

## COMBINED STRATEGIC SCRUTINY AND CUSTOMER FOCUS SCRUTINY COMMITTEES

27 April 2022

### Present:

Councillors Atkinson, Allcock, Begley, Branston, Denning, Hannaford, Mrs Henson, Jobson, Mitchell, M, Moore, J, Newby, Pearce, Sheldon, Sparkes, Sparling, Vizard, Wardle and Warwick

### Apologies:

Councillors Mitchell, K and Sills

### Also present:

Director Corporate Services, Director Finance, Democratic Services Officer (SLS) and Democratic Services Officer (HB)

### In attendance:

Councillor Bialyk	Leader
Councillor Ghusain	Portfolio Holder Communities & Culture
Councillor Sutton	Portfolio Holder Net Zero Exeter 2030

Councillor D. Moore attended under Standing Order 44.

Roli Martin	Project Manager Exeter City Futures
Elaine Anning	Operations Director Exeter City Futures
Frazer Osment	Chair LDA Design

## 12 **Appointment of Chair**

**RESOLVED** that Councillor Vizard be appointed Chair of the meeting.

## 13 **Minutes**

The minutes of the meeting of the Combined Strategic Scrutiny and Customer Focus Scrutiny Committees held on 30 March 2022 were taken as read, approved and signed by the Chair as correct.

## 14 **Declarations of Interest**

No declarations of discloseable pecuniary interest by Members were made.

## 15 **Exeter Development Fund Overview**

Members noted that Scrutiny is being asked to perform a critical friend role for the Council's Executive in examining and highlighting the merits and risks associated with the City Development Fund ahead of the full Business Case being presented to the Executive for consideration later this year.

The planned sessions are as detailed below.

Session 1	Introduction – 30 March 2022
Session 2:	What is the economic case for pursuing a City Development Fund to support delivery - 27 April 2022
Session 3:	Governance/Fund Management/Governance and Risk – 6 June 2022

16 **Exeter Development Fund - Session Two - The Economic Case**

Councillor Diana Moore attended the meeting having submitted a number of questions under Standing Order 44.

The Chair welcomed Roli Martin, Project Manager and Elaine Anning, Operations Director of the Exeter City Futures Team (ECF) who would set out the economic case for pursuing a City Development Fund to support delivery, along with Frazer Osment, Chair of LDA Design, who also attended as an external witness.

Frazer Osment offered a high level observation on the viability challenges and constraints in delivering the vision. He provided a brief background of his experience of development work within the private and public sector, working with major developers and public sector bodies who wished to achieve significant change. The many projects undertaken by LDA, included the design and delivery of the 2012 Olympic Park, the complex renovation of the Battersea Power Station and Millbay docks in Plymouth.

The presentation (attached to the minutes) sought to highlight the viability challenges in bringing forward large scale change in the urban environment and specifically in respect of Liveable Exeter. The challenges faced by society has stimulated an alternative development approach in respect of the response to matters such as climate change and improving social equity. The vision and aims at the heart of Liveable Exeter included leveraging the value and assets of the city to provide quality neighbourhoods, deliver affordable homes, a renewed infrastructure, and investment in services with wider benefits for residents, businesses and visitors of Exeter alike.

Frazer referred to the following challenges from a viability perspective :-

- securing quality - large scale developers selecting projects based on profitability, the quality of the homes, including room sizes, may be compromised;
- type and tenure - house builders being profit led often at the expense of the range of tenure offered which may not always match need;
- delivering benefits beyond the site - the value of a development should extend beyond the immediate site boundary. One local example of a Liveable Exeter site at Water Lane included enhancements at the Riverside Valley Park;
- timing and phasing - land ownership by developers can delay development in response to economic downturn or scheduling to maximise profit, and
- capturing the value generated - profit maximisation could be at the expense of capturing the site value.

He also set out the portfolio approach:-

- master developer perspective – addressing the challenges of realising the type of change relating back to fundamental viability. Whilst an initial site may not return profit, success can be where there is local authority/public sector involvement providing a holistic approach, creating momentum across the wider city by bringing forward a number of sites;
- setting the benchmark and brand identity - setting quality standards across the city meeting environmental considerations, and achieving buy in from other developers. Cambridge, a city similar to Exeter, has achieved a significant

transformation in the quality of development in and around the city over the last 20 years due to the wider and strategic vision;

- upfront infrastructure and long term value creation - better be achieved by a wider perspective and partnership approach rather than a single developer involvement, and
- diversity can equal pace - offering a range of tenure, innovative designs and an emphasis on wider community improvements to provide quality of life could speed neighbourhood regeneration. It was important to make choices and disrupt the market to ensure diversity of development and accelerate the scale and pace of development of new sustainable communities and desirable neighbourhoods.

Elaine Anning, Operations Director for Exeter City Futures (ECF) introduced her presentation which would provide an overview of the economic case. (attached to the minutes). The economic challenges of delivering a sustainable, healthy, and vibrant community on brand new land had been covered at the last Combined meeting of Scrutiny. The management of the viability gap would generally require a level of funding intervention from Government as the Community Infrastructure Levy (CIL) and Section 106 payments would not cover the full cost of the support infrastructure required for the type of community that would be built.

A proof of concept exercise had been conducted which would conceptually enable such developments to offer a more viable and better opportunity rather than the usual development business approach. Partners have indicated their support, in principle for the projects, but no commitment has been made to date. A number of workshops had been held with partners to explore what may be required to divest assets into the Development Fund, along with the necessary approvals and safeguarding considerations. The funding structure and pooled land assets from partners of Exeter City Futures as well as Government funding would move the project forward and be used to leverage private sector borrowing to finance the costs of the whole development as well as to procure the required expertise in house to commence delivery and build out the sites.

The economic case included a long list of options to deliver Liveable Exeter, filtered against the strategic objectives of the project to create a short list of options and followed by a benefits costings exercise.

The options appraisal process included:-

- Scope – what is the extent of the project.
- Solutions – what are the potential options for achieving our ambitions.
- Delivery – who will provide this option.
- Implementation – how will we achieve this, what is the programme.
- Funding – how will it be funded.

The proof of concept Outline Business Case for the project was fully funded by One Public Estate who work on cross public sector partnerships to deliver economic benefits with housing. The potential of this Fund could revolutionise how the partnership could use assets to deliver homes and communities. Seconded from Global City Futures, Exeter City Futures jointly employed herself and Roli Martin and their team to write the full Outline Business Case with specialist consultant support. The briefs from the formal procurement with the support of JLL, real estate and financial modelling consultancy services provided by Deloitte and the procurement briefs which were prepared with the City Council's procurement team were available for Members to view. These services were funded out of a £200,000 budget provided for the purpose. The business case has been completed to the Government's Green

Book required standard and signed off by the project's sponsors and would be available in May and available for full review by Members before any decisions were made.

The detail of the proposed developments with a full cost consultancy approach for each of the sites was outlined –

- 9448 apartments,(including 15% 1 bed; 65% 2, and 20% 3) with an average size 754 sq ft; 1251 townhouses (55% 3 bed; and 45% 4 bed) 1076 sq ft. To include 35% affordable housing.
- 750k sq ft retail/leisure; 1.3m sq ft office space, 1.6m sq ft industry (Marsh Barton); and 106k sq ft comm/pub facilities
- Schools – 810 primary places – assumed 3 schools and 600 secondary places 1 school.

Design enhancements with an uplift for sustainability design enhancements to be provided for both the apartments and the townhouses would also be in the following terms -

- Apartments - Carbon neutral living/Photovoltaic systems/High-performance windows/District Heating/Mechanical ventilation systems and Community biomass boiler.
- Townhouses - Carbon neutral living/Photovoltaic systems/High-performance windows/District heating/Mechanical ventilation systems and Electric vehicle charging points and integrated building management systems.

A number of other benefits were outlined including addressing fuel poverty removing 3,000 Exeter residents from fuel poverty with the resulting health benefits, and the varying costs of retrofit to address energy efficiency captured during the complex process. Graduates from the University of Exeter offered their support in the process.

The One Public Estate Funding format included –

- development of a replicable financial model that optimises public sector assets for housing and infrastructure.
- a portfolio approach to urban development that brings together public sector partners to maximise economic growth and efficiencies while providing ongoing, tangible stewardship of community assets and facilities.
- disrupting the market to accelerate the scale and pace of the development of new sustainable communities and desirable neighbourhoods to live and work.
- to enable a built environment that ensures the city's Net Zero objectives.
- protect public sector land assets from disposal.
- build market leading development capability within the local public sector.

In concluding the presentation, the short list for progressing the Development Fund included three options of

- 1) Business as Usual development approach;
- 2) joint venture approach seeking the viability gap funding versus the benefits that were likely to be accrued versus the
- 3) Exeter Development Fund.

The modelling included a varied inflation rate, but Deloitte have advised the Retail Price Index (RPI) 2.9%, debt interest rates of 6%, annual revaluation of 1% on assets

once constructed, with the assumptions applied consistently in all scenarios produced. The total cost of delivering the whole project was £48 billion with Government equity rated at 31%. A return was not a priority of the project; but offered a cost effective means of delivering the aspirations of the project through improved health, wellbeing and improved economic benefits.

The detail of the Outline Business Case would be provided to Members in advance to inform debate at the remaining planned meetings of these sessions.

Elaine Anning responded to a Member's comment on the opportunity for Members to have information before the meeting to formulate questions and scrutinise the process. She had endeavoured to provide an overview of the economic case at this meeting, but would seek to circulate more detail on this at the earliest opportunity. She advised that the risks of the proposed approach could be evaluated when the business case was formally presented to Members at the fourth session.

The following responses were given to Members' queries:-

- Government funding through the One Public Estate Programme sought adherence to guidance provide by the HM Treasury "Green Book" on how to appraise programmes and projects. Homes England, as the critical friend had reviewed their work and given feedback and would continue support through the next stage;
- the appraisal included a long list approach, scored against the critical success and strategic objective of the project. The short list included costings to confirm the preferred formula;
- the timing in bringing forward individual developments was dependent on a number of factors including allocation of Government funding and continued commitment of respective partners for the identified sites. A first-site delivery of 2023 was when work on the first site was due to commence, and a lead in time of around 24 months to get to construction would follow the Government's allocation of funding;
- the model was based on public sector land ownership investment and Government equity investment. Public sector land ownership could not be divested to the private sector and would always be owned by the Government in some form or another.
- the principal land owners of the St David's Gateway/Red Cow Village were Network Rail, the University of Exeter and some City Council land ownership. Exeter City Futures had been working with Network Rail on the future modelling of the site, potentially using the Fund.

Councillor Jobson referred to a number of questions submitted prior to the meeting, and in the spirit of completeness and the meeting being conducted in a timely matter, she confirmed she was content to defer for a response if the information was going to be forthcoming and then ask any further questions. She was reassured that conceptual detail of the risk analysis and the range of interest rates would be included and looked forward to receiving the detail of the business case in due course.

Councillor D. Moore, having given notice under Standing Order No. 44, attended the meeting and submitted the following questions in advance. The response to the first question was given by the Director of Finance and Section 151 Officer and the remainder of the questions were answered by Roli Martin of Exeter City Futures and were set out in italics:-

1. As Council and other public sector assets are to be invested as equity - if the fund loses value or fails how will the assets be protected from disposal (as cited)?

*R Members were legal custodians of the management of the Council's assets for Exeter citizens and should always consider the risk of any future loss of asset. As with all public sector investments, this will be the key consideration for each public body. Whilst a local authority is protected from falls in asset values by the statutory overrides in place when it owns the asset, the statutory override protecting Councils from falls in the value of their investments in Companies ends in 2023, and it is unlikely that it will be extended. Similarly a loss of public assets without a return through failure of the fund will also be unacceptable. Understanding the risk management approach will require a balanced approach which will therefore be key and could involve -*

- *Drip feeding sites in exchange for equity,*
- *a mix of sales to the fund along with equity, or*
- *straight sales of assets to the Fund.*

*The next piece of work will be important and start to build up a consensus approach on risk for each partner with an acceptable strategy for risk mitigation.*

2. These models show the value created for the Fund only. What financial calculations have been undertaken to examine the impact of loss of capital from the Council's balance sheets and associated loss of income from assets it currently controls but might put into the Fund?

*R The commission was to look at the Fund and the benefits to the city. No work has been done on individual Councils/partners. As part of the commercialisation/implementation stage of the project over the next two years, partners will do their own value for money (vfm) exercises as part of their own divestment proposal business cases to identify what they can use in their portfolio.*

3. As these proposals are not conventional and carry a high level of uncertainty at this concept stage what confidence interval has been agreed with the Treasury for this work?

*R No specific confidence interval (a statistical sampling tool) has been agreed with the Treasury. Optimism bias had been incorporated into all the economic analysis. In response to a further question from Councillor Moore, it was confirmed that the figures provided in the presentation included optimism bias.*

The following responses were given to Members' further queries:-

- the collapse of Midas and challenges facing the construction industry was a concern. ECF had existing links and could influence and offer opportunities for a wide range of skills through its partners of both Councils, Exeter College, the Royal Devon & Exeter Hospital (RD&E), Global City Futures and the University of Exeter, the latter, in particular, offering leading research capabilities in climate change;
- with a number of sites within the St. David's ward, land ownership will be critical in bringing forward identified sites. Work will occur with communities to find outcomes that are right for the site but weaknesses in the planning system will provide challenges as with all developments and the aspirations of the community led approach in relation to viability may not match;

- the modelling of tenures included rent with control of ownership retained but the mix of variables could include onward sale, with the potential to sell some of the property to generate funds and improve the modelling.
- as land owners, the Development Fund will engage its own contractors who operate to private sector margins;
- One Public Estate (OPE) as the sponsor was made up of the Cabinet Office and the Local Government Association. ECF were delivering the project with a two year runway for the next phase of the business case. Some of the work could be completed at cost but the skills and expertise would be drawn from the other Board members comprised of both Councils, Exeter College, the RD&E, Global City Futures and the University of Exeter;
- ECF had modelled for affordable housing revenues of 80% of the market. There would be an impact on returns if more social housing was proposed, but the greater value of economic and society benefits was acknowledged. That model was not in the current business case but was part of modelling work they could do in the next stage. The affordable housing projection for all sites was based on the City Council's 35% policy target. The debt facility rate was set at 6% based on the prevailing rates at the market, and based on a 3.5% return, below which losses could be anticipated;
- the analysis of a project underway for Marsh Barton will be used for which sites should be taken forward for the flagship sites. Additional work was also being carried out on Southgate as well as on the St David's gateway. Funding has been provided in the next round by the Department for Levelling Up, Housing and Communities (DLUHC) for additional work but it was important not to duplicate other work already underway but collaborate over sites to ensure robust data;
- the Government had required the grant of £800,000 to be given to Exeter City Council under the purview of the Section 151 Officer. ECF submit monthly invoices to the Council for funding to be released in stages in arrears. Grant funding was included within ECF accounts which are lodged with Companies House, but the majority of the funding has not been drawn down. A value for money review was part of the funding regime. Detail of the funding was not currently included in the Corporate Risk Register;
- ECF are supporting all partners with the City Council in assessing the programme's viability and identifying inputs to the process and the identified sites, followed by the County Council. Workshops provided for the partners have enabled them to engage them with the process. The Southgate and Marsh Barton sites were largely owned by the City and County Council, with the RD&E having some involvement in the latter. The Marsh Barton sites could be broken down into parcels and the partnership ownership would have an effect on which site was brought forward;
- there was flexibility built into the model allowing for adjustments to be made to the affordable housing percentage. There was no provision for socially rented accommodation in the current model but any drop in the financial return would recoup additional social benefits. It was accepted that a number of infrastructure elements do not generate rental income, but the return would be made from the rental of the commercial and residential properties. The place based approach would add value by providing desirable neighbourhoods;
- social value was part of the overall equation and it was anticipated that monetisable social value will come from the development in the next piece of work offering a balance between health and well-being, carbon neutrality as well as providing new homes which was a commercial activity.

- the release of certain Council assets, for example, within the HRA, may be achievable but it was the responsibility of the City Council's Section S151 Officer to make sure Members were aware of all of the facts of divesting Council assets which would be subject to Secretary of State approval. There would also need to be assurance that in terms of commercial properties other than lease responsibilities, the income can be replaced;
- the programme's overall rationale was to break the cycle of the traditional mode of development and achieve adequate public sector control through a partnership approach. A robust framework to ensure the city's brownfield sites could be brought forward as set out in the Liveable Exeter vision and show what actually was achievable.

The Director Finance, as the Section 151 Officer, stated that he was the responsible officer for advising Members on the financial implications of the Development Fund viability, and to ensure they had an understanding of the impact on the City Council in terms of its assets and risk. He would anticipate that other partners would be taking their own advice on whether to commit to the programme. He noted the Member comment that the City Council could engage independent advice to make sure that ECF have demonstrated viability, and if the decision was made to go ahead whether the risk was manageable or acceptable to the City Council.

The Chair thanked Frazer Osment, Elaine Anning, and Roli Martin for their presentations. A third session on the governance arrangements would be held on 6 June and Ian Piper Chief Executive of the Ebbsfleet organisation would be invited along with the Exeter City Futures team.

The meeting commenced at 5.30 pm and closed at 7.00 pm

Chair