

SLOUGH BOROUGH COUNCIL

REPORT TO:	Cabinet
DATE:	16th January 2023
SUBJECT:	Severance of the Council's leasehold interest at Greenwatt Way, Slough SL1 2ES.
CHIEF OFFICER:	Pat Hayes, Executive Director Housing and Property
CONTACT OFFICER:	Fin Garvey, Group Manager – Place Delivery Peter Robinson, Financial Consultant Peter Worth, Finance Lead Technical Advisor
WARD(S):	Chalvey
PORTFOLIO:	Councillor Rob Anderson, Lead Member for Financial Oversight and Council Assets
KEY DECISION:	YES
EXEMPT:	Public but with appendices 2 to 5 exempt under paragraph 3 of Schedule 12A Local Government Act 1972 – Information relating to the financial or business affairs of the Council
DECISION SUBJECT TO CALL IN:	YES
PUBLIC APPENDICES:	1 – Site map
CONFIDENTIAL APPENDICES	2 –Lease dated 30 January 2020 3 – Avison Young valuation report dated 22 July 2022 4 – Counsel's opinion dated 26 July 2022 5 – Proposed severance terms dated 23 November 2022 6 – Land at 450 Bath Road – Overage Provision

1. Summary and Recommendations

- 1.1. This report relates principally to a leasehold interest in land which is no longer required by the Council and seeks approval for the lease to be terminated with immediate effect. In addition, it covers an overage agreement with the same party, which is in dispute, but seeks approval to terminate for an agreed settlement as part of the termination of the lease.

- 1.2. The Council's leasehold interest in land at Greenwatt Way was acquired in 2020 to facilitate the proposed construction of new care facilities as part of the Chalvey Extra Care Housing (ECH) initiative. This project was removed from the Council's Capital Programme in November 2021.
- 1.3. The freehold for 450 Bath Road was sold by the Council to Dr. Kumar on 12th February 1993. As part of a 10-year agreement that expired on 11th February 2003 any increase in the value of the property in this time would be shared on a 50/50 basis with the Council. This recognised that the Council would be entitled to an additional sum if Dr. Kumar gained planning approval to increase the building size in this timeframe. This is termed an overage provision.
- 1.4. It has not been possible for the Council to agree the valuation with Dr. Kumar and to avoid legal and valuation costs it has been agreed to include the value of the overage provision in the settlement for the lease.
- 1.5. The report sets out key lessons that need to be learned from this matter.

Recommendations:

- 1.6. Cabinet is recommended to:
 - a) Approve the proposed termination of the existing 42-year lease agreement with Bharani Enterprises (UK) Limited and release of the overage on the property at 450 Bath Road, Slough where the Council is the beneficiary of the overage for the negotiated one-off payment of £1m plus VAT and
 - b) Delegate authority to the Executive Director Housing and Property, in consultation with the Lead Member for Financial Oversight and Council Assets, the s.151 Officer and the Monitoring Officer, to negotiate the terms of severance, and approve the associated documentation to affect the termination of the lease and release of the overage.

Reason:

- 1.7. The existing lease agreement did not set out what would happen if the Council decided not to pursue the ECH initiative, nor did it specify a process for agreeing severance terms. Independent advice has been obtained from property valuers and counsel on the Council's options and these are set out in the confidential appendices.
- 1.8. A process of negotiation has taken place with the freeholder to establish a basis on which they would be willing to terminate the existing lease.
- 1.9. The freeholder has indicated that they are willing to operate a care home facility on the site but do not wish to fund the initial investment. As an alternative however they are willing to accept a one-off severance payment from the Council of £1m.
- 1.10. Officers consider that this represents value for money on the basis that the annual payments due under the lease would total £5m over the remaining lease term of 40 years.
- 1.11. Disposal of this leasehold interests supports the priority of the new Corporate Plan for *"a Council that lives within its means, balances the budget and delivers best value for taxpayers and service users."* It will also enable the Council to simplify the property portfolio and enable the Council to focus on its core activities and services.
- 1.12. As the proposed settlement payment is in excess of £0.5m it represents a key decision, therefore Cabinet approval is required.

Commissioners Review

1.13. *“The recommendations are supported on the basis that they represent the best way out of a difficult position in a reasonable timescale. Cabinet should spend some time in considering the lessons learned and the action required by both Councillors and officers.”*

2. Report

Introduction and Context

2.1. Appendix 1 provides a site map showing for the brownfield site at Greenwatt Way, Primary Road, Chalvey, Slough SL1 2ES. Since March 2015, the two plots BK476759 and BK467908 have been held in the freehold ownership of either:

- members of the Kumar family, or
- Bharani Enterprises (UK) Limited (Companies House reference 08625027), a company owned and managed by the same family, incorporated in July 2013

2.2. Dr. M L H Kumar is director and shareholder of Bharani Enterprises (UK) Limited (“BEL”). He is also a local GP and senior partner of two surgeries in Slough and another in Maidenhead trading as Bharani Medical Centres. BEL is currently constructing a new surgery at Greenwatt Way, see plot reference BK476759.

Lease agreement with the Council

2.3. On 30 January 2020, the Council entered into a 42-year lease with BEL in respect of plot reference BK467908, and contracted to make payments as follows:

- a lease premium of £1.75m at inception, plus
- annual rental of £125,000 (plus VAT) per annum with the first two years’ instalments paid in advance.

2.4. Key components of the lease agreement are summarised in Appendix 2.

2.5. The purpose of this transaction was to support the Chalvey Extra Care Housing (ECH) initiative. ECH was a proposal to build 60 1 and 2 bed ‘Extra Care’ homes, with health and residential care facilities adjacent to the new primary care facilities referred to in paragraph 2.2 above. A Capital Project Business Case report prepared in June 2019 explains that:

- the Council’s Housing Strategy for 2016-2021 had identified the need for additional 987 units of older person’s accommodation, and Chalvey ECH would contribute to meeting those requirements;
- also, the construction supply-chain and ongoing operational management of the new facilities would create local employment opportunities;
- these new facilities would be operated by BEL but constructed by the Council at an estimated total cost of £15m. This capital cost would be financed by a combination of Right to Buy capital receipts and PWLB borrowing.

2.6. An initial payment of £2m (comprising the lease premium of £1.75m plus two years annual rental totalling £0.25m) therefore formed part of the Council’s capital programme in 2020/21. A further £6.7m was approved as part of the 2021/22 Capital Programme to finance the construction element of ECH (project reference P208) with a commitment in principle to a final tranche of funding (of c£6m) from the Capital Programme in 2022/23.

2.7. It was initially envisaged in the Business Case that ECH would operate at a net profit overall, generating a future income stream for the Council which would offset interest

charges and annual lease costs. However, subsequent examination of the ECH Business Case by officers has indicated that:

- cash flow forecasts prepared in 2019 significantly under-estimated both the initial construction costs and the ongoing operational expenses associated with the project; and
- therefore, the prospect of any financial return to the Council would be remote.

Overage Provision on 450 Bath Road

- 2.8. The freehold for 450 Bath Road was sold by the Council to Dr. Kumar on 12th February 1993. As part of a 10-year agreement that expired on 11th February 2003 any increase in the value of the property in this time would be shared on a 50/50 basis with the Council. This recognised that the Council was entitled to the 50% share should Dr. Kumar gain planning approval to increase the building size in this timeframe. This is termed an overage provision.
- 2.9. Dr. Kumar carried out a development in 1994 which increased the area of the property above the existing 275m² by 37m² and obtained planning consent for a further 116 m² in 2003, within the timescale of the overage provision agreement. The overage was triggered by the granting of planning permission, and this was subsequently implemented.
- 2.10. Despite planning permission being obtained, there is no evidence that Dr. Kumar notified the Council as was his obligation under the terms of the sale agreement.
- 2.11. It has not been possible for the Council to agree the valuation with Dr. Kumar and to avoid legal and valuation costs it has been agreed to include the value of the overage provision in the settlement for the lease.
- 2.12. Details of the overage provision are set out in confidential appendix 5.

Section 114 Notice and subsequent Capital Programme Review

- 2.13. The Council's financial position, and its strategic priorities, have altered significantly since the ECH initiative was originally developed in 2019. On 2 July 2021 the Executive Director Finance and Commercial (s.151 officer) issued a Section 114 Notice, advising that significant reductions in both revenue and capital spending were necessary in order to improve the Council's financial position.
- 2.14. On 20 September 2021, the 2021/22 Quarter 1 Revenue and Capital Budget Monitoring Report to Cabinet confirmed that *"the current capital programme is unaffordable, and a number of schemes are being reviewed to determine whether they can be stopped, or their scope reduced"*. Paragraph 8.1 of that report goes on to state that *"project managers have been asked to identify options that would allow the capital programme to be reduced, so that the only schemes remaining will be those where there is either a contractual liability, a Health and Safety obligation, or the project is fully financed from grant funding"*.
- 2.15. None of these exemptions applied to ECH as construction was not yet underway and no contracts for design or building work had been let.
- 2.16. Also on 20 September 2021, Cabinet approved an "Asset Disposal Strategy", stating that *"an orderly programme of asset disposals"* was necessary to improve the Council's financial position. The report is clear that asset disposals in their widest possible context are being referred to, therefore disposals of leasehold interests and limited company investments are to take place wherever possible as well as sales of freehold land and buildings.

2.17. Subsequently, in November 2021, the 2021/22 Period 6 Revenue and Capital Budget Monitoring Report authorised significant reductions in the capital programme. Appendix E reports these changes on a detailed line by line basis, with the ECH project P208 shown as cancelled.

Options considered

2.18. Once the ECH project had been cancelled, the initial reason for the Council's acquisition of the leasehold interest at Greenwatt Way no longer applied. Although the existing lease agreement did not specifically consider what would happen if the Council (or BEL) decided not to pursue the project, three possible ways forward have been identified:

2.19. **Option A** – For the Council to purchase the freehold of BK467908 with a view to onward sale. An independent valuation carried out by Avison Young on 22 July 2022 includes a valuation of the freehold, this is attached as confidential appendix 2. However such a purchase would not be in line with the Council's current policy of not purchasing any new assets for investment purposes. Avison Young have also indicated that there are site constraints which does not make this advisable. Further information is provided in the confidential appendix. Furthermore, BEL are not, at this time, interested in selling the freehold.

2.20. **Option B** - To retain the existing leasehold interest but secure third-party funding for a new care home facility or alternative development. An independent legal opinion provided by Jonathan Gaunt KC at Falcon Chambers (see confidential Appendix 4) has advised on the options available to the Council. In addition, the length of the lease may restrict the options to secure third party funding. BEL have indicated that they are still willing to operate a care home facility on the site.

2.21. **Option C** – Undertake a separate process for resolving the settlement of the overage provision on 450 Bath Road and agree a different amount for the settlement of the lease. This risks further delay and additional legal and valuation fees, as well as delaying BEL progressing its development of the site.

2.22. **Option D** – To terminate the existing lease by way of a surrender the leasehold title to BEL for a one-off payment of £1m plus VAT and release of the overage payment on the property at 450 Bath Road, Slough where the Council is the beneficiary of the overage plus any legal costs associated with the sale. This will save the Council spending c.£5m in lease rental payments over the next 40 years for an asset which the Council does not need.

2.23. **Option D** is therefore recommended to Cabinet for approval on the basis that:

- it offers the best overall value for money
- it provides the best fit with existing Council policies on maximising asset disposals and reducing non-essential capital expenditure, and
- it reduces the Council's exposure to future financial risk.

Summary of proposed terms

2.24. As no exit provisions are set out in the current lease, a process of negotiation has taken place with BEL to establish a basis on which they would be willing to terminate the existing lease.

2.25. Following a process of negotiation which has been ongoing for almost 6 months, BEL have indicated that they are willing to settle for a one-off payment of £1m (plus VAT) and release of the overage on the property at 450 Bath Road, Slough where the

Council is the beneficiary of the overage, the Council will fund both parties legal costs associated with the sale which are relatively small.

- 2.26. The value of the overage provision is in dispute with the parties having different views on the value of the land at the relevant time and therefore the value of the overage. Settlement of this would require further legal expenses and it was felt that incorporating settlement represented best value for the Council.
- 2.27. A letter to BEL outlining the proposed terms of severance in more detail is set out in confidential Appendix 5.

Lessons Learned

Lack of adequate business case

- 2.28. While the concept to build Extra Care Housing in Slough was reasonable, like many transactions undertaken prior to April 2021 the letting of the contract suffered from poor financial advice, a lack of proper management oversight and due diligence and a lack of governance.
- 2.29. Investigations into the background to why Council officers decided to enter the lease as signed have been difficult to establish. Many individuals involved have left the Council. There was little or no documentation, discussions with the other party appeared to be on an informal basis and were not minuted. There was no involvement of the Council's Monitoring Officer and basic instructions to the Council's external legal advisors were not given and in some cases advice given ignored.
- 2.30. The business case produced was lacking in that it did not include detailed financial estimates. It materially under-estimated the cost of building the extra care housing and did not include details of how the project would be funded. The costs of the lease were wrongly assumed to be capital expenditure and included in the capital programme as such, rather than as an ongoing revenue commitment. There was no proper options appraisal and a significant optimism bias in that it assumed the Council would not just have an increased level of Extra Care Housing in the Borough but that it would make a financial return. No consideration was given to the Council purely be an enabler and encouraging a specialist provider to undertake the work. There was no evidence that there was any detailed financial review or scrutiny by the then s.151 Officer of what was a major financial decision.
- 2.31. **Steps to avoid recurrence** – the Council now has a project management team and directors are expected to produce business cases meeting the standards of HM Treasury guidance. Procurement and commissioning of services would be reviewed by a strategic procurement board, with finance and legal colleagues represented on the same.
- 2.32. The Council is also taking a different approach to investment and is only borrowing to fund essential works. It also has a high-quality financial team who would be able to undertake a full and informed business case or realise when external expertise is required. It needs to ensure going forward that this continues to be the case.

Lack of valuation to inform decision

- 2.33. No valuation of the land was undertaken prior to the Council's purchase. It is hard to understand why such a large premium was paid on entering the lease and the amount of the annual lease payment that together far exceeded the value of the land or what it was purchased for.
- 2.34. **Steps to avoid recurrence** – for all asset disposal decisions, the Council's decision is informed by up to date valuation evidence and advice from independent experts. If the Council does acquire properties in the future, the decision would be for cabinet to

make and the report would be supported by relevant information, including valuation, legal and financial advice.

Lack of project management

- 2.35. Whilst the payments were included in the business case but there was no consideration that the project could go wrong or that the Council would not proceed with it.
- 2.36. The project was poorly managed and had numerous project managers through the course of the project. Given the scale of the project it was surprising that there was no corporate overview.
- 2.37. **Steps to avoid recurrence** - Programme management and project support is now being implemented through the Corporate Project Management Office.

Decision-making

- 2.38. A wide delegation was given to a single officer, with no requirement to consult a lead member or key statutory governance officers. This was for a multi-million pound project for which finances were not fully in place.
- 2.39. **Steps to avoid recurrence** – there is now a corporate schedule setting out key decisions for cabinet. This includes review by legal, finance, procurement and other relevant teams, as well as sign off by the whole corporate leadership team and discussion with cabinet members informally before any formal decision-making. Major projects are split into key phases with clarity in the report as to the next stages and if cabinet authority is required for these. All cabinet reports contain an options section and the use of wholly Part 2 (exempt) reports has ceased – where confidential information is included, the report is split into Part 1 and Part 2 with as much information as possible presented in Part 1. Where information cannot be put into the public domain at a particular point, consideration is given to reporting this back to elected members in a public report in the future. For example, an update report is presented to the Asset Disposal Cabinet Committee on asset disposals.

Issues with lease

- 2.40. External lawyers were instructed with no obvious oversight from the Monitoring Officer or the Council's shared legal practice. The instruction appears to come directly from the service directorate. The lease contained no exit provisions, and it is unclear why it was entered into prior to finances being in place for construction. An alternative agreement to lease does not appear to have been considered.
- 2.41. **Steps to avoid recurrence** – Part 3.6 of the Council's Constitution states that executive directors have authority as follows:

“Instructing external lawyers in relation to legal matters and disputes, where agreement has been sought from the HB Public Law or the Monitoring Officer, that instructions are appropriate”

Executive directors have been reminded that they are not permitted to instruct external lawyers without explicit consent and the legal advice should be available to the Monitoring Officer and there should be clarity on the cost. HB Public Law also offer a managed legal service, whereby they would instruct the external lawyers and manage the instructions and billing.

Overage provisions

- 2.42. There appeared to be no clear records of overage provisions on land disposed of, meaning that these have not been periodically checked by the asset management team or key sites flagged by the planning team when a planning application is made.

Steps taken to avoid a similar occurrence – the Executive Director of Housing and Property will put in place a system to ensure that overage provisions are recorded in a central register and appropriate systems are in place to check sites on a periodic basis.

3. Implications of the Recommendation

Financial implications

- 3.1. In addition to the savings of £12.7m already realised by not progressing with the initial proposal to construct a new care home facility on Greenwatt Way, the proposed severance payment of £1m provides a saving of £0.125m per annum for a further 40 years in line with its existing contractual obligations. No debtor had been included in the Council’s accounts for the overage provision on 450 Bath Road.
- 3.2. A discounted cash flow comparing the value of the payment of £1m now as opposed to paying £5m in instalments of £0.125m per annum for 40 years was completed as one of the considerations for agreeing the payment. The lump sum represented a positive benefit and therefore good value to the Council.
- 3.3. Provision has been made in the accounts for the cost of the contract with the remaining balance reducing the Council’s capitalisation requirement.

4. Legal implications

- 4.1. Pursuant to section 123 of the Local Government Act 1972 (“Section 123 LGA 1972”) and/or Section 1 of the Localism Act 2011, the Council has the power to dispose of either freehold or leasehold interests in land in any manner it wishes, subject to certain provisions. The Council has a statutory duty to obtain the best price reasonably obtainable, subject to certain exemptions.
- 4.2. When disposing of land, the Council has a duty to obtain best consideration under section 123 LGA 1972, not less than the best that can be reasonably obtained. What is reasonable depends entirely on the nature of the transaction. However, failure to obtain an independent valuation or to take proper legal or professional advice, could constitute a breach of the Council’s duty to obtain best consideration as set out in Section 123 of the Local Government Act 1972.
- 4.3. The Council has commissioned Avison Young to assess both the freehold and the leasehold value of the land at Greenwatt Way, and to advise on the likely prospects of a profitable sale if the freehold was acquired and then re-marketed. The Council has also obtained Counsel’s opinion on the practical implication of various clauses contained in the lease. Officers are confident that Option C reflects the professional advice provided by both sets of external experts.

5. Risk management implications

- 5.1. The recommendations required from Cabinet, as outlined in this report, are intended to improve the Council’s financial position by minimising future payments due under an existing land lease which is now surplus to the Council’s requirements. Specific risks are summarised below:

Risk	Summary	Mitigations
Financial	Ongoing obligation to pay £0.125m per annum for the next 40 years if severance terms cannot be agreed	The proposed negotiated settlement of £1m represents a reduction in

		total outgoings over the life of the lease .
Governance	Failure to properly approve financial decisions in line with the Council's Constitution and Scheme of Delegation requirements.	Cabinet approval is required for all financial decisions in excess of £0.5m
Legal	Failure to meet best consideration requirements of s123 LGA 1972	The Council has engaged external property advisors and King's Counsel to advise on valuation and legal aspects of the proposed transaction and has acted in accordance with their advice.
Reputational	Failure to properly consider the available options for the future of leasehold property no longer required by the Council, or to negotiate a settlement which did not represent best consideration, would expose the Council to adverse comment and criticism.	This risk can be mitigated by comprehensive reporting to Cabinet which sets out the available options and demonstrates that the decision being taken represents the best value for money overall.

6. Environmental implications

6.1. No environmental implications have been identified as a direct result of this report.

7. Equality implications

7.1. No equality implications have been identified as a direct result of this report.

8. Procurement implications

8.1. The procurement of Avison Young to provide property advice, and of Jonathan Gaunt KC to provide independent legal advice, was secured in compliance with:

- The Public Contracts Regulations 2015;
- Council Contract Procedure Rules; and
- Expenditure Control Panel requirements.

9. Workforce implications

9.1. No workforce implications have been identified as a direct result of this report.

10. Property implications

10.1. This report will reduce the Council's ownership of leasehold land and property holdings not required for operational purposes, in line with policies already approved by the Council.

11. Background Papers

Appendix 1 - Site map for BK476759 and BK467908

Appendix 2 (confidential papers) – Lease entered into between SBC and Bharani Enterprises (UK) Limited on 30 January 2020

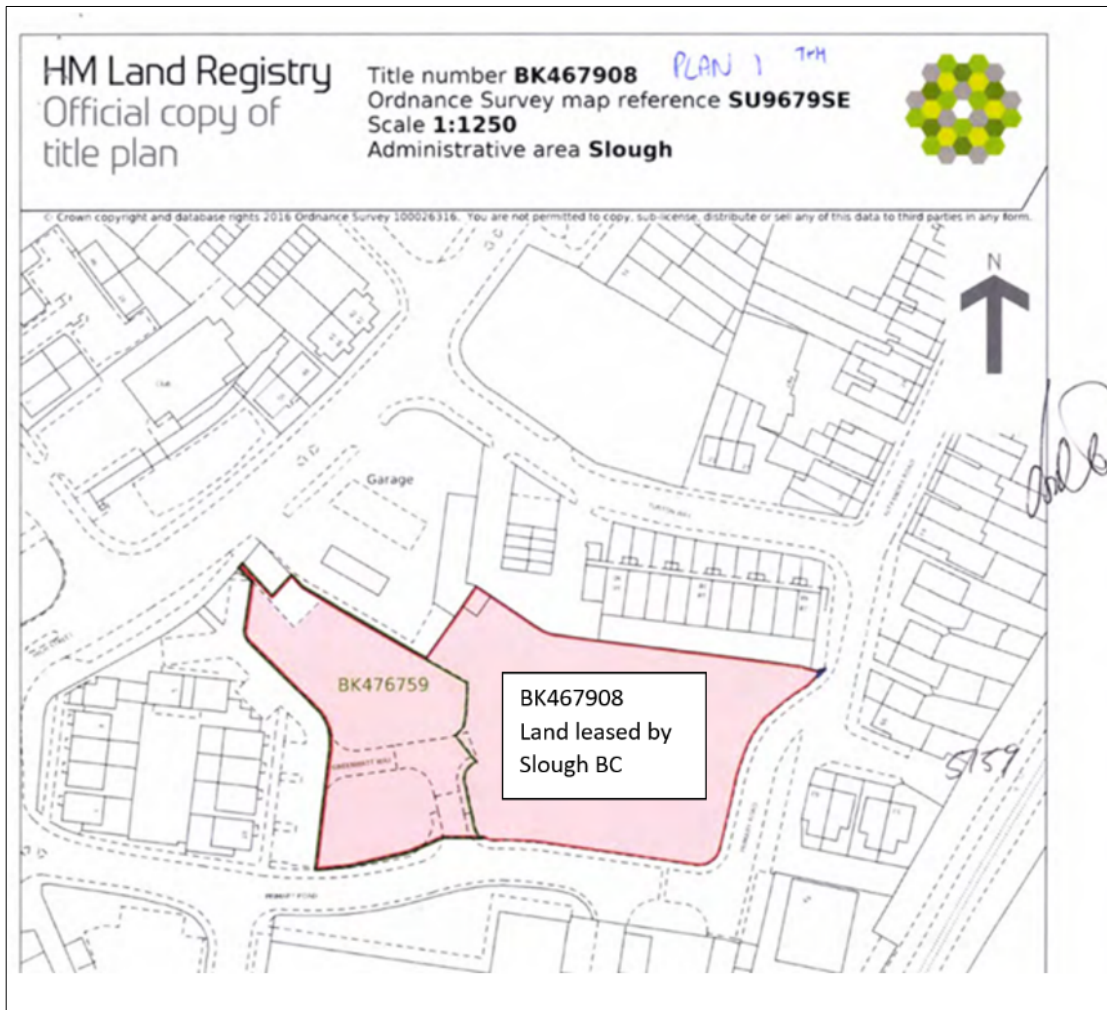
Appendix 3 – (confidential papers) - Independent valuation provided by Avison Young on 22 July 2022

Appendix 4 – (confidential papers) – Legal advice obtained on 26 July 2022 from Jonathan Gaunt KC

Appendix 5 – (confidential papers) – Proposed severance terms 23 November 2022

Appendix 6 - (confidential papers) – Land at 450 Bath Road – Overage Provision

Appendix 1 – Site map for BK476759 and BK467908



Appendices 2, 3, 4, 5 and 6 contain exempt information and are in Part II of the agenda.