

Merton Council Sustainable Communities Overview and Scrutiny Panel



Date: 2 June 2016
Time: 7.15 pm
Venue: Committee rooms C, D & E - Merton Civic Centre, London Road, Morden
SM4 5DX

AGENDA

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|---|---|--------|
| 1 | Apologies for absence | |
| 2 | Declarations of pecuniary interest | |
| 3 | Call-in report of Land at 111 - 127 The Broadway,
SW19 (Known as P4) | 1 - 54 |

**This is a public meeting – members of the public are very welcome to attend.
The meeting room will be open to members of the public from 7.00 p.m.**

For more information about the work of this and other overview and scrutiny panels, please telephone 020 8545 4035 or e-mail scrutiny@merton.gov.uk. Alternatively, visit www.merton.gov.uk/scrutiny

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Sustainable Communities Overview and Scrutiny Panel Membership

Councillors:

Abigail Jones (Chair)
Stan Anderson
David Chung
James Holmes
Najeeb Latif
Russell Makin
John Sargeant
Imran Uddin (Chair)

Substitute Members:

Edward Foley
Janice Howard
Mike Brunt

Note on declarations of interest

Members are advised to declare any Disclosable Pecuniary Interest in any matter to be considered at the meeting. If a pecuniary interest is declared they should withdraw from the meeting room during the whole of the consideration of that matter and must not participate in any vote on that matter. If members consider they should not participate because of a non-pecuniary interest which may give rise to a perception of bias, they should declare this, withdraw and not participate in consideration of the item. For further advice please speak with the Assistant Director of Corporate Governance.

What is Overview and Scrutiny?

Overview and Scrutiny describes the way Merton's scrutiny councillors hold the Council's Executive (the Cabinet) to account to make sure that they take the right decisions for the Borough. Scrutiny panels also carry out reviews of Council services or issues to identify ways the Council can improve or develop new policy to meet the needs of local people. From May 2008, the Overview & Scrutiny Commission and Panels have been restructured and the Panels renamed to reflect the Local Area Agreement strategic themes.

Scrutiny's work falls into four broad areas:

- ⇒ **Call-in:** If three (non-executive) councillors feel that a decision made by the Cabinet is inappropriate they can 'call the decision in' after it has been made to prevent the decision taking immediate effect. They can then interview the Cabinet Member or Council Officers and make recommendations to the decision-maker suggesting improvements.
- ⇒ **Policy Reviews:** The panels carry out detailed, evidence-based assessments of Council services or issues that affect the lives of local people. At the end of the review the panels issue a report setting out their findings and recommendations for improvement and present it to Cabinet and other partner agencies. During the reviews, panels will gather information, evidence and opinions from Council officers, external bodies and organisations and members of the public to help them understand the key issues relating to the review topic.
- ⇒ **One-Off Reviews:** Panels often want to have a quick, one-off review of a topic and will ask Council officers to come and speak to them about a particular service or issue before making recommendations to the Cabinet.
- ⇒ **Scrutiny of Council Documents:** Panels also examine key Council documents, such as the budget, the Business Plan and the Best Value Performance Plan.

Scrutiny panels need the help of local people, partners and community groups to make sure that Merton delivers effective services. If you think there is something that scrutiny should look at, or have views on current reviews being carried out by scrutiny, let us know.

For more information, please contact the Scrutiny Team on 020 8545 4035 or by e-mail on scrutiny@merton.gov.uk. Alternatively, visit www.merton.gov.uk/scrutiny

Committee: Sustainable Communities Overview and Scrutiny Panel

Date: 2 June 2016

Wards: Abbey

Subject: Call-in of Land at 111-127 The Broadway, SW19 (Known as P4 and referred to in this report as “the site”)

Lead officer: James McGinlay, Head of Sustainable Communities

Lead member: Councillor Mark Allison, Deputy Leader and Cabinet Member for Finance

Contact officer: Jacquie Denton, Principal Estate Surveyor,
jacquie.denton@merton.gov.uk, 020 8545 3080

Recommendations:

- A. That the Sustainable Communities Overview and Scrutiny Panel consider the information provided in response to the call-in request and decide whether to:
- Refer the decision back to Cabinet for reconsideration; or
 - Determine that the matter is contrary to the policy and/or budget framework and refer the matter to Full Council; or
 - Decide not to refer the matter back to Cabinet, in which case the decision shall take effect immediately.
-

1 PURPOSE OF REPORT AND EXECUTIVE SUMMARY

- 1.1. This report provides a response to the points raised in the call-in request relating to Cabinet’s decision regarding the site taken on 18 May 2016.

2 DETAILS

- 2.1. The call-in request and documents provided in response to this are appended to this report.

3 ALTERNATIVE OPTIONS

- 3.1. The Council’s constitution requires the Panel to select one of the options listed in recommendation A.

4 CONSULTATION UNDERTAKEN OR PROPOSED

- 4.1. None for the purposes of this covering report.

5 TIMETABLE

- 5.1. None for the purposes of this covering report.

6 FINANCIAL, RESOURCE AND PROPERTY IMPLICATIONS

- 6.1. None for the purposes of this covering report.

- 7 LEGAL AND STATUTORY IMPLICATIONS**
- 7.1. The Council's constitution requires the Panel to select one of the options listed in recommendation A.
- 8 HUMAN RIGHTS, EQUALITIES AND COMMUNITY COHESION IMPLICATIONS**
- 8.1. None for the purposes of this covering report.
- 9 CRIME AND DISORDER IMPLICATIONS**
- 9.1. None for the purposes of this covering report.
- 10 RISK MANAGEMENT AND HEALTH AND SAFETY IMPLICATIONS**
- 10.1. None for the purposes of this covering report.
- 11 APPENDICES – THE FOLLOWING DOCUMENTS ARE TO BE PUBLISHED WITH THIS REPORT AND FORM PART OF THE REPORT**
- Appendix 1: call-in request form
 - Appendix 2: Cabinet Report, 18 May 2016 (exempt report)
 - Appendix 3: report setting out officers' response to the call-in (to follow)
- 12 BACKGROUND PAPERS**
- 12.1. None for the purposes of this covering report.

Merton Council - call-in request form

1. Decision to be called in: (required)

Land at 111-127 The Broadway, SW19 (known as P4).

2. Which of the principles of decision making in Article 13 of the constitution has not been applied? (required)

Required by part 4E Section 16(c)(a)(ii) of the constitution - tick all that apply:

(a) proportionality (i.e. the action must be proportionate to the desired outcome);	
(b) due consultation and the taking of professional advice from officers;	√
(c) respect for human rights and equalities;	
(d) a presumption in favour of openness;	
(e) clarity of aims and desired outcomes;	√
(f) consideration and evaluation of alternatives;	√
(g) irrelevant matters must be ignored.	

3. Desired outcome

Part 4E Section 16(f) of the constitution- select one:

(a) The Panel/Commission to refer the decision back to the decision making person or body for reconsideration, setting out in writing the nature of its concerns.	√
(b) To refer the matter to full Council where the Commission/Panel determines that the decision is contrary to the Policy and/or Budget Framework	
(c) The Panel/Commission to decide not to refer the matter back to the decision making person or body *	
* If you select (c) please explain the purpose of calling in the decision.	

4. Evidence which demonstrates the alleged breach(es) indicated in 2 above (required)

Required by part 4E Section 16(c)(a)(ii) of the constitution:

<p>(a) proportionality (i.e. the action must be proportionate to the desired outcome);</p>	
<p>(b) due consultation and the taking of professional advice from officers;</p> <p>The site is of strategic importance and key to building a creative arts cluster (as identified in Merton's Economic Development Strategy). Yet paragraph 4 makes clear that there has been very little consultation with local groups who would be key to the success or otherwise of this aspiration, such as the New Wimbledon Theatre, Polka Theatre, Wimbledon College of Art and Wimbledon Choral Society. Nor has there been recent consultation with residents living nearby.</p>	
<p>(c) respect for human rights and equalities;</p>	
<p>(d) a presumption in favour of openness;</p>	
<p>(e) clarity of aims and desired outcomes;</p> <p>The council clearly has a duty to deliver best value. However, there is no clarity in the report as to what constitutes best value. Best value may not necessarily be delivered through an outright sale. Nor is there clarity about what might deliver best value for the wider community in and around Wimbledon town centre. Over many years, there has been an aspiration – including by the council - to provide a new community facility as part of any redevelopment of this site to benefit residents and yet this would not be delivered through the proposed outright sale.</p> <p>With regard to financial implications, current pressure is on the council's revenue budget not capital budget and – unlike with a long leasehold geared interest sale for example – an outright freehold sale risks increasing pressure further on the revenue budget as a result of lost future income.</p>	
<p>(f) consideration and evaluation of alternatives;</p> <p>This call-in relates primarily to the due consideration and evaluation of alternatives. Whilst it may be the stated aim of the Administration to maximise the potential of the land at 111-127 The Broadway SW19 (known as "P4"), the Cabinet has failed to demonstrate that</p>	

an outright sale of the property at the price proposed is necessarily maximising its potential.

The last call-in relating to this decision in 2013 was submitted because no valuation had been undertaken of the site. This proved the right decision given the proposed sale proceeds being discussed at that point and the 5-fold amounts now being discussed. The situation, however, has moved on again since 2013 and any decision being made in 2016 must now take into account the current plans for Crossrail 2 which could involve the re-development of part of Wimbledon town centre. It may well be that the proposed sale price already reflects this, but this is by no means clear.

A decision as important as this should not also be accepted on the basis that the Council perceives that it would cause a "loss of reputation" if it "changed its mind" after lengthy discussions. It has to be presumed that a legally binding "verbal agreement" had not been given before official approval of the decision and, therefore, any prospective buyer would understand that a change in circumstance/new information would be taken into account without detriment.

In consideration of the alternative options, Merton Council has failed properly to evaluate these. It is an overly risk-averse decision taken by a Cabinet which has not seriously undertaken any real examination of alternatives, but just wants to "get rid of the land as soon as possible". 3.5 states that "the council is keen to look at retaining property and developing sites to add value". Yet where it has the golden opportunity to do so here with P4, it simply puts obstacles in the way such as "the council does not currently have in-house experience and expertise to carry out such a project", without including any detail of what it would cost in terms of time and/or resources to buy-in or develop such experience and expertise. By focusing solely on the risks of the alternatives, the council shows that it is scared of failure rather than necessarily taking the most beneficial decision for the long term future of Wimbledon and its residents.

3.3 states that the Council would either need to (a) provide the finance for the scheme or (b) seek to let a design, build and finance contract. Taking these in turn

Financing a scheme

No details are provided in the report of what level of financing would be needed for such a scheme and the rate of interest at which this funding could be borrowed.

3.3 highlights the risk of a "speculative development" whereas 6.5 notes "the current confidence in the Wimbledon office market".

If the market is speculative, then surely it would be better to be in control of the development, than risk the developer coming back in a year's time (after planning permission has been granted and the

building sold) saying that it can't find tenants and requesting change of use to residential for example (as happened with the development on Hartfield Road, stating that the building was "too far away from the station"). This risk has not been included in the paper.

No valuation on a lease of an office block with vacant possession has been undertaken; nor of current rental amounts which could be earned. The paper highlights the business rates that could be generated, but these would still accrue to the Council in either of the 2 alternative scenarios.

Based on the range of valuations received; planning permission itself appears to be worth an additional £3million. If the Council was in control of a development which could provide the "high quality" being sought in 3.5, then it would be likely to be given planning permission.

Letting a design, build and finance contract

The paper talks about the amount of time this would take. This option has not seriously been considered as an alternative as the council have had since 2013 to test the market to see if this would be attractive. Given the fact that there were 114 registered interests and 17 offers received; there is obviously considerable interest in this site in the market.

Again, no costing has been given to benchmark against an outright sale.

No detail is given in the report about the potential benefits of a Long Leasehold Geared Interest sale. The site could be sold subject to a 150 year lease for example with the council retaining the freehold. This would generate a year on year return for the council which could more than offset the loss of parking revenue whilst the council would also retain additional control over the development. The option would still remain to sell the freehold interest at a future date.

5. Documents requested

- Any internal or external discussions or costing on what expertise would be needed and possible exploratory discussions with 3rd parties to underpin comments made in para 3.2 of the report.
- All minutes and documentation relating to any discussions held with other Councils that have formed a joint venture to develop property sites.
- Evidence to substantiate the differing timescales expected for the various options (outright sale; financing a scheme; design build and finance)
- Full costings and risk analyses for the following options:
 - a) Freehold sale of the land
 - b) Long annuity income receipt
 - c) Joint Venture
 - d) Council develops land directly

- Details of the latest utilisation rates for the P4 car park compared to other car parks in Wimbledon town centre.
- Forecasts for capital appreciation of the site over the next 5, 10 and 20 years
- Details of any 'non embarrassment' clause proposed as part of the contract to avoid the purchaser 'flipping' the asset at a profit

6. Witnesses requested

- "Expert" on joint ventures who could talk through the options, risks and opportunities of such an approach.
- Andrew Scott Robertson to discuss current market conditions and medium-term expectations.
- Former Abbey Ward Councillor; Diane Neil Mills
- Director of Environment and Regeneration, Chris Lee
- Head of Sustainable Communities, James McGinlay
- Property Management and Review Manager, Howard Joy
- General Manager of the New Wimbledon Theatre
- Chairman or Representative of the Wimbledon Broadway Car Park Action Group (which previously submitted an application to list the site as an 'asset of community value')

7. Signed (not required if sent by email): in alphabetical order:

Cllr Michael Bull, Cllr Suzanne Grocott, Cllr Daniel Holden, Cllr David Williams

8. Notes

Call-ins must be supported by at least three members of the Council (Part 4E Section 16(c)(a)(i))

The call in form and supporting requests must be received by 12 Noon on the third working day following the publication of the decision (Part 4E Section 16(c)(a)(iii)).

The form and/or supporting requests must be sent **EITHER** by email from a Councillor's email account (no signature required) to democratic.services@merton.gov.uk **OR** as a signed paper copy (Part 4E Section 16(c)(a)(iv)) to the Assistant Head of Democracy, 5th floor, Civic Centre, London Road, Morden SM4 5DX. For further information or advice contact the Assistant Head of Democracy on 020 8545 3361

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By virtue of paragraph(s) 3 of Part 1 of Schedule 12A
of the Local Government Act 1972.

Document is Restricted

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Local Authority Land Sale

Discussion Document - 2nd June 2016

Jeff Morton MRICS

Jeff Morton - MRICS - Executive Career & Credentials - Investment Management

Transactional - Investment Management Experience

- 28 years industry experience having transacted in excess of £2.50bn sales and acquisitions over last 10 years.

Employment

Henley Investments 2012 - June 2016 - Then Consultant - Pure Global Capital

- Chief Operating Officer, Equity Partner and Investor for private real estate vehicle of \$1.20bn GAV investing UK, Germany & Holland.

BlackRock 2006 - 2012

- Managing Director and Head of Investment - Transactions & Asset Management for £3.00bn BlackRock UK Property Fund.

Merrill Lynch Investment Managers 2004 - 2006

- Director: Head of Asset Management and Transactions for £2.00bn MLIM UK Property Fund.

Central London Securities CLS Holdings plc 2002 - 2003

- Director: Head of UK Property. Listed company valued at circa £725m.

Hemingway Properties plc 1999 - 2001

- Director: Head of Asset Management for property company circa £300m AUM.

Haslemere Estates plc 1988 - 1999

- Transactions and Asset Manager for property company circa £1.00bn AUM.

Past Executive Directorships

- Premier Marinas Holdings. Eight UK marinas comprising 5,500 berths south coast.

(1) Existing Asset Management Considerations (Three Main Scenarios)

- a) **Hold** - Potential cost implications but revenue is retained
- b) **Sell** - Capital receipt received
- c) **Joint Venture** - Several types to consider

(2) Timing

- a) Need to confirm that the asset is not required for operational or investment purposes
- b) Understand why are the LA are selling and is timing of sale “Business Critical”
- c) Are previous policy decisions determining current action and is this still the best course of action
- d) **Is the market operating as it should be or are there potentially negative factors influencing value and currently a good example is Brexit**
- e) Is the market likely to change over next 12 months positively or negatively?
- f) If negative i.e. values are falling, is it compelling to sell now or justifiable to “wait and see”

(3) Legal

- a) What restraints if any are the LA under in terms of selling
- b) Is the only real alternative an open market sale so as to ensure best price/value is achieved
- c) What constitutes best value - is it highest price or other factors

(4) Reputational

- a) If deciding a JV is a suitable alternative choosing the wrong partner and many other factors could lead to both reputational and financial risks
- b) Need to be careful to avoid conflicts of interest
- c) Withdrawing from any deal or process should be considered responsibly

(5) Summary Outcomes

- a) **Hold** - Self-manage existing asset but LA unlikely to maximize potential value due to non-development expertise within in-house skill set
- b) **Sell - Open Market - Auction / Private Treaty** - Object is to get best price and delivery of scheme that is appropriate for site and community - Likely to sell with firm guidelines as to what planning uses are acceptable to include size, constraints, heights, massing etc.
- c) **Include a 'non embarrassment' clause to avoid purchaser 'flipping' asset at a profit - or potentially include overage provisions - however overage reduces price**
- d) Widest exposure definitely satisfies questions around whether best price is achieved - planning outstanding - gives further element of control - but not full control
- e) Dependent on timing constraints, could sell on a subject to planning basis = longer wait for receipts but potentially achieves a higher price
- f) Private Sector "generally" seeks to maximize returns and is less interested in niceties such as aesthetics, quality of materials but fully focused on profitability
- g) **Joint Ventures** - Provides an alternative mechanism for capturing longer term

value as the LA will hold an equity stake in the JV

- h) Possible to obtain a non-monetary gain if that is a potential objective (e.g. JV partner to develop new council/neighbourhood premises at their cost)

(6) Typical Buyers

- a) The current market is very difficult for developers and obtaining development finance is particularly tough and an expensive cost for investment appraisals
- b) This site I would speculate should attract interest from major developers and REITS but is likely to be sought after by UK Funds who have the lowest cost of capital and would be seeking higher returns through developments often with third party partners
- c) Typically Funds such as Hermes, BlackRock, Aviva, Standard Life, Threadneedle, Prudential, Rockspring, AEW, L&G etc would consider such exposure albeit Brexit may have had an effect on value.
- d) Is it possible for the LA to JV with Funds or REITS and others that have the necessary development expertise.
- e) Limited demand for speculative development or land-banking at current time.

(7) Sale Types

- a) Freehold Sale V Long Leasehold Geared Interest.

Freehold

- b) Say the site is worth £20m then this is the gross proceeds less costs. 'Day 1' receipt typically.

Leasehold Geared Interest

- c) What if the site is worth £20m and sold not freehold but subject to a 150-year lease with the LA retaining the Freehold

- d) The 150 year lease could be “geared” at say 10% of rent passing (side by side v non side by side - important gearing is not too high
- e) Potentially subject to a minimum base rent say of passing rent of 2.5% per annum or fixed base rent it’s all negotiable
- f) Gearing / ground rent can be set to suit LA depending on whether initial capital receipts or future income is most important
- g) If site is worth say £20m residual value the Gross Development Value very high level is £60m. Keeping numbers at this very high level a 5% gross yield provides an income to the developer of £3m per annum
- h) The above assumes all commercial in this illustration when in reality the subject site will be mixed use thus including residential and ground rent income
- i) The LA could negotiate to keep the Ground Rent income which is very valuable and a liquid investment cap yield $3.50\% - 4.00\% = 25 \times$ ground rent income
- j) Say LA accept minimum base of 2.00% and the market can absorb this “ratchet” that’s £60k per annum of revenue
- k) Potential to sell the freehold interest at a future date for a capital receipt
- l) Maximum of £300k per annum revenue on the above illustrative figures at 10%
- m) In addition to the income there is the capital receipt from the sale (although logically this figure is lower than freehold but does depend on competition

(8) Some Factors to Consider

- a) What is the reduction in liquidity if any by selling Leasehold rather than

Freehold

- b) Likely to be dependent on the nature of the planning title and any covenants imposed but all of these are within the LA gift to make these flexible (within reason)
- c) What is the **reduction in price if any** by selling Leasehold rather than Freehold
- d) The sale of leasehold geared interests is very common for offices as it is for other asset classes. This is best illustrated by the sale of such interests by the large landowners in central London such as The Grosvenor Estate, The City Corporation, The Cadogan Estate, Howard De Walden Estate and the numerous Livery Companies to name but a few.
- e) What are the benefits in having the reversion of the land at expiry to the LA
- f) What are the accounting implications if any
- g) What are the wider benefits to the LA in having additional control
- h) The LA has excellent borrowing power and possibly cash surplus thus the cost of borrowing is typically below market levels and could be a profit centre if lending at a higher rate than current cost with the loan secured against the asset.

(9) Simple JV Illustration

- a) LA Contributes land with planning audit and detailed advice - Land value based on third party valuation
- b) Partner contributes procurement expertise and delivery management etc
- c) Profits - Typically apportioned 50% - 50% but can be structured numerous ways but important both sides are motivated to succeed

- d) In every deal its essential to determine and show explicitly the relative equity being put into the deal by each party.
- e) Value of LA land relatively easy, JV partner share based on build cost for example but is it up front or deferred etc
- f) Typically, the party injecting the greater/highest amount of equity gets the greatest rewards or highest profits thus parity is important
- g) The LA borrows at low rates and may even have cash reserves thus can lend the project at higher rates for superior returns could be outside of arrangement
- h) Existing LA debt may be in place at higher LA market levels and capital receipts pay down liability
- i) End profits shared as agreed apportioned typically on sale - not uncommon for JV Partners to have a pre-emption on sale but again liquidity affected.
- j) Detailed documentation and expertise required to administer the process

(10) Risk - Reward Scenario Summary - Conclusions & Recommendations

1. **Lowest Risk > Potentially Lowest Price > Highest certainty of sale = Freehold sale of land with negligible planning conditions. Timing & Cost Consideration - Nil delay & no additional costs other than those currently allowed for.**
2. **Lower Middle Risk > Potentially Geared Leasehold Sale = Possibly lower price but retains valuable ground rent income which in turn could be sold in the future > Provides long term annuity income and retains an element of control on design etc. Timing & Cost Consideration - Initial view from independent third party supplier to interrogate & validate this advice 10 - 15 working days and at negligible costs. If sale route**

progressed standard fee at 1% of contract price - no post sale ongoing fees anticipated.

3. Higher Middle Risk > Joint Venture > Potential trips & traps not least crucial to choose a good partner and prepare first class documentation and detailed brief > increased risk but shares in expected upside profitability as aligned with partner and scheme will inevitably be enhanced in design and value engineered thus GDV higher than currently anticipated. Retains increased control on design etc. = Potentially higher rewards. Timing & Cost Consideration Initial view from independent third party supplier to interrogate & validate this advice 10 - 15 working days and at negligible costs. If JV route progressed standard fee at 1% of contract price - with some post sale ongoing fees required.

4. Highest Risk > LA Develop Direct > Potentially greatest profit & definitely greatest risks and thus not a recommended route.

(10) Third Party Advisory & Recommendation

- a) *Option 2 - 3 All need careful third party advisory input which involve initially negligible costs up front and minimal time delay 10- 15 days to validate. Progression of option 3 involves increased time and costs up front but with appraisals undertaken potential profit is higher - ongoing fee costs required.*
- b) *For the avoidance of doubt Jeff Morton is not retained by anyone and has no fee proposed or agreed. He has no financial interests in the site or indeed anything within the LA area. This report offers no warranty or liability it is merely the authors opinion who is acting in good faith and as a good corporate citizen for the benefit of others.*

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