


<p><b>London Borough of Hammersmith &amp; Fulham</b></p> <p><b>CABINET</b></p> <p><b>8 FEBRUARY 2016</b></p>	
<p><b>VARIATION TO THE STRUCTURE AND CONTRACTUAL TERMS OF THE JOINT VENTURE VEHICLE</b></p>	
<p><b>Report of the Cabinet Member for Economic Development and Regeneration, Councillor Andrew Jones and the Cabinet Member for Housing, Councillor Lisa Homan</b></p>	
<p><b>Open Report</b></p> <p>A separate report on the exempt part of the Cabinet agenda provides exempt financial information.</p>	
<p><b>Classification - For Decision</b></p> <p><b>Key Decision: YES</b></p>	
<p><b>Wards Affected: All</b></p>	
<p><b>Accountable Director:</b> Juliemma McLoughlin, Director for Planning &amp; Growth</p>	
<p><b>Report Author:</b> Matthew Doman, Development Manager</p>	<p><b>Contact Details:</b>  Tel: 020 8753 4547  E-mail:  matthew.doman@lbhf.gov.uk</p>

## 1. EXECUTIVE SUMMARY

- 1.1. The Council established HFS Developments LLP as a joint venture vehicle with Stanhope Plc in March 2014 and entered into contractual documentation relating to the governance and business of HFS Developments LLP (the “LLP” or “JV”) at such time.
- 1.2. This report requests approval for the following:
  - for the Council, as a Member of the LLP, to take such actions as are necessary to wind up the LLP and for the Council to take such actions as are necessary to establish a new company limited by shares (the “New Company”) in its place, with the Council becoming a shareholder in the New Company alongside Stanhope Plc;

- to approve the amended Site Specific Development Plan for Edith Summerskill House (“ESH”) such that they can be adopted by the LLP (or, if applicable, the New Company);
- for the Council to take such actions as are necessary to approve the allocation of affordable housing grant funding to enable the redevelopment of ESH;
- for the Council to take such actions as are necessary to terminate the contractual documentation entered into with the LLP and enter into new contractual arrangements with the New Company with such variations as are required to enable the development of ESH by a Registered Provider of affordable housing (RP), and other variations, including a contractual obligation on the Council to reimburse the New Company for costs associated with meeting the conditions at ESH in the unlikely event that the Council withdraws the allocation of affordable housing grant funding referred to above;
- to approve the allocation of additional funds to complete the decant process of ESH and the demolition of WMC;
- to approve the undertaking of the necessary steps required to carry out and complete the demolition of ESH.

## **2. RECOMMENDATIONS**

- 2.1. That approval be given for the Council to take such actions as are necessary to wind up the LLP and to establish a new company, with the Council becoming a shareholder in the New Company alongside Stanhope Plc.
- 2.2. That delegated approval be granted to the Cabinet Member for Economic Development and Regeneration, in conjunction with the Director for Planning and Growth to enable the appointment of the Council’s directors to the New Company and any other decision that is required so as to effect the foregoing recommendations, including the approval of any amendments to existing contracts, termination of existing contracts and approval of new contracts required to effect the foregoing.
- 2.3. That the revised SSDP ESH, as set out at Appendix 1 of the exempt report on the exempt Cabinet agenda, be approved so they can be adopted by the LLP (or, if applicable, the New Company).
- 2.4. That approval for the appointment by the Council (as a member or shareholder of the JV) of an RP partner by the JV be delegated to the Cabinet Member for Economic Development and Regeneration in conjunction with the Director for Planning and Growth and the Lead Directors of Housing.

- 2.5. That approval be given for the Council to directly undertake the demolition of ESH.
- 2.6. That approval be given to undertake a procurement exercise to appoint a demolition contractor to undertake the demolition of ESH.
- 2.7. That approval for the appointment of the demolition contractor and any consultant appointments required in respect of the demolition of ESH be delegated to the Cabinet Member for Economic Development and Regeneration in conjunction with the Director for Planning and Growth.
- 2.8. That approval be given to the Council providing a contractual obligation to reimburse the JV its costs (capped at £2m for ESH and £2.5m for WMC) for fees incurred in achieving planning consent in the unlikely event that the opportunity sites are not redeveloped. In this scenario the land will be returned to the Council free from adverse rights and with detailed planning consent.
- 2.9. That approval be given for the Council to incur additional consultancy fees for ongoing legal and professional advice as set out below:

Legal Advice	£100,000
Valuation Advice	£ 75,000
Financial Advice	£ 10,000
Other Professional Advice	£ 15,000

As costs incidental to the disposal of assets, these may be offset against capital receipts that ensue.

- 2.10. That approval to incur any additional fees in relation to the Council meeting its obligations under the terms of the conditional JV agreement be delegated to the Cabinet Member for Economic Development and Regeneration, in conjunction with the Director for Planning and Growth and the Lead Directors of Housing as Edith Summerskill House is designated as Housing Land.
- 2.11. To note that if negotiations with remaining leaseholders at ESH prove unsuccessful a compulsory purchase order (CPO) will be required to facilitate development.

### **3. REASONS FOR DECISION**

- 3.1 To remedy the funding issues encountered as a result of competing QC opinions on whether the Council's power to participate in the JV with Stanhope Plc via a limited liability partnership (i.e. HFS Developments LLP) presents a material risk of the transaction being challenged.
- 3.2 Approval by the Council of the revised SSDP is required under the existing contractual documentation relating to the JV.

- 3.3 To make amendments to the contractual documents as a result of the revised development proposals currently being contemplated by the JV which require approval by the Council.
- 3.4 The JV requires certainty that funding will be available to enable them to commit funds to satisfying the conditions required to bring forward the development.
- 3.5 The appraisals carried out by the JV indicate that ESH will require a significant amount of grant funding in order to deliver a 100% affordable development.
- 3.6 By undertaking the demolition of ESH the Council is able to:
- remove some of the development risk that could potentially affect delivery;
  - potentially accelerate delivery as it can bring forward the demolition; and
  - make cost savings as the Council will be able to recover the VAT associated with the demolition works.

#### **4. INTRODUCTION AND BACKGROUND**

- 4.1 On 28 March 2014 various agreements were entered into between the Council, Stanhope Plc (“Stanhope”), HFH Ventures UK Limited and HFS Developments LLP (“the Agreements”).
- 4.2 The purpose of these arrangements was to appoint a private sector partner to participate in the redevelopment of council owned sites for the provision of new housing over a 15 year period. The first sites to be developed are sites known as Watermeadow Court (“WMC”) and Edith Summerskill House (“ESH”). The Agreements also envisage further sites (“future sites”) to be identified for possible development as the project progresses.
- 4.3 The Agreements were conditional on a number of matters, including the JV securing funding. The Conditional Joint Venture Agreement entered into between the Council, Stanhope, HFH Ventures UK Limited and HFS Developments LLP also allows for an opportunity site to be transferred to a third party once such conditions are satisfied where the parties agree to do so.
- 4.4 Since the Agreements were entered into, the following matters have arisen:
- i. the Council and Stanhope have discussed the principle of varying the existing JV arrangements to enable 100% affordable housing

to be provided at ESH, on the basis that this will allow an overall greater number of affordable housing to be achieved by the JV. A corresponding reduction of affordable housing is now envisaged at WMC with a commuted sum to be required from the JV in lieu of such provision to enable planning requirements to be met.

- ii. the parties have agreed in principle that a Registered Provider (“RP”) be appointed by the JV to deliver the development of ESH;
- iii. It is proposed that the funding of the delivery of ESH by the RP be funded by grant funding and the Council will (subject to the RP satisfying the necessary statutory requirements for the provision of such funds) either provide the funding, or where it unilaterally withdraws such funding, reimburse the JV’s costs reasonably incurred in respect of satisfying the conditionality in the Sale Agreements (capped at £2m ESH and £2.5m for WMC). In the event of the latter ESH and WMC will return to Council ownership.
- iv. the Council and Stanhope wish to wind up the LLP and establish the New Company

## **5. PROPOSAL AND ISSUES**

The changes to the JV arrangements raise specific issues that need to be carefully considered. These are summarised below:

### **5.1 Changes to the JV Structure**

The Agreements currently envisage delivery of specified “opportunity sites” by the JV constituted as a Limited Liability Partnership. The Agreements include a number of conditions, one of which is a funding condition, so that the JV has to secure funding for the development of the relevant Opportunity Site. Following exchange of the Conditional Joint Venture Agreement, in the JV’s discussions with a potential funder, the funder raised a concern as to whether the Council was permitted to enter into an LLP structure. Whilst the Council’s legal advisors have advised that an LLP structure was permitted, in order to avoid this concern being raised by other funders in the future, the parties wish to change the structure at this stage so that the JV is constituted as a company. Therefore, the proposal is that HFS Developments LLP is wound up and a New Company (constituted with the Council and Stanhope as 50/50 Shareholders) is formed and which will take the place of the LLP going forward.

### **5.2 Changes to the Conditional Period in the Agreement and consequential amendments to the Agreement**

To allow for the revised planning approach, and mitigate risk of a planning application refusal, it is proposed that the conditional period of the Agreement be extended. Further provision that allows for reversion to the

initial approach in relation to affordable housing in the event that planning is not achieved is also proposed (40% affordable housing on either site)

### **5.3 Changes to the approach to the delivery of Affordable Units**

The SSDPs for both ESH and WMC envisage affordable housing being delivered at both ESH and WMC in accordance with the Council's usual minimum requirements of 40% affordable housing delivery. It is now proposed that the SSDPs be varied so that ESH is to be developed for 100% affordable housing. WMC will be developed for 100% open market housing with no on-site affordable provision but it is proposed that a commuted sum payment be made to facilitate the delivery of the off-site affordable housing at ESH.

### **5.4 Appointment of the RP**

The proposal is that the delivery of the affordable housing at ESH is to be delivered by an RP appointed by the JV. The Agreement permits the transfer of an Opportunity Site (and the novation of the Agreement) to a third party approved by the parties.

It is proposed that the JV appoint the RP via a procurement process that is in accordance with the procurement policy agreed by the JV partners.

## **6. OPTIONS AND ANALYSIS OF OPTIONS**

6.1 The options considered for the delivery of new affordable housing on WMC and ESH were:

1. Retain the existing SSDPs which propose a mix of private sale and discount market sale units on both ESH and WMC with all units being developed and sold by the JV.
2. To change the affordable element on both ESH and WMC to social rent in line with the Council's new housing strategy.
3. To change the tenure mix to 100% market sale on WMC and 100% social rent on ESH with ESH reverting to Council ownership and the social rent units being let and managed by the Council.
4. To change the tenure mix to 100% market sale on WMC and 100% social rent on ESH with ESH being transferred to an RP who will own and manage the building.

### **RETAIN EXISTING SSDPs**

6.2 The existing SSDPs contain a tenure split of 60% private market sale and 40% discount market sale units for both WMC and ESH. This approach

no longer meets the Council's affordable housing strategic objects where the provision of social rent housing is to be prioritised.

### **CHANGE TENURE**

- 6.3 Changing the tenure of the affordable units on both WMC and ESH to social rent was considered however the impact on viability for both schemes as a result of the cost of providing the necessary social units meant that the number of affordable units would have been significantly reduced.
- 6.4 In addition, as ESH is to be a tower block development, a mixed tenure approach that includes 40% social rent would create design problems which would impact on the overall number of units that could be delivered. Other issues raised included that it could be more difficult to attract private buyers as a result of the high proportion of social rent tenants; that the market value of the units for private sale would be greatly reduced which would affect the number of affordable units the scheme could support; and the ability of purchasers to find mortgage providers would also be affected.

### **SINGLE TENURE APPROACH**

- 6.5 In order to maximise the provision of social rent a single tenure approach to both WMC and ESH has been considered. Due to the fact that ESH is better serviced by transport and amenities, and the fact that greater sales figures can be generated at WMC the proposal is that ESH delivers 100% affordable homes and WMC 100% private sales.
- 6.6 Early discussions with the GLA have suggested that a tower containing 100% social rent units is unacceptable therefore an approach that includes intermediate rent is being proposed. Currently the proposal is for 80% social rent and 20% intermediate rent but that is subject to planning and agreement with the GLA.

### **COUNCIL RETAINS ESH**

- 6.7 For the Council to retain ESH the JV will have to develop the site with grant funding being provided by the Council to fund the net cost of construction. The Council's legal advice suggests that although not prohibited under State Aid rules this approach does carry a greater risk than if the Council were to grant fund an RP.
- 6.8 This approach is also likely to necessitate the need for the Council to borrow funds, albeit on a relatively short term basis, in order to complete the development which may not be possible due to the capital funding restrictions created by the Housing Revenue Account Debt cap. The Council would also have to bear the development risk under this approach.

## **TRANSFER TO AN RP**

- 6.9 If ESH is transferred to an RP the RP will be responsible for the development and the risk is transferred from the JV to the RP.
- 6.10 The Council will be able to grant fund the RP to cover the net cost of delivering the completed scheme as 100% affordable.
- 6.11 The Council will retain 100% nomination rights and will be able to restrict the tenure and rent levels charged. Currently the proposal is for 80% social rent and 20% intermediate rent but that is subject to planning and agreement with the GLA.
- 6.12 The RP will be responsible for the maintenance and management of the building.

## **7. CONSULTATION**

- 7.1 The proposals included within this report have been reached after detailed consultation was undertaken with Cabinet Members and legal advisors.

## **8. EQUALITY IMPLICATIONS**

- 8.1 An Equality Impact Assessment was completed prior to the creation of the JV which established that due to the procurement process undertaken by the Council to appoint a private sector partner and to dispose of the opportunity sites, there are no negative equality implications.
- 8.2 The redevelopment of the opportunity sites has a number of positive equality implications as the existing properties have been vacant for a number of years and the buildings are largely uninhabitable. The new developments will increase the supply of new homes in the Borough with a mix of Social and Intermediate Rent and private market sales.
- 8.3 Implications verified/completed by: Matthew Doman, Development Manager, Planning and Growth x4547.

## **9. PLANNING IMPLICATIONS**

- 9.1 The S106 contributions that are required to enable the redevelopment of the Council owned sites specified for affordable housing purposes would be an appropriate use of the funds, as they were secured for either affordable housing or social and physical infrastructure purposes in the Borough. The timetable for payment/receipt of the funds is considered to be realistic and the triggers for payment will be monitored.
- 9.2 Implications verified/completed by: Peter Kemp, Planning Change Manager, Planning and Growth, x6970
- 9.3 Under the provisions in the Town and Country Planning (Mayor of London) Order 2008 the planning applications would be referable to the



Mayor and planning permission cannot be issued without his direction to do so. The Mayor has the discretion on referrals to direct refusal or 'call-in' the application for his determination. This potentially increases the planning risk.

- 9.4 The London Plan seeks the creation of mixed and balanced communities by delivering a range of tenures on each development. In light of this the Mayor requires the maximum reasonable amount of affordable housing to be provided on-site (40% minimum in LBHF), unless exceptional circumstances exist. A contribution in lieu of on-site provision should only be accepted where this would have significant benefits to affordable housing delivery. There will need to be robust justification to demonstrate that there are exceptional reasons for accepting the contribution in lieu of on-site provision.
- 9.5 The WMC planning application would need to be supported by a Viability Assessment to demonstrate that the financial contribution is the maximum reasonable amount that the development can afford. This would need to be assessed by an independent viability assessor on behalf of the Local Planning Authority.
- 9.6 Any planning permission at WMC would be subject to a Section 106 Agreement and would include clauses to ensure that the financial contribution could only be used for affordable housing delivery in the Borough. To reduce planning risk it may be necessary to link the two developments in the Section 106 as part of demonstrating the exceptional case for accepting the contribution in lieu of on-site affordable provision at WMC.
- 9.7 The proposed affordable tenure split of 80% social rent and 20% intermediate at ESH would more closely align with the London Plan requirements.
- 9.8 Implications verified/completed by: Steven Roberts, Principal Complex Applications Officer, Planning and Growth, x3315.

## **10. LEGAL IMPLICATIONS**

- 10.1 The proposed changes to the Agreement raise the following legal implications (please note procurement implications are addressed in section 13 below):

### **STATE AID**

- 10.2 Consideration has been given to potential State Aid implications that may result from the change in approach. Issues are likely to arise at two levels, these being as follows:

- at the level of the JV on the basis that it is being alleviated of planning obligations that would normally be imposed on developments of this nature; and
- at the level of the RP in relation to payments to be made by the Council to cover the cost of social housing that will be in the ownership of the RP.

10.3 State Aid rules require the application of State resources, which can include planning requirements for the delivery of social housing as part of any development, to be undertaken in a manner that ensures no additional benefit is gained by the party in receipt of the resource.

10.4 Where there is to be a commuted sum rather than the on-site provision of social housing, even if at a rate equal to the costs of delivering such social housing, there may still be a benefit to the developer due to an increase in value resulting from the absence of affordable housing. This could raise potential arguments that the Council is waiving usual planning requirements due to its involvement in the JV.

10.5 The Council will need to be satisfied that the commuted sum applied to WMC is at a level that negates any benefit from not only alleviation of the cost of providing 100% affordable housing at ESH, but also the increase in the value of WMC due to it having no social housing. It is essential that there is a clear audit trail setting out its decision making to show this is in line with planning legislation.

10.6 Services of general economic interest (SGEI) are economic activities that public authorities identify as being of particular importance to citizens and that would not be supplied (or would be supplied under different conditions) if there were no public intervention. The provision of social housing can be regarded as a public service obligation and funding the RP to compensate for the costs of delivery is permitted and does not constitute State Aid if applied correctly. This includes where the compensation is limited to the “net costs” of performance of the SGEI.

10.7 The Council needs to show that the recipient of the grant funding under the SGEI is not being overcompensated as a result of its delivery. Scrutiny of grant applications and the provision for reconciliation during the SGEI should mitigate this.

10.8 Eversheds has provided advice on the applicable rules and any funding agreement between parties will be drafted so as to comply with the requirements of the SGEI Decision.

10.9 Implications verified/completed by: Tim London, Solicitor at Eversheds

## **VIRES**

- 10.10 In order to fund the two opportunity sites Stanhope Plc had secured funding from HFH UK Ventures Limited (AIMCo) subject to conditions being met. Following entering into the Conditional Joint Venture Agreement AIMCo exercised its right to take advice on whether, in creating the LLP, the Council had acted ultra vires
- 10.11 AIMCo received Counsel advice from David Elvin QC stating that in his opinion the creation of the LLP posed a material risk of the transaction being set aside as the Council had acted ultra vires in entering into such arrangements.
- 10.12 Eversheds recommended a second opinion be sought. In his opinion, received on 17<sup>th</sup> June 2015, James Goudie QC refutes Elvin's claims and confirms that because the purpose of the transaction was housing and regeneration, rather than a commercial purpose, the Council had acted intra vires and it was not necessary to establish a company for the delivery of the Council's objectives.
- 10.13 Goudie's opinion confirms the advice received from Eversheds prior to entering into contract arrangements however, as a result of the competing Counsel opinions, the Council and Stanhope consider that the best way to move forward is to wind up the LLP and create a company. The reason for doing this is to remove any uncertainty potential funders may have as a result of competing views on the issue.
- 10.14 The legal basis for the revised structure covering both the substantive proposal and the methodology is
1. The powers in relation to housing and regeneration contained in the Housing Act 1985 and the Town and Country Planning Act 1990
  2. The powers of land disposal contained in the Local Government Act 1972 including the obligation to secure the best consideration reasonably obtainable.
  3. The ancillary powers contained in section 111 of the Local Government Act 1972
  4. The power of general competence contained in section 1 of the Localism Act
  5. The powers contained in the Local Government Finance Act 2003
- 10.15 Implications verified/completed by: Denis Cooper, Solicitor at Eversheds

## **11. FINANCIAL AND RESOURCES IMPLICATIONS**

- 11.1 As set out in the exempt report on the exempt Cabinet agenda.

## **12. RISK MANAGEMENT**

- 12.1 The risks in relation to a procurement challenge are set out in section 13 below. Eversheds is providing advice on how to mitigate potential risk items and contract amendments will be kept to a minimum to limit challenge.
- 12.2 The risk that the JV is unable to achieved detailed planning consent on the revised SSDP proposals will be mitigated as follows:
- i. Detailed discussions with planning officers and the GLA are and will be undertaken in order to reach an acceptable position prior to the submission of a planning application.
  - ii. It is proposed that a commuted sum payment for WMC in lieu of the onsite provision of affordable housing be made to allow for 100% private housing at WMC. This commuted some can contribute to the cost of provision at ESH or be used for additional affordable housing within the Borough.
  - iii. An extension to the conditional period to allow for revised planning approach is also proposed. This will enable an appeal or reversion to the original affordable housing proposals if planning permission is refused.
- 12.3 Financial risks are identified in section 11 and will be closely monitored throughout the project cycle.
- 12.4 The risks in relation to State Aid are covered in section 10. Eversheds is advising on this matter and the funding agreement will be drawn up to meet the necessary obligations.
- 12.5 There is also a risk that, should the land be transferred, the selected RP fails to deliver in accordance with the development obligations placed upon it in relation to ESH. This risk will be mitigated by the JV undertaking a robust procurement exercise to ensure that the selected RP partner has a significant track record of similar successfully completed development schemes and the financial and technical capabilities to undertake the project. There is also provision that if the RP is unable to deliver the JV can step in and complete the development.
- 12.6 Implications verified/completed by: (Matthew Doman, Development Manager, Planning and Growth, x4547).

## **13. PROCUREMENT IMPLICATIONS**

- 13.1 The new procurement regulations<sup>1</sup> require a new procurement process where “substantial changes”<sup>2</sup> are made to a contract that is regulated by

---

<sup>1</sup> *The Public Contracts Regulations 2015 (the "Regulations") came into force on 26 February 2015 and implement Directive 2014/24/EU*

the Regulations and provide for a right of termination to be implied into a contract where an awarded contract without a new procurement. Substantial changes include changes that:

- if they had been made as part of the initial procurement would have allowed for the admission of other candidates or could have resulted in a different outcome;
- result in a change to the economic balance of the contract in favour of the contractor in a manner not provided for in the original contract; or
- extend the contract scope.

In Eversheds' analysis there is a risk that the proposed variations have made the project more viable resulting in an economic benefit accruing to Stanhope and also that could have impacted on the outcome of the procurement (i.e. a different a woman identified). In looking at the proposed variations Eversheds comments have included that:

- to mitigate the risk of non-compliance with the Regulations the change to the structure from an LLP to a limited company must not change the economic balance for the project in Stanhope's favour;
- as bidders understood there to be a 40% affordable housing requirement for both WMC and ESH and based their submissions on this, that had the changes now contemplated, including to the SSDP, been conveyed during the initial procurement could arguably have impacted submissions received and on the evaluation outcome of the initial procurement. Similarly the provision of the costs contribution as described above at paragraph 5.5 could have impacted on proposals;
- there is a risk that the introduction of the RP to deliver 100% affordable housing at ESH and the Council taking responsibility for the clearance of the ESH site has the effect of decreasing the risk of delivery of the scheme and/or increasing profit to Stanhope; and
- the position is made more complex given the intention is that the Council grant fund the RP. The availability of this funding may have impacted on bidders proposals during the procurement and care must be taken to ensure such the provision of the funding does not constitute a breach of the Regulations as the direct award of a public works contract.

Given the factors above it is not possible to determine that there is no risk of challenge associated with the agreeing to the proposed variations.

### 13.2 Implications verified/completed by: Leyna Stewart, Solicitor at Eversheds

---

<sup>2</sup> Which could relate to a single change or arise because of the cumulative impact of a number of changes when taken together

- 13.3 Procurement of works and services by the JV will seek to maximise social return on investment, in particular focusing on job creation and training opportunities for the local community and the Borough, investment in local communities and support for local supply chains.

**LOCAL GOVERNMENT ACT 2000**  
**LIST OF BACKGROUND PAPERS USED IN PREPARING THIS**  
**REPORT**

	<b>Description of Background Papers</b>	<b>Ext of holder of file/copy</b>	<b>Department/ Location</b>
	None		

**LIST OF APPENDICES (contained in the exempt report on the exempt Cabinet agenda)**

Appendix 1: Revised SSDP for Edith Summerskill House

Appendix 2: Cashflows and Finances