PETERBOROUGH CITY COUNCIL

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PROGRESSING FUNDING FOR PETERBOROUGH'S FUTURE GROWTH
LEADER OF THE COUNCIL AND CABINET MEMBER FOR GROWTH, STRATEGIC PLANNING, HOUSING, ECONOMIC DEVELOPMENT AND BUSINESS ENGAGEMENT
December 2014

Cabinet portfolio holder: Responsible Director:	Cllr Marco Cereste, Leader of the Council and Cabinet Member for Growth, Strategic Planning, Housing, Economic Development and Business Engagement Simon Machen, Director of Growth and Regeneration
Is this a Key Decision?	YES If yes has it been included on the Forward Plan : Yes Unique Key decision Reference from Forward Plan : KEY/25JUL14/02
Is this decision eligible for call-in?	YES
Does this Public report have any annex that contains exempt information?	NO
Is this a project and if so has it been registered on Verto?	YES Verto number: 816

RECOMMENDATIONS

Cabinet gave its approval on 24 February 2014 for the Council to establish a Joint Venture ("JV") to regenerate key city centre sites. In order to further that regeneration the Cabinet Member is recommended to approve:

1. An updated Business Case that reflects the evolution of the project (Annex 1)
2. The establishment of a JV Limited Liability Partnership ("LLP") with Lucent Peterborough Partnership SARL ("Lucent"), a partner registered in Luxembourg
3. The grant of option agreements to be made in favour of the LLP on land sites set out in paragraph 4.4.1 of this report
4. The Council receiving loan notes in exchange for the land sites transferred to the LLP
5. An agreement for lease for new offices at Riverside South (Fletton Quays) be made with the LLP
6. The Director of Growth & Regeneration in consultation with the Leader of the Council, the Director of Governance and Executive Director, Resources to exercise delegated authority to agree to all necessary legal agreements with Lucent and the LLP to establish the JV's structure
7. The Director of Governance, in consultation with the Executive Director, Resources to exercise delegated authority to a) transfer the land sites and b) agree the terms of the agreement for lease and subsequent lease for the new offices
8. To appoint the Leader and Deputy Leader as representatives to the LLP.

1. SUMMARY OF MAIN ISSUES

1.1 In February 2014, Cabinet approved work to establish a new Joint Venture (JV), with the aim of securing regeneration of key city centre sites in partnership with capital market investors. The proposals within that Cabinet Report were later debated by Full Council in their 5th of March 2014 meeting, and the recommendations from Cabinet were approved.

1.2 Cabinet delegated authority to key senior officers to progress the establishment of the JV and the necessary legal and commercial documentation associated with those arrangements. The structure of the JV has further evolved and this report seeks approval for these revised arrangements.

1.3 The underlying principles for the concept – of developing commercially viable schemes to help drive the growth and regeneration of the city, and particular the city centre – remain unchanged. The pipeline of schemes are set out in the attached Business Case (Annex 1). The sites highlighted for potential disposal in the February 2014 Cabinet Report remain the same; the schemes proposed in outline in that Cabinet Report for those sites remain the same; the future office consolidation remains the same; the Council's option to choose to have more or less exposure to profit and risk remains the same; and the decision making structures that ensure the Council has to agree to proposals before they move forward remain the same. How some of this will work in operation is now different in some areas, and describing these operational changes forms the purpose of this report.

2. PURPOSE OF THIS REPORT

2.1 This report is for Leader of the Council and Cabinet Member for Growth, Strategic Planning, Housing, Economic Development and Business Engagement to consider exercising delegated authority under paragraph 3.4.3 of Part 3 section 3 of the constitution in accordance with the terms of their portfolio to lead the City Council's growth and regeneration and with the authority to appoint to key strategic partnerships

3. TIMESCALE

Is this a Major Policy Item/Statutory Plan?	**NO**	If Yes, date for relevant Cabinet Meeting	N/A

4. DETAILS OF DECISION REQUIRED

4.1 Background

4.1.1 In February 2014, Cabinet approved the establishment of a new Joint Venture (JV) to bring forward growth in Peterborough, with the aim of securing approximately £130m of long term development investment into the city for a number of key city centre sites, the development of which was currently on hold. This built on previous work that the Council had been undertaking. The Council would be investing £3m of existing growth funding as part of establishing the JV, as well as making available some of its city-centre land assets available for purchase. The first stage of this strategy was to be the development – by the JV company – of viable schemes taken to the point of having achieved planning consent, which investors would then take forward to physical delivery. Full Council debated this report at its 5th March meeting, and approved the recommendations from Cabinet.

4.1.2 The February Cabinet Report gave delegations to senior officers to work on and agree the documentation, such as the shareholders agreement and option agreements, that are necessary for such arrangements to be put in place. This work has been on-going, and in April 2014 the Council signed Heads of Terms with Hume Capital Securities PLC ("Hume"). These Heads of Terms represented an agreement of broad principles against which a commercial deal would be developed in more detail.

4.1.3 Since that time, work has continued towards implementing the optimum Joint Venture model for the Council. Through this iterative, collaborative process that model has evolved in a way that offers benefits to both the Council and the investment partner, and this CMDN details the revised structure of the arrangements that are now proposed.

4.2 The Proposed Model

4.2.1 The underlying principles of the arrangements remain essentially the same as outlined in the original Cabinet Report in February 2014 (see section 4.1.3 of that report), but more detail and specifics about how it will work can now be provided:

a) A Joint Venture (JV) will be established. This will be a Limited Liability Partnership (LLP), and will be 50:50 controlled by the Council and its partner, meaning that both parties have equal voting rights in decision making. The JV LLP's purpose will be to develop viable schemes for key sites in the city.

b) The investor that will partner with the Council in the JV LLP is Lucent Peterborough Partnership SARL[1], which will be set up as a wholly owned subsidiary of Lucent Strategic Land Fund. They are specialists in developing viable schemes for sites and obtaining planning permission for these. Lucent Strategic Land Fund was an investor introduced to the Council by Hume Capital Securities PLC as being a potential partner in the arrangements, and is already working with other Local Authorities (Allerdale Borough Council) in similar arrangements.

c) Hume Capital Securities PLC, with whom the Council signed Heads of Terms in April 2014, has since decided to develop an investment fund that would enable it to potentially purchase and take forward schemes developed by the JV LLP. The Heads of Terms have been reviewed and do not prevent the Council entering into an agreement with Lucent to set up the JV LLP.

d) The Council will grant option agreements to the JV LLP for sites it has available for disposal. When the option agreement is called upon by the JV LLP and land transfered, the Council would receive a loan note for the market value of the site and also benefit from profit share from schemes that are developed.

e) In the first few months of the JV's existence, an Investment Plan will be created that programmes the work to develop more detailed scheme-specific project plans, all of which have to be approved by both the Council's and the partner's representatives on the JV's Board before they can be taken forward. It is only after approval of the project plan that the Council will transfer any relevant site to the JV.

f) When the JV LLP exercises a relevant Option Agreement and takes ownership of the land, the Council receives a loan note for the market value of the asset. Market value

[1] A SARL is the Luxembourg equivalent of a UK limited company.

will be determined by an independent property valuer appointed by the both partners at "day-one" and they will apply an industry standard red-book appraisal against a project brief based on the scheme under consideration for the site. The land value will meet the Council's duty under s.123 Local Government Act 1972 (i.e. the best consideration reasonably obtainable); it will be a market value based on the type of scheme being proposed. The council will receive a 'Loan Note' for that site market value and this is explained further later in this document; their use is normal commercial practice.

g) When the Council and Lucent agree projects to go ahead based on the project plans, Lucent will invest all the money required to develop these projects into the JV LLP on the same loan note basis; the Council will always have the option – but not an obligation – to invest finance, in addition to contributing land.

h) For approved projects, the JV LLP will create a new wholly-owned subsidiary special purpose vehicle (SPV) to take the scheme through to planning approval, and assign all the finance required and the relevant land.

i) Once the SPV has developed a viable scheme and obtained planning permission – and always subject to the final approval of both JV LLP partners through the JV LLP's Board – it is sold on so that physical regeneration can take place, to the buyer identified early in the process.

j) Proceeds from the SPV sale pay off the Council's and Lucent's loan notes, and may be required to pay other Third Party land / development costs if necessary.

k) After the retention of a working capital reserve (which will be determined and agreed by the LLP's Board), remaining profits are then split equitably between the JV LLP partners, based on their relative contributions to the JV LLP.

4.2.2 In brief, a summary of the changes are set out in the table below:

Previous structure	**Revised Structure**
1. To set up a Joint Venture Company with a Guernsey investment fund ("fund")	1. To set up a Joint Venture ("JV") Limited Liability Partnership ("LLP") with Lucent Peterborough Partnership SARL ("Lucent")
2. To invest £3m into the Joint Venture for shares	2. The Council is no longer required to invest £3m (although it has the option to contribute cash to projects if it wishes), which offers a greater revenue saving
3. Option agreements granted to transfer land sites to the fund in exchange for cash or investment units in the fund	3. Option Agreements granted to transfer the same land sites to the JV LLP in exchange for loan notes when the option is exercised and redeemable once sites are sold
4. The land granted under an Option agreement to be transferred to the fund when planning consent obtained	4. The option agreement sets out that the land will only be transferred when a Project Plan is approved by the Council and Lucent representatives on the JV LLP Partnership Board

5. The Agreement for Lease for new offices at Fletton Quays to be made with the fund at the time option agreements are granted	5. The Agreement for Lease to be made with the JV LLP (rather than the Fund as previously). The Agreement for Lease is entered into after the JV LLP exercises the relevant option agreement.

4.3 The Joint Venture and its Structure

4.3.1 The JV would be overseen by a small Board, comprising four voting board members. The Council would have two representatives and Lucent would have two representatives. The quorum for the Board is four. Each set of representatives has a single vote, and all decisions made by the Board must be approved by both parties. For the avoidance of doubt, this means that if either party does not agree to it (or abstains from voting), then nothing happens.

4.3.2 Earlier Cabinet Member Decision Notices dated April and May 2014, nominated the Leader and Deputy Leader to act as directors on the board of a JV company. As the revised structure involves establishing a JV LLP (not a company) the Leader must appoint representatives (not directors) to the JV LLP Partnership board.

4.3.3 Under the Council's constitution the LLP is deemed to be a key partnership and appointment to the Board of the LLP falls automatically to the relevant Cabinet members with the Leader determining who he considers to be most appropriate to fill the required number of seats. The appointment as representatives is therefore made to the Leader and Deputy Leader.

4.3.4 Unlike with directors, the representatives' duties are not statutory duties. However, they still owe contractual duties which are similar to a director's duties in that they are responsible for the day to day running of the LLP, and are required to act in good faith and in the best interests of the JV LLP. Site specific SPVs created by the JV LLP will be limited companies and the Council's representatives on the LLP will be company directors for these, and in this case will owe the usual fiduciary and other duties and responsibilities to these companies that being directors places upon them.

4.3.5 It was previously envisaged that the Council would invest £3m of existing money allocated for growth into shares in the JV, which would have been matched by a partner, to provide the working capital for schemes to be developed. As the model has evolved, it has been possible to agree that this is no longer a requirement, and whilst the Council continues to have the option to invest in the development of schemes to increase its profit share, it is a choice rather than a necessity. This brings an additional revenue saving benefit for the Council at a time of significant pressure on revenue budgets.

4.3.6 As each project plan is developed, it will be clear and agreed by both parties the finance required for the scheme to obtain planning permission. The Council will have the option to invest at that time. If the Council chooses not to, Lucent will cover all of these costs for every JV Board approved project plan. The investments that either Lucent or the Council make into the development of schemes will be made as a loan to the JV, which will be repaid once the scheme obtains planning consent and is then sold to a third party at the appropriate point for physical delivery.

4.3.7 Profits that are left after the repayment of land and investment loan notes, (and a working capital reserve established if the Board agrees to this), will be split between the JV LLP partners according to the ratio of aggregated investments they make. This means that if the Council's total investment is 60% (made up on the Council's land, its contributed staff time, and any optional financial investment it has chosen to make) and Lucent's is 40%, the Council would be allocated 60% of any profits. The Council can choose to take such profits out of the JV LLP (for example, to support service delivery), or it can re-invest them in regeneration projects. It does not have to decide this immediately, which gives the Council flexibility for the future.

4.3.8 Day to day, the JV LLP would be run by a small project team with representatives from both partners. This team will work on each scheme to ensure it is developed appropriately into a commercially viable project for which planning consent can be obtained. The Council will also need to establish internal support and governance arrangements to ensure it can support and respond to proposals arising from the JV.

4.4 Council Assets and Office Consolidation

4.4.1 The assets the Council will make available to the JV LLP remain unchanged from the original February Cabinet Report, and the list is provided below for completeness. Following the February Cabinet report and approvals received at Full Council in March 2014, all of the sites were added, where necessary and appropriate, to the disposals list.

Site	CCDPD policy
Wirrina Car Park	CC7: Riverside North
Former B&Q site	CC6: Riverside South
Former Matalan site	CC6: Riverside South
Bridge House Site	CC6: Riverside South
Engine Sheds	CC6: Riverside South
Bayard Place	CC3: City Core
Market Multi-storey Car Park	CC3: City Core
Pleasure Fair Meadows Car Park	CC6: Riverside South
Aqua House	CC6: Riverside South
The Mill (purchase negotiations in progress)	CC6: Riverside South
Central Library (inclusion subject to further discussions)	CC10: City North

4.4.2 The purchase of Aqua House, which was underway in February, has now completed and an Option Agreement will be granted for this asset as part of the JV LLP set-up. As was the case in February, the Council cannot grant an option agreement on The Mill site at this stage because it does not own it, but it is included here to continue to highlight that if it does acquire this site, the intention would be to grant an option agreement to the JV LLP shortly after acquisition.

4.4.3 Each of the option agreements for the sites above will only be exercisable by the JV LLP if its Board (and thus the Council) approve a Project Plan that requires the site. For avoidance of any doubt, if the Project Plan is not approved, the option cannot be called upon and the site cannot be transferred into the SPV. The Council must be happy with the proposed scheme and the finances and values within it for it to proceed, and this will include giving due regard to any income it currently receives from the site that could be lost if that site is developed (such as for the Wirrina car park, for example).

4.4.4 When a site is transferred, the JV LLP issues a loan note to the Council for the market value of the site. The land is then placed in the relevant SPV, and a commercially viable scheme developed and planning consent obtained. When this SPV is sold, proceeds from the sale repay the loan notes outstanding within the JV LLP pro rata between Lucent and the Council, including any accrued but unpaid interest on both partners' loan notes.

4.4.5 The projects originally proposed in the February Cabinet Report remain unchanged, and would be taken forward – including the Council's office consolidation, subject to the same preconditions relating to financial acceptability by the Council – by the JV LLP subject to both the Council and Lucent agreeing the relevant Project Plans. Office consolidation is discussed further in section 12 of this report, Property Implications.

4.5 Governance

4.5.1 In governance terms, there are three different decision-making bodies within the proposed JV arrangements: the members of the LLP itself, Lucent and the Council (equivalent to shareholders in a company), the Board of the JV LLP, and the Project Team in the JV LLP.

4.5.2 As noted in 4.3.8 above, the project team is to be made up of a number of representatives from both Lucent and the Council, and would run the JV on a day to day basis. It has the authority to do so delegated to it from the LLP Board. The project team's primary function is the development and refresh of the Investment Plan and the Project Plans that sit within this, as well as co-ordinating delivery of approved Project Plans by the SPVs.

4.5.3 Decision making by the Project Team is, like the Board, by consensus, and they are expressly only able to take decisions that are in keeping with the Investment Plan and / or relevant Project Plan as approved by the Board and JV LLP members. Significant variations from this (the change of use of a site from the original intention, or where returns from the project are expected to adversely deviate by 20% or more from original approved estimates) must be referred upwards to the members for approval (see list of reserved matters in section 4.5.5 below) . In the event the Project Team are unable to agree on an issue, it is elevated to the Partnership Board to determine, and if the Partnership Board fails to resolve, it is referred to Council and Lucent, as members, for a decision.

4.5.4 The Board is the ultimate decision maker within the JV LLP itself, being comprised of an equal number of representatives from Lucent and the Council. Decision making is by consensus, and both parties must agree before a decision can be approved. The Board will meet monthly in the first twelve months of the partnership's life, and then every three months or as otherwise agreed by the Board.

4.5.5 Lucent and the Council, as members of the JV LLP, will delegate the operation of the JV LLP to the Board and the Project Team. Their respective interests are represented by their delegates on the JV LLP Board. There are also specific matters that are reserved to the Council and Lucent in their role as members for approval rather than being within the remit of their representatives on the Board. Some of these reserved matters include:

a) Adoption of the First Investment Plan.

b) A material variation to a Project Plans (being either a change of use of a Site or Project; or where there is an expected adverse deviation of 20% from the expected returns to the JV LLP as originally set out in a Project Plan

c) Extending the JV LLP's or any Project SPV's activities outside the scope of the Business or close down any business operation.

d) Giving or taking any loans, borrowing or credit (other than normal trade credit in the ordinary course of business) in excess of those stated or referenced to in the relevant Project Plan.

e) Giving any guarantee, suretyship or indemnity to secure the liabilities of any person or assume the obligations of any person in excess of those stated or referenced to in the relevant Project Plan.

f) Creating any Encumbrance over the whole or any part of the undertaking or assets of the JV LLP or over any Member Interest in excess of those stated or referenced to in the relevant Project Plan.

g) Commencing, settling or defending any claim, proceedings or other litigation brought by or against the JV LLP or any Project SPV, except in relation to debt collection in the ordinary course of the Business.

h) Approving the annual accounts of the JV LLP.

i) Changing the name of the JV LLP.

j) Employing any employees, or making any offers of employment to any person. Changing the terms and conditions of employment of any employees.

k) Making a petition or passing any resolution to wind up the LLP or any Project SPV or make any application for an administration or winding up order or any order having similar effect in a different jurisdiction in relation to the LLP or any Project SPV or give notice of intention to appoint an administrator or file a notice of appointment of an administrator unless in any case the LLP or any Project SPV is at the relevant time insolvent and the Directors reasonably consider (taking into account their fiduciary duties) that it ought to be wound up or it ought to enter into administration.

l) Admitting any person as a member of the JV LLP save in respect of a transfer of Member Interest permitted pursuant that specified in the Members Agreement.

m) Forming any subsidiary of the JV LLP that is not required pursuant to a Project Plan, or acquiring any shares in any other company, whether through subscription or transfer, such that the company concerned becomes a subsidiary of the JV LLP.

n) Consolidating or amalgamating with any company, association, partnership or legal entity or acquire any business or undertaking of any other person.

o) Entering into any partnership or profit sharing arrangement with any person or create any share option, bonus or other incentive scheme.

p) Making any agreement with any revenue authorities or any other taxing authority, or make any claim, disclaimer, election or consent of a material nature for tax purposes in relation to the JV LLP, its business, assets or undertaking (including the Project SPVs).

4.5.6 The delivery of the regeneration of key sites is governed by the creation and approval of the Investment Plan and the Project Plans for each scheme. All three decision making elements above are involved in the preparation and approval of these:

a) The Project Team works to prepare the Investment Plan and, once that has been approved, the Project Plans that sit underneath it. Once the Project Team, by consensus, agrees these documents, they are provided to the next Board meeting for discussion and approval.
b) The Board consider the Investment Plan / Project Plan. If approval is not obtained, it can be referred back to the Project Team for further work or be abandoned. If both Lucent and the Council's representatives support the document, it is approved by the Board and referred back to the member organisations – Lucent and the Council – for final approval.
c) Council approval follows the Council's usual governance and decision-making process, with the relevant Investment Plan / Project Plan being considered by the Cabinet Member with the relevant portfolio, and subject to scrutiny in the usual way.

4.6 Risks and mitigations

4.6.1 Any proposal of this scale contains a degree of risk and this is no different. Importantly, though, significant effort has been expended to ensure that the proposals contain a variety of safeguards and protections that minimise the potential impact of these risks, the likeliness of them happening, or both. The list below captures the main risks the Council should be aware of and how these are managed.

a) Sale proceeds from an SPV could be less than is needed to pay off related loan notes

Part of the project planning process is to carefully assess the viability of a scheme, which includes market estimates for the ultimate sale price and regard for factors that could result in this varying. It is unlikely either JV partner would wish to proceed with a scheme that presented significant risk to returns in this way. There may, however, be an occasional case where a scheme is highly attractive for non-financial reasons (such as a community regeneration project), and the Council wishes to proceed despite a low or negative return; one of the benefits of this model is that the Council could decide at that point to use profits from previous schemes to off-set the viability gap present, allowing a site to be redeveloped where it would otherwise be unable to be. It is also possible that two sites could be linked to create an overall viable proposal where one profitable site supports delivery of one that is not commercial viable.

b) Costs for obtaining a planning consent could rise above what was expected

Careful estimates of costs for obtaining consent are developed in the project plan, which details the assumptions around those to ensure they are robust and transparent. Costs are monitored within the SPV carefully, including forecasting forward against the baseline plan, and any variation from this is addressed by the project team in the first instance, who will try to bring the expenditure back in line with the baseline. In the event that additional funds are needed, it would be requested from the JV LLP and for the partners to decide to fund at that point through an additional loan note.

c) An off-take partner cannot be found to buy a consented scheme

This is unlikely because of two factors: firstly, that it is a general intent to secure an off-take partner at the project planning stage, to provide reassurance that this would not happen and also to remove much of the larger financial risk. Secondly, that even in the event this did not happen or that the intended off-take partner withdrew, a consented scheme is generally much more attractive for purchasers than land without such consent, especially where the JV LLP can demonstrate the scheme is financially robust and viable, which should support attracting a buyer.

d) The Council and Lucent are unable to agree how a site should be developed

The JV LLP will be based on an ethos of partnership working to develop sites that are consistent with planning policy and the Council's wider aims for the city, whilst being commercially viable. Lucent accept this might mean that the most commercially beneficial scheme may not be the one the Council want to pursue, and the Council accepts that there is a need for the scheme to be financially robust and provide a commercial return. This shared understanding exists when entering into the JV arrangements, and it is considered unlikely that there would be a situation where both parties could not resolve any differences to agree a project plan, not least because it is in both parties interest to do so. However, were such a situation to arise, then the site would remain undeveloped and in Council ownership.

e) A situation arises whereby the Council needs a site for a different purpose, but for which an option agreement has been granted to the JV LLP

The Council would be able to ask the JV LLP to release the option agreement on the relevant site. Whilst there is no contractual obligation upon the JV LLP to do so, it is in the interest of the partnership for the JV LLP to be reasonable.

f) Having established an SPV to obtain a consented scheme, market conditions change such that the plan is no longer viable

Assumptions about market conditions will generally be made as part of the project plan, but it is possible – as with events like the 2007/8 crash – that market factors change dramatically in a short space of time. This level of unpredictability is unusual, but obviously not impossible, and a decision would need to be made at that point how to proceed. For example, the project team may determine an alternative scheme that produces a viable outcome, and this would then be referred back through the decision making process for approval. Alternatively, the Council has a buy-back option that allows it to retake control of any transferred land not being taken forward at the then-market value for the site.

g) The JV LLP agrees a project plan and establishes an SPV to take a scheme forward and obtain planning consent, but planning consent is ultimately refused

The involvement of the Council in the JV LLP's project team is partly intended to ensure that the proposals are entirely consistent with planning policy, and the SPV would work closely – just as any other developer would – with the Council's planning team through the pre-app process to ensure this was the case. The Council's planning function would, of course, be entirely independent to this process and would treat the JV LLP in the same was as any other third-party developer.

h) The independent valuation of the Council's land indicates that it is worth less than the Council would expect it to be

The approach being taken to valuation is intended to be entirely fair, transparent and based on standard industry practice. The price will be a fair price for the site, at the appropriate market value at the time. In the event the valuation is unacceptable to the Council, it could choose not to approve the project plan that the site is used within, which would mean the scheme – and thus the transfer of ownership – would not take place. It would need to weigh this against the fact that the Council will have been working to develop a scheme it wanted to see on that site, and that it may have been some of these aspects that were obviously desirable to the Council that have restrained the land value.

5. CONSULTATION

5.1 These proposals have been developed through extensive internal consultation with officers from finance and legal services, including the Head of Strategic Finance and the Director of Governance, both of whom have been involved in developing and refining the proposals. The Leader of the Council has been consulted throughout.

6. ANTICIPATED OUTCOMES

6.1 That the Council will conclude the necessary legal agreements required in order to set up a JV LLP, and that this entity will begin working on developing the schemes discussed in the original February 2014 Cabinet Report.

7. REASONS FOR RECOMMENDATIONS & ANY RELEVANT BACKGROUND INFORMATION

7.1 The recommendations within this report are a result of refinements to the proposals Cabinet approved in February 2014, in line with the recommendations of that report. These revisions will help deliver the underlying aims outlined in that report, helping to bring forward key city centre regeneration sites, allowing the Council to further the city's growth and regeneration with minimal additional investment whilst delivering potential financial and other benefits to the Council and the city.

8. ALTERNATIVE OPTIONS CONSIDERED

8.1 Section 10.1 of the February 2014 Cabinet Report discussed the alternatives to the approach the Council proposes to take. *T*hose options are not repeated here but the Cabinet report remains relevant and has been brought to the attention of the Leader in making this decision.

9. FINANCIAL IMPLICATIONS

This section considers the financial implications in the following three areas:

- A summary of the key arrangements

- Loan notes and associated issues
- The impact on the Medium Term Financial Strategy

It should be noted that the general commentary on funding for growth in Peterborough, as well as the detail of the South Bank business case that was included in the original Cabinet Report is not repeated here, but these issues remain relevant to the new partnership.

9.1 A summary of the key arrangements

An overview of the proposed arrangements is included in section 4. The overall aims of the JV remain the same, but there are some differences from a financial perspective that are worth highlighting:

- The JV partnership is with Lucent Peterborough Partnership SARL, a company registered in Luxembourg that is a wholly owned subsidiary of the Lucent Strategic Land Fund
- The Lucent Strategic Land Fund is regulated by the Commission de Surveillance du Secteur Financier (CSSF). Investment Funds in Luxembourg are required to adhere to EU legislation with regards to the origin of investment.
- No investment into the JV LLP is now required by the Council. Previously the Council would be investing £3m (£2m borrowing, £1m S106 monies for affordable housing). Lucent will fund the operation of the JV LLP and development costs, but will then receive a return on its investment from the sale proceeds post-planning. The Council could choose, if it wished, to invest directly in schemes. This investment would be subject to the Council's normal decision making process
- The JV works up an initial project plan outlining the scheme, including forecast costs of achieving planning permission and the likely sale process that would include the estimated sale proceeds
- The option agreement on the property is exercised when the project plan is agreed by project team, and then the JV LLP Board
- The Council receives loan notes for the value of each property at the point of transfer. Similarly Lucent receive a loan note at the point they invest cash into the JV.
- The Council receives cash once the scheme with planning consent is sold (after costs and the retention of a working capital reserve if this is approved by the JV LLP Board). The Council could choose not to receive the cash, and to maintain the investment in the JV LLP.

9.2 Loan notes

9.2.1 Neither party receives a cash return until planning permission has been granted and the asset sold. In return for assets, cash or services transferred into the JV LLP, both parties receive loan notes in return. These loan notes are paid when the JV LLP receives cash. Interest is payable on the loan notes at a rate of 12%, but is rolled up i.e. it increases the value of loan notes, rather than actually being paid annually.

9.2.2 In summary this process works as follows

- The Council transfers land to the project SPV via the JV LLP once the project plan is agreed. The land is valued at that point before planning permission. The Council's loan note is for that value

- Lucent provides cash to fund the project. Its loan note is for the value of its funding
- Loan notes are aggregated at JV LLP level, even if there are multiple projects and SPV's
- Proceeds are shared out based on the respective share of loan notes at JV LLP level (not at individual project level)
- Once a scheme is complete, the proceeds, less any fees or tax, are shared as follows (from the top down)

Retention of working capital reserve (to be agreed by the JV LLP Board) Payment to third parties (such as potential third party land development costs, if necessary and agreed)
Council's Loan Note, including accrued but unpaid interest, is repaid (based on valuation at time of transfer) Lucent's Loan Note, including accrued but unpaid interest, is repaid (based on value of cash put into JV)
Surplus applied to partners in proportion to Loan Note Value at JV level (i.e. combined value of all loan notes across all projects at that stage)

9.2.3 A numerical example of how this could work is outlined below. It must be noted that this is simply an example to help explain the process outlined in para 9.2.2 above. The values are not based on any specific sites or valuations:

9.2.3.1 In relation to a site to be sold, the simple worked example below is based on the following assumptions:

- Council transfers land valued at £1m to the project SPV and is issued loan notes to this value.
- Lucent invest the necessary funding to pay for design and development, which includes planning and legal fees, at £1m and is issued loan notes to this value.
- Sale price of the land = £3 million
- The Purchaser would be under an obligation to pay £3 million to the Project SPV for the land.

9.2.3.2 The exit methodology would then work as follows:-

- Purchaser pays £3 million to the Project SPV;
- Project SPV uses the £3 million to repay any outstanding SPV Loan Notes held by the JV LLP and then to pay that balance to the LLP
- The JV LLP would receive the £3 million and then allocate this amount to the Members loan accounts, split between the Members in their profit share proportions at that time (in this example, 50:50).
- The amounts allocated to the loan accounts would be used first to repay any outstanding JV LLP loan notes. Any remaining balances could be distributed or reinvested into future projects, as decided by the Member. The net position for the Council and Lucent would therefore be that each would receive £1.5 million, £1m as repayment of the loan notes and £500k profit. The loan note repayment would be treated as a capital receipt, and the profit as revenue income.

9.2.3.3 This simple example assumes that there is only one project undertaken by the JV. When there are multiple projects (as will be the case for the Peterborough JV), then the profit share is based on the total loan notes held across all projects. A more detailed example of this is included in Appendix 1 at the end of this Decision Notice.

9.2.3.4 If the land transferred to the JV LLP was deemed to have no commercial value (for example, because development values are very low), then the Council would not receive a return (but may wish to see the project proceed for broader regeneration benefits, including potential council tax, new homes bonus and retained business rates).

9.2.4 As before, the Council have engaged Grant Thornton (GT) to advise on the structure and accounting implications of the partnership. They have confirmed that the loan note approach is normal commercial practice

9.2.5 With regard to accounting treatment, effectively the loan note is an asset – gained in exchange for land. The accounting regulations class this transaction as capital spend. The GT advice expands upon the reasons for this, and confirmation has been provided by Pinsent Masons. The proposed treatment has been shared with PriceWaterhouse Coopers as the Council's external auditors. They have confirmed to the Council that they are "not minded to challenge the proposed accounting treatment".

9.2.6 Whilst the loan note is deemed to be capital spend, the Council does not actually make any payments. Nor does it face any capital financing charges, such as minimum revenue provision. There is no budget within the capital programme. Whilst this is in some respects an accounting technicality, it is suggested that any such arrangements are badged against the 'invest to save' budget. The exact values will be known when sites are valued and project plans agreed. Updates can be provided in Cabinet financial reports on the position.

9.2.7 There is some potential risk arising from this partnership, as there is in any type of development arrangement. For example, even though a project plan has been agreed and the asset transferred (with both parties carefully considering and managing as far as possible any risks prior to approval), the JV LLP could encounter difficulties in progressing the scheme. In this case the Council does have the option to buy the asset back (effectively the sale proceeds to JV then repays the Council loan note, so the transaction should be net nil, although the Council would need to pay market value if the value had increased). Such a transaction would need specific approval in the Council.

9.2.8 The assets of the JV LLP (assets transferred by the Council and cash transferred in by Lucent) will be held as security for the loan notes. The only time that the security should be enforceable is if the JV LLP defaults in its payment obligations to the Loan Note Holders (i.e. the Members). This enforcement would require agreement of both Lucent and the Council. In an extreme case, where the cash had been used, Lucent may have access to the remaining security. However the need for the JV LLP Board to act would have been triggered well in advance of such a situation.

9.3 The impact on the Medium Term Financial Strategy

9.3.1 The Council's £3m original contribution was to be funded from the approved capital programme as follows:

- £2m from the 2014/15 capital budget outlined above.
- £1m from affordable housing Section 106 monies.

As this is no longer required, the £2m can be saved. This increases the savings from the proposals by £130k per year. The total savings from the approach are now as follows:

- 2015/16 to 2017/18 £380k per year (up from £250k)
- 2018/19 onwards £530k per year (up from £400k)

9.3.2 The original report outlined the current viability gap for the south bank business case. This remains the case, and it will be the role of the JV LLP to develop the detailed business case, including investigating further the options for ensuring a viable business case. Those proposals would be presented to the JV LLP Board, which includes the Council representatives, for approval before it can proceed. As part of any business case, the Council will also need to consider the impact on business rates and council tax (both in terms of gains from new buildings and homes, but also losses if commercial properties are redeveloped). The viability gap will need to be closed before the scheme can proceed.

9.3.3 The medium term financial strategy (MTFS) agreed in March 2014 by Council included relevant sections in the Capital Strategy, Asset Management Plan and Treasury Management Strategy to allow the JV partnership. This included the revised capital programme, the sites listed in this report on the asset disposal list and the approach to granting option agreements. Whilst not all aspects of these are required, they cover most of what is required under these proposals.

9.3.4 Under the previous proposals, the Council was to invest £3m into the JV, but received 100% of full market value in return. In this partnership, the Council does not have to invest, but in return gets market value pre planning plus a share of any uplift (sharing that uplift with the partner). External advisers have confirmed this approach is normal commercial practice.

10 LEGAL IMPLICATIONS

Although there are number of changes under the new structure, there are no adverse legal implications arising from these changes. This section deals with the legal implications in the following six areas.

- Authority to use a Limited Liability Partnership (LLP) in the Joint Venture's (JV) new structure
- Legal status of an LLP
- Constitution
- Procurement
- State aid
- Loan notes

10.1 Authority to use an LLP for the Joint Venture

10.1.1 The Council must be satisfied that it has the statutory power to use an LLP to enter into the JV's revised structure. It has a statutory power, normally described as a General Power of Competence (GPC) to enter into the proposed JV structure.

10.1.2 The Council has obtained advice from Pinsent Masons, its external legal advisers, regarding the use of an LLP under this power. They have advised that the key consideration for the Council is to look at its primary or dominant purpose for wanting to enter into the JV structure.

10.1.3 If the purpose of exercising this power is for a “commercial purpose”, then it must be done through a company (not an LLP). Although the LLP is created with a view to profit, and on the face of it indicates a “commercial purpose”, this does not automatically mean that this is the Council’s own primary or dominant purpose. The profit element in this structure is ancillary to the Council’s predominant motive.

10.1.4 As the Council’s primary or dominant purpose to enter the JV is for the growth and economic regeneration of Peterborough and not for a “commercial purpose”, it can use an LLP to establish the JV.

10.1.5 The Council has also considered statutory Guidance issued to local authorities trading through a company. Although the Guidance does not apply because the Council is not trading through a company, the Council is nevertheless adhering to the Guidance to demonstrate that it is acting reasonably and in due consideration of the financial implications of the JV structure. In line with this Guidance, an updated Business Case is attached (Annex 1) for the Council’s approval.

10.1.6 The Guidance also provides that local authorities should approve a Business Plan for the JV. The Business Plan (called ‘Investment Plan’ in this Report) is to be agreed within three months of completing the JV agreement. It will be approved by members of the LLP, namely by the Council and Lucent (acting unanimously) before it is adopted by the LLP.

10.2 **Legal status of an LLP**

10.2.1 The key features of an LLP are:

- An LLP is a body corporate with a legal personality separate from its members. An LLP is incorporated by registration at Companies House. Like a company, the LLP is required to file accounts and other information regularly.
- It is able to enter into contracts, hold property and can sue and be sued. As a separate legal entity, the LLP and not its members are liable to third parties.
- LLP members have limited liability, in that generally they do not meet the LLP’s liabilities.
- The members act as agents for the LLP and are only liable up to the amount they have contributed to the LLP. This means that the Council’s and Lucent’s liabilities as members of the LLP are limited to their land transfers or cash funding.

10.3 **Constitution** – Terms of reference and Cabinet’s recommendations

10.3.1 This decision is made under paragraph 3.4.3 Part 3 Section 3 of the Constitution which provides the Leader to exercise his specific delegation in accordance with the terms of their portfolio to lead the City Council’s growth and regeneration.

10.4 Procurement

10.4.1 Public Contract Regulations 2006 (Rules)

The Council must act in accordance with the Public Contract Regulations 2006 (Rules). Under the Rules, the award of public contract works, services or supplies require competition. The creation of the LLP to procure investment and sell land will fall outside the Rules, and will not trigger a call for competition.

10.4.2 Under the JV structure, the Council commits to lease offices in a new building at Fletton Quays from the LLP. Ordinarily, taking a lease of an existing building for public office accommodation will fall outside the Rules. Where the Council's lease is for a new building (not yet existing), the agreement for lease will also fall outside the Rules because it will not place contractual obligations on the LLP to build the offices on its behalf.

10.4.3 European Union General Treaty Principles (Treaty)

Even where the Rules do not apply, the Council must nevertheless consider the application of the General Treaty Principles (Treaty) on the JV structure. The Treaty lays down the principles for the functioning of the European Union through freedom of services, goods, equal treatment, transparency and non-discrimination. Pinsent Masons have advised that the JV structure will fall outside the scope of the Rules, and that there is no need for competition under the Treaty.

10.5 State aid

10.5.1 Unlawful state aid occurs where a benefit is granted from a public resource for free or on favourable terms which distort competition. The Council has considered state aid implications on the JV structure and there is no unlawful state aid implication. This is explained in more detail below.

10.5.2 The creation of the LLP does not in itself create state aid issues where the investment contributions are made on equal basis between the private and public sector. In the JV's new structure, the contributions by the Council and Lucent to the LLP are potentially different and may not be made on a 50/50 basis. However, this does not raise state aid implications because the risks and returns are directly proportionate to their respective contributions.

10.5.3 The transfer of the land sites by the Council under the specific Option agreements do not raise state aid implications. The Council has the power to dispose of assets in this way, and in doing so it shall secure the best consideration reasonably obtainable. The JV LLP structure would specifically provide for the Council to receive agreed market value consideration for each land transfer by reference to an independent valuation. This method of valuation satisfies best consideration reasonably obtainable and as such no state aid implication will arise.

10.6 Loan notes

10.6.1 The option agreement will provide that the JV LLP will have a right to direct that upon the exercise of an option, the land is transferred to a wholly owned subsidiary Special Purpose Vehicles (SPV) of the JV LLP.

10.6.2 On transfer of a land site to the SPV, it will issue a Loan note with sufficient value to satisfy the transfer price. Loan notes can be issued as consideration (instead of cash) under a contract for the sale and purchase of land. It is quite common for loan notes to be used in transactions like the proposed JV structure.

10.6.3 The SPV loan note will then be exchanged for a JV LLP loan note. This means that the Council will receive a loan note from the JV LLP.

10.6.4 An advantage of using a loan note is that if the JV LLP defaults in its repayment obligations, the Council and Lucent as noteholders will be in a better position to unsecured creditors of the JV LLP. If the JV LLP borrows for example from a bank, then any security taken by the bank would most likely rank ahead of the security held by the Council and Lucent – this means that the bank would get their money back first, then the Council and Lucent, the unsecured creditors and so on. However, the Council will be in control over any such decision by the JV LLP to borrow money from a bank because it has a shared 50/50 control in the decision making of the JV LLP.

10.6.5 In the JV structure, Lucent will act as a security trustee. This means that Lucent will hold the loan notes on trust for the Council and Lucent. The appointment of Lucent as trustee will avoid having to issue security separately to the Council and Lucent which can be costly. If the Council needs to enforce its security to get repaid on the Loan note, then Lucent will act on its behalf. For assurance, the Council has received a draft legal opinion from Luxembourg qualified lawyers which indicates that it may enter into the JV structure and act as trustee under Luxembourg law.

10.7 **Conclusion**

10.7.1 There are no adverse legal implications arising from the changes to the JV structure for the reasons set out in this section.

11. STAFFING IMPLICATIONS

11.1 A number of staff within the growth team may be affected by these changes and this will be dealt with in accordance with the Council's normal employment policies and procedures, in consultation with those staff and the trade unions. Additionally, the office consolidation proposal will have impact on staff currently at a number of disparate locations, and this will be subject to appropriate consultation at the time.

12. PROPERTY IMPLICATIONS

12.1 **Option Agreements**

12.1.1 The granting of option agreements on the sites mentioned in section 4.4.1 commits the Council to sell these sites in the event the option is triggered. It should also be kept in mind that it limits what the Council can do with those sites for the life of that option, which is initially five years. For example, the Council cannot – without the JV LLP's agreement – sell that site to another party, or otherwise redevelop it.

12.1.2 The value of land within these option agreements is to be determined, as noted in 4.2.1(f) earlier in this report, at the time the option is exercised. This will be by an independent property valuer, working to an industry standard methodology.

12.2 Office Consolidation

12.2.1 As the February 2014 Cabinet Report noted, the Council has changed considerably in size and nature in recent years as it has moved increasingly towards a commissioning model, and employee headcount has reduced significantly. The Council recognises that its office needs have not kept pace with these changes and office consolidation could provide more efficient accommodation for employees, improved energy efficiency and the potential for cost savings in the long-term. In particular the current office estate has costly maintenance requirements and whilst the Council's current 10 year capital programme includes some funding for maintenance, the likely investment needed over the next 25 years would be considerably higher.

12.2.2 There will be a number of pieces of work that the Council will need to complete for it to properly understand its office requirements going forward, and this will need to be done so that it can take only as much space in new offices as it needs, minimising future costs, and to ensure the new offices integrate well into the Council's strategic approach for service delivery going forward.

12.2.3 This work will include elements like the Council developing its workforce planning strategy and reviewing its customer access strategy. This work will necessarily involve some cost for the Council, but it is important to understand that establishing / reviewing these strategies are good practice and would be undertaken regardless of office consolidation. Funding for this work will need to be identified, and is likely to be provided on an invest to save basis from the Council's capital fund or capacity building reserve.

12.2.4 Subject to the approval of this report, when the JV LLP exercised an option agreement on Fletton Quays with a project that included office accommodation, it would trigger an Agreement for Lease between the Council and the JV LLP. By entering into this Agreement, the Council would be agreeing to lease new offices on Fletton Quays once they were built.

12.2.5 It is important to understand that the Council is in control of whether this happens. The option agreement can only be triggered if there is a project plan agreed that requires the land in that option agreement, and the Council has to agree all project plans. If the Council does not agree a project plan, the relevant option agreement cannot be triggered.

12.2.6 This project plan agreement has to take place not only at the JV LLP Board, but also as a shareholder member of the JV LLP through the Council's normal governance processes. For the avoidance of doubt, this means that the Agreement for Lease is – in effect – contingent upon an approved CMDN for the relevant project plan going through the Council's standard governance process, open to scrutiny in the usual way.

12.2.7 It remains the case that the Council would only want to approve this course of action and enter into the Agreement for Lease if the financial model underpinning this consolidation proves *at worst* cost-neutral for the Council. In short, consolidation only goes ahead and the Council only enters into the lease if it makes financial sense for the Council to do so.

13. DECLARATIONS / CONFLICTS OF INTEREST & DISPENSATIONS GRANTED

Declarations by any cabinet member consulted by the decision maker and any dispensation granted by the Audit Committee or Head of Paid Service (Chief Executive). Note, the Audit Committee grants dispensations where the member concerned has a pecuniary interest, whereas the Chief executive may grant a dispensation for these purposes to any cabinet member consulted on these proposals whether by an officer or another individual cabinet member where there is a common law conflict of interest that may not amount to a pecuniary interest under the Regulations.

14. BACKGROUND DOCUMENTS

Used to prepare this report, in accordance with the Local Government (Access to Information) Act 1985) and The Local Authorities (Executive Arrangements) (Meetings and Access to Information) (England) Regulations 2012

None.

APPENDIX 1: Example Gain share for multiple projects

Section 9.2 of the report includes a simple, single project example of how the investment and profit share arrangements would work. With multiple projects (as we expect there to be with the JV), then the profit share is allocated based on the proportion of all loan notes across all projects. An example of this is outlined below (with the simple example repeated first):

1. One project only – as per section 9.2 example

- Assume £1m loan note for PCC and £1m loan note for Lucent SARL
- If £3m is realised on sale of that project then:
    - Profit distribution is calculated on the loan note ratios at time of distribution i.e. 50%/50%
    - Each loan note is paid and the remainder split on the original loan note ratios at distribution. i.e. 50%/50%

2. Two Projects

- Assume Project as above but a second concurrent project with £0.5m PCC and £1m Lucent SARL
- So total loan note ratio council : Lucent sarl are 43%/57%
- If same £3m is realised on project 1 then:
    - Distribution calculated on ratio of values at time of distribution:
    - Loan notes of £1m each applicable to Project 1 are paid but the distribution is paid on ratio of the loan notes at distribution. Ie 43%/57%
- The split is calculated on the total loan pots at the time of distribution - there is then a payment waterfall breaking this down into loan note and proportion of upside

This can be seen below:

	PCC	**Lucent**	**total**
	£m	**£m**	**£m**
Proceeds - project 1 £3m			
loan note payment	1.0	1.0	2.0
profit	0.429	0.571	1.0
total	1.4	1.6	3.0
remaining loan notes	0.5	1.0	1.5
	33.3%	66.7%	
Proceeds - project 2 £3m			
loan note payment	0.5	1.0	1.5
profit	0.5	1.0	1.5
total	1.0	2.0	3.0
Overall			
loan notes	1.5	2.0	3.5
profit	0.9	1.6	2.5
total	**2.4**	**3.6**	**6.0**

In summary, this example would have the following impact:

- Project 1 has a loan note share of 50%/50%
- Project 2 has a loan note share of 33%/67%
- The aggregated share of the two projects is hence 43%/57%
- The impact for allocation of profit is as follows (assuming project 1 completes first, and that each partner takes all cash on completion):
  - Project 1 profit allocated at 43%/57%
  - Project 2 allocated at 33%/67% (we are back to there being one project)

This example this works in Lucent’s favour as they have higher investment across the two projects. It could easily be the other way round.

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<tr><td>Ward Councillors
(if decision is ward specific)</td><td></td><td></td><td></td></tr>
<tr><td>Legal</td><td>Kim Sawyer</td><td>Approved</td><td>20/11/2014</td></tr>
<tr><td>Finance</td><td>Steven Pilsworth</td><td>Approved</td><td>19/11/2014</td></tr>
<tr><td>Democratic Services</td><td>Gemma George</td><td>Approved</td><td>20/11/2014</td></tr>
<tr><td>Procurement Project Director
(if decision is contract/procurement related)</td><td>Andy Cox</td><td>Approved</td><td>20/11/2014</td></tr>
<tr><td>Head of Strategic Property
(if decision is property related)</td><td>Jon Lewis</td><td>Approved</td><td>20/11/2014</td></tr>
<tr><td></td><td>Other Officers / Members</td><td></td><td></td><td></td></tr>
<tr><td>Director's approval
Directors are requested not to sign if the above section is incomplete</td><td colspan="3">Simon Machen</td><td>Date
01/12/2014</td></tr>
<tr><td>Date sent to Cabinet Member <u>if key decision</u></td><td colspan="3">To be inserted by Democratic Services</td><td></td></tr>
<tr><td><u>If key decision</u> – date decision may be taken</td><td colspan="3">To be inserted by Democratic Services</td><td></td></tr>
<tr><td>Cabinet Member approval</td><td colspan="3"></td><td>Date</td></tr>
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Please tick one of the Options</td><td colspan="3">Option 1
I agree with the officer’s reasons for recommending the decision.</td><td></td></tr>
<tr><td colspan="3">Option 2
I agree with the officer’s reasons for recommending the decision and have the following additional comments to make.</td><td></td></tr>
<tr><td colspan="5">Once signed by Director, please pass to Democratic Services. We will contact the Cabinet Member and arrange for signature.</td></tr>
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