return to the County Council in excess of land value, if developed in a partnership arrangement. The extent of land available, with development potential, indicates a considerable opportunity to gain commercially acceptable financial return above land values and costs. The details will be assessed during the procurement and set up period, then reported by consultants after appraising values across the proposed sites.

4.6 To manage the process and risks, due diligence would be undertaken ahead of seeking a decision on the selection of a partner and in finalising governance and supporting structures, drawing on the external advice gained.

5.0 Legal Implications

5.1 The overall legal position is that the County Council is discharging a legitimate function in its plans to develop land for sale. The aim of the proposal is to promote a commercial return for the longer term benefit of the Council's broader aims. In order to avoid any concern that the County Council would be directly undertaking commercial activity it is being proposed that, should the final partnership's design require it, a wholly owned company is established to enter into commercial arrangements with the partnership. This would ensure that the arrangement is fully operating within a company commercial environment, subject to the constraints and accountabilities that go along with that arrangement. It would also enable that company to take commercial decisions quickly within the constraints of the overall principles and aims imposed by the County Council. This should enable the joint venture partnership to proceed with schemes and initiatives in a more timely and effective way.

5.2 The arrangements for the setting up of the company and the principles by which the company would operate and interface with partnership will be the subject of a further decision once the detail of the partnership emerges from the planned procurement.

5.3 The proposed procurement process together with the company arrangements in setting up trading arrangements will be conducted through the County Council's legal department and supported as appropriate by obtaining specialist legal advice from leading external consultants to ensure a transparent and fully compliant process.

6.0 Risk Assessment Implications and Mitigations

6.1 Corporate and service risks and action to mitigate:-

Risk	Trigger	Mitigation
Inappropriate commercial enterprise becomes the partner	Procurement that does not explore details and identify how a suitable partner could work safely with a local government organisation	Work with consultant teams in soft marketing to identify suitable partners and follow up with evidence of working at other local authorities. Use a competitive dialogue process to develop a tender sifting process that is robustly conducted through consultant teams with experience of similar procurements for public authority joint ventures
Political	Commercial drive from a company seen as not aligned to the wider responsibilities and conflicting with more community focussed demands placed on a County Council	Clarity on the County Council's policy objectives and criteria in making surplus sites available to the partnership for development and enabling the partnership to operate commercially at arms-length. The enhanced financial returns generated will be used to enable new opportunities that can be directly seen to benefit outcomes in the West Sussex Plan
Perception of lower value in lack of competition through entering a long-term partnership	Single source seen and commented on as lacking market tension and being too close to the partnering company	Partnering commercial enterprise demonstrates market tension in acting as management and resource centre by obtaining multiple bids on work packages to demonstrate and maintain a best value, competitive element on all stages. The partnering enterprise will have incentivised interest to lower delivery costs for its own return. Overage arrangements in place to capitalise on movements in the market, during the lifespan of the partnership agreement.
Disagreements between directors and member companies	Differences in benchmarks, goals and values in trading outcomes sought which may shift over time as organisational objectives change	The council will have 50% representation on the partnership board. An arbitration procedure would be signed up to by the Council and the commercial company. Beyond the initial tranche of sites the Council could also cease to transfer surplus land to the partnership.

Risk	Trigger	Mitigation
Poor return from underperforming venture	Market decline	Commercial enterprise as partner is vulnerable to loss and will only proceed with viable propositions. Each opportunity assessed as a business case. Proceeding with a package of sites over a longer period allows for property development risks to be spread and smoothed.
Land value increase shared with developer partner	'Promotion' of land value through planning consent raises value on land and some of the increased value goes to the commercial enterprise	Land title retained by County Council until option to build is exercised to develop. At that point the value is assessed by an agreed valuation method and the County Council 'sells the land' to the partnership. The cost of gaining a planning consent is returned to the commercial partner plus an added uplift set out in the partnership agreement. Further uplifts in land value such as amendments to the planning consent would be captured through overage
Perceived circumstances of carrying out a development will result in a lower value return on land as it is not market tested in offering land for sale or is a delayed return compared to that of early land sale	Land seen as not tested for sale on open market, therefore might not be seen as best value if an open market bidder were to offer a speculatively high bid	The valuation of land is not an exact science, ultimately depending on strength of bids being made during an open market tender if a bidder chooses to speculate on higher value expectations. An estimate of the final sales total value for any completed development will provide the headline overall return, then after deducting all costs and the profit percentage required it leaves a 'residual' sum which will be the land value. This value is informed by the market through predicted returns in sales of housing. There is additional profit gained on house sales by build costs being lowered, through efficiencies in multiple work streams, which will also be gained by the Council in addition to land value. This is the usual and accepted operating basis for developers

Risk	Trigger	Mitigation
		and funders, because it returns predicable profits from house sales that are directly informed by market forces in selling houses. Costs charged by the commercial enterprise direct are controlled by the partnership agreement and these will be competitively tendered – these will include development management costs, marketing costs and agreed profit on cost. In the open market these would differ between commercial partners for different sites
Debts passed to the County Council	Partnering company becomes insolvent	Corporate arrangements that limit liability in partnerships are a usual feature of such agreements and protect liabilities of either party passing to the other via the partnership. Robust selection of companies proving long trading evidence will be required
Loss of opportunity through programme delivery delays	Company pressures elsewhere take over and property investment missed to add value to land in market timing	Programme agreed in a contractual commitment over long-term period that is linked to earnings and performance targets. Damages recover conditions can be put in place for late delivery or lack of performance.
Poor standard of development results affecting the Council's reputation	Partnering enterprise placed under commercial pressure by its parent company to increase returns or changes to company ethos.	Robust procurement process that set out quality standards in Employer's Requirements, independent checks and selection on basis of highest company standards records, also exit strategy available.
Partnering enterprise changes priorities of profit above WSCC profit	Corporate change or take-over results in reduced importance allotted to the partnership	Contracting arrangement contains exit strategy and procurement requires long record of partnering with local authorities and commitment to successful outcomes

Risk	Trigger	Mitigation
Inability to deliver	Lack of resources or overstretching of company in market difficulties, changing priorities	Review in selection to confirm delivery record over long period. Build in to company partnering structure the ability to exit.
Cultural differences between Council and commercial enterprise	Embedded aversion to managing risk prevents entrepreneurial judgment at the Council	Work with council staff and supporting consultants having direct commercial experience, to develop a culture of manging risk in a commercial environment. Importantly, select a commercial enterprise that has experience of working with a local authority and understanding its values and governance.

6.2 The risks are considered manageable with the support of well-resourced and experienced external consultants, but particularly can be reduced by a robust selection procedure on commercial enterprise selection. This must focus on companies with long standing and proven records in partnering with local authorities that have delivered regeneration mixes of housing and commercial developments from promotion to aftercare. It is considered crucially important to select against a track record of the company's ethos towards honest and open trading in a partnership with local authorities, where public facing values are understood.

7. Other Options Considered

Option	Pros	Cons
Sell surplus land	• Brings in early capital receipt to spend on capital projects • Results in development • Clean break from land with no risk	• Misses opportunity of additional value (unless overage obligations are imposed), even if outline planning were to be obtained • Misses investment opportunity to retain part of development • May result in unwanted outcome even if restrictions attempted and does not guarantee the programme of development for the land and therefore investment in community

Reason for rejection Misses the opportunity to maximise the generation of financial returns and in the promotion work to raise value, particularly over long period of improvement in planning use.		

Option	Pros	Cons
Direct develop by appointing contractor on site by site basis	• All earnings directly received • Allows for control of style and approach • Offers opportunity to increase and decrease amount of development undertaken according to market and Council opportunities available without link to requirements of outside partnering enterprise.	• Lacks pace of multiple sites, carries risk, resourcing implications and higher costs • Single line of failure. Council carries most of the risk • Difficult to arrange contractual 'skin in the game' towards sales success to motivate builder.
Reason rejected Misses opportunity to benefit from lower costs through shared management and supply chain efficiencies, together with difficulties of providing skilled resources at the County Council. The Council carries most of the risk and the decision taken not to proceed with the Barnham development demonstrated that the level of risk was not acceptable.		
Option	**Pros**	**Cons**
Development Agreement (A contract agreement in which the delivery partner acquires the land title and provides financial returns on an overage basis as development completes and sells)	• Reduced risk to Council • Some control is retained on development by introduction of contract conditions and parts of development can be retained • Potential for lower investment by developer as land may not be fully paid for at start.	• Tends to be used on small or medium sites • Complex and longer term sites that require extensive planning work may not be well suited and limited ability to control the development in terms of quality and programme • Likely to require repeat setting up on other sites and therefore higher costs
Reason rejected The model is more suitable for individual sites that are known in detail and therefore largely de-risked - it not so suitable for the wider range of sites, which includes large and multiple phased developments currently held by the County Council.		

Option	Pros	Cons
Development Partnership	• Varying risk opportunities to Council	• Suited to straightforward sites that are more

(Contracted arrangement across multiple sites and ranges of agreement types, which can include Council funding and taking risk down to forming a development agreement on specific sites to transfer all risk)	• Some control is retained on development by introduction of contract conditions and parts of development can be retained • Specialist companies can make all arrangements	predictable in timing • A contractual arrangement that will require creation of delivery outcomes for each site and to protect the Council's interests, specialist companies organising arrangement take fee and may absorb little risk • May miss the opportunity of increased returns through systems of standard building lowering costs • Lack of available resources within WSCC to manage such an arrangement.
Reason rejected Arrangements to make these provisions across future sites can be complex and rely on contract clauses and anticipating outcomes. Delivery arrangements not likely to be linked to gain from economies in supply.		

Option	Pros	Cons
Form a joint venture with commercial organisation in a multi-site partnership (As set out in the report on Development Delivery Strategy from Savills presented to PropCo Panel 28 March)	• Programme format of working in a long-term corporate relationship that is commercially resourced and incentivised towards shared success, bringing pace, expertise and resilience • Risk and resources are externally and commercially managed with expertise and pace, but with controls that can be exerted over development in terms of quality, content and programme • Becoming the 'norm' in county councils' land disposal arrangement bringing economies of scale and in reduced process costs to boost returns, even when shared	• Profit return seen to be potentially reduced by sharing returns • Less familiar trading arrangement with potential partners and councils with a low level of precedent case law • Requires working with a commercial partner that may bring conflicts of interest in driving a profitable outcome
Reason chosen Aligns with the policy that is becoming increasingly adopted by public sector landowners,		

and encouraged by Central Government, to share risk and maximise capital return and particularly enable the generation of revenue returns from landholdings. Creating a long-term partnership provides the skilled resources across a range of building types and ability to promote value return on sites that often require early lengthy periods of planning use change before getting near to planning applications. Allows flexibility as market knowledge develops. Also, creating supply chains and standardised building methods will lower build costs when compared to pricing individual sites. Creates opportunities to add unique selling points in addressing priorities for the County Council. Bringing a commercial enterprise into a corporate partnership provides the highest inventive towards creating financial viability and profit return both have a motivation to creating a corporate success that moves with the times rather than having to envisage contractual circumstances of the future.

8. Equality and Human Rights Assessment

8.1 There are no direct implications.

9. Social Value and Sustainability Assessment

9.1 The procurement process will provide opportunities for potential partners to demonstrate how they can help achieve the West Sussex Plan council's objectives for prosperous places (e.g. local supply chains) and sustainability (e.g. design standards).

10. Crime and Disorder Reduction Assessment

10.1 Undeveloped vacant sites do on occasions generate complaints about crime and anti-social behaviour. Bringing these sites forward for well- designed development in a quicker way will reduce these incidents.

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Appendices
1 Development Programme Delivery Strategy Report - Executive Summary

Background Papers
None