

Agenda Item No.6 (d)

DERBYSHIRE COUNTY COUNCIL

CABINET

8 June 2017

Report of the Strategic Director – Corporate Resources

LOAN ARRANGEMENTS WITH DERBYSHIRE DEVELOPMENTS LIMITED
(STRATEGIC LEADERSHIP, CULTURE AND TOURISM)

1 Purpose of the Report

To seek member agreement to the making of two loans to Derbyshire Developments Limited (DDL), one for working capital purposes, the second to fund site acquisition and development. To make members aware of potential costs around site development and the treatment of Minimum Revenue Provision payments.

2 Information and Analysis

Cabinet agreed to the establishment of a wholly owned company to exploit potential development opportunities on Council land at its meeting on 14 June 2016. It was always envisaged that the company would require start-up funding from the Council due to the potentially lengthy lead in times to get a property development opportunity to the stage of delivering an income stream. In addition it was also anticipated that the Council would provide the substantial funding required, by way of loan, to enable the company to deliver individual site developments.

There are clear benefits to both parties from this arrangement: the Council will be able to charge a market rate on the investment, and the company will be able to fund its development plans. This should also be a tax-efficient way of providing funding to the company whilst securing a return to the Council.

Start-up Loan

This loan is designed to cover the running costs of the company, such as staffing, accommodation, IT, audit, financial systems etc. up until the point where developments are underway and sales will recover these fixed costs of being “in business”. Based on current details from the company it is proposed that a further loan of £300,000 be added to that already approved by Cabinet of £200,000 to finance these costs until 31 March 2019.

The loan terms are:

Interest Rate	4.78% (as advised by Arlingclose)
Maximum Loan	£500,000 (including £200,000 already approved)
Interest due	Monthly.
Loan due for repayment	In full, no later than 31 March 2019
Loan draw down	In any amounts required by the company up to 30 March 2019

At present the Council can achieve a rate of around 1% on cash investments so this arrangement presents an enhanced return to the Council for accepting enhanced risk.

Development Loan

The benefits of providing a substantial loan facility to allow the company to purchase land from the Council and develop appropriate housing units for sale are clear. As each development will present a different set of challenges and opportunities it will be necessary to ensure the loan facility requested in each case is reasonable, sustainable and affordable to ensure the company can repay the sums loaned. The company will be requested to supply the Council with whatever information the Council feels is appropriate for it to lend the resources required. This may also include taking a charge over whatever assets the company has available, however, as the Council is the company's owner this may not be necessary.

The analysis of the company's proposal will be undertaken by staff in the Finance and ICT Division of the Corporate Resources Department in isolation from the Director of Finance and ICT who, as a Director of Derbyshire Developments Limited, has a potential conflict of interest. It is proposed to ask the Finance Manager (Projects & Exchequer) to lead on this task whilst ever the conflict of interest for the Director of Finance and ICT exists.

No loan will be made for site development and building works etc. until the business case for each individual site has been approved by Cabinet. The amount of loan required per site could be up to £5m and the maximum facility required at any one time is not expected to exceed £15m.

The loan terms proposed are:

- Maximum total value of loans outstanding at any one time is not to exceed £15m;
- The maximum loan per site is not expected to exceed £5m;
- The interest rate will be at the prevailing rate after consideration of various factors including advice from the Council's external treasury management

advisors, Arlingclose, compounded and payable monthly. As of May 2017, the rate is 4.78%.

- Loan principal can be drawn down at any time once the business case has been agreed by Cabinet subject to evidence of payments actually forecast to be due each month;
- Loan principal can be repaid at any time. The outstanding balance on the loan for each site must be repaid no later than seven days after the last property has been sold on that site and the sales proceeds received into DDL's bank account.

The Council's Treasury Management advisors (Arlingclose) suggest a minimum rate of 4.78% should be payable on loan amounts to special purpose/start-up companies.

It is proposed that authority be delegated to the Director of Legal Services to conclude loan agreements based on the broad principles outlined in the report.

Site Development Works

One aspect of the relationship between the company and the Council is the decision whether to offer the company a particular piece of surplus land, in what condition and at what cost. The proposal is that the Council will follow a defined procedure to determine whether it will offer a piece of land to the company for its market value. This procedure will include details concerning minimum space requirements the company has already informed the Council about as well as confirmation that the land will be used for developing property for sale, not rent. Once the company has considered an outline agreement for sale in relation to a piece of surplus Council land the Council will make good all necessary works to ensure the land is 'development ready', these works include demolition of existing buildings, site security, design and outline planning permissions, any necessary survey, such as habitat, archaeological etc. The costs of these works will be initially incurred by County Property and ultimately recovered from the sale price paid by DDL. However, there could be instances where development works are undertaken by the Council but no sale results. In this case these aborted costs, subject to a cap of £30,000 per site (excluding demolition costs), will be met from the General Reserve; demolition costs will be met by the earmarked reserve set up for this purpose.

Minimum Revenue Provision (MRP)

There is a clear argument for suggesting that loans to DDL of the nature discussed in the report may attract a requirement to make a MRP contribution at a rate of 2.5% of the loan value outstanding per annum. In view of the expected temporary nature of the borrowing it is thought that the Council can make a decision to forego making an MRP payment, ultimately this will come under the scrutiny of the external auditor. If the auditor expects a MRP

payment to be made this would cost a maximum of £375,000 per annum. It is considered it is a reasonable risk to proceed along the lines that a contribution will not be required. This is also the view of the Council's Treasury Management advisers.

3 Financial Considerations

Subject to a formal business case for each site the Council should see a reasonable return from loans to DDL, irrespective of any dividend payments due once the business becomes profitable. As an example, £5m loaned to DDL for one year at 4.78% will produce a return in excess of £200,000 greater than currently achievable on treasury management activities. A positive return would still be due if the MRP argument goes against the Council's understanding of the auditors likely position.

4 Legal Considerations

The Council has the necessary legal powers to provide the loans set out in this report to DDL. In particular the General Power of Competence under the Localism Act 2011 and section 12 of the Local Government Act 2003.

When transferring land to DDL the Council must ensure:

- that it fulfils its statutory duty to receive best consideration under section 123 of the Local Government Act 1972; and
- the the transfer of land is for the development of properties for sale not rent in accordance with sections 24 and 25 of the Local Government Act 1988 and General Consent C.

The Council has taken advice in relation to ensuring that the loans and transfer of land do not breach the principles of the state aid regime.

5 Other Considerations

In preparing this report the relevance of the following factors has been considered: - human rights, equality of opportunity, health, environmental, transport, property, social value and crime and disorder considerations.

6 Background Papers

Papers held in the Technical Section, Finance and ICT, Room 137.

7 Key Decision

No.

8 Call-In (Is it necessary to waive the call in period)

No.

9 Officer's Recommendations

- 9.1 That Cabinet agrees to a working capital loan and site development to DDL based on the terms proposed in the report subject to negotiation by the Director of Legal Services with the Company.
- 9.2 All site development loans to be considered only after the consideration of a detailed business case by Cabinet.
- 9.3 That Cabinet agrees to the suggested funding of any site development works by the Council.
- 9.4 That Cabinet notes the position on possible MRP payments.

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