WEST DUNBARTONSHIRE COUNCIL

Report by the Executive Director of Housing, Environmental and Economic Development

Council: 26 January 2011

Subject: The Securitisation of the Council's Non-Operational Estates Portfolio

1. Purpose

1.1 The purpose of this report is to inform the Council of the Business Case for an alternative Business Model and subsequent fund raising proposal in relation to securitising the Council's Non-Operational Property Portfolio and to gain approval to take forward the recommendations within the report.

2. Background

2.1 The 2010 comprehensive spending review imposed a new funding environment on all public bodies. The Council's revenue and capital budgets have reduced by 4.53% and 23.3% respectively. Funding challenges are going to be a major issue for the Council over the next few years.

2.2 As a result, the Council is examining ways to reduce ongoing revenue expenditure and at the same time looking at opportunities to raise additional capital investment to fund spend-to-save initiatives or alternatively invest in activities and assets that would generate enhanced revenue income.

2.3 On 27 October 2010, Council agreed the Corporate Asset Management Strategy. The Strategy's Action Plan included the undertaking of a feasibility study to establish whether securitisation of the Non-Operational Estates Rental Income was feasible and how much capital it might generate, with a target date of 31 January 2011. On 27 October 2010, Council agreed to instruct Officers to bring a report to the meeting of Council on 26 January 2011, to include a feasibility study and business case, which will outline asset securitisation proposals.

2.4 Asset securitisation essentially involves borrowing monies based on the amount of the rental or income stream of certain properties. Standard securities are taken by the lenders over these properties. On 10 November 2010, the Tendering Committee agreed to let the tender for the preparation of the Business Case to Ernst and Young and, subject to Council agreeing in January 2011, to proceed to a full tender following the business case, to agree that consultants with suitable expertise be invited to tender under the terms of catalyst, the framework agreement established by the Office of Government Commerce (OGC). The monies borrowed can then be used to carry out projects to reduce the Council's revenue budget.

2.5 In 10 November 2010, the Council engaged Ernst and Young to carry out the feasibility study. The feasibility study highlighted that our Non-Operational Property Portfolio was particularly suited to raising this additional debt finance by securitising the rental from these assets over a 20-25 year period with a financial institution. Since then work has been completed on the business case. This report sets out the key issues arising from the business case, a full copy of which is attached as Appendix 1.

3. Main Issues

3.1 The Business Case states that up to £35.1 million could be raised from the securitisation of our Non-Operational Property Asset Base. The structure of repayment of the Debt Finance would be over 25 years.

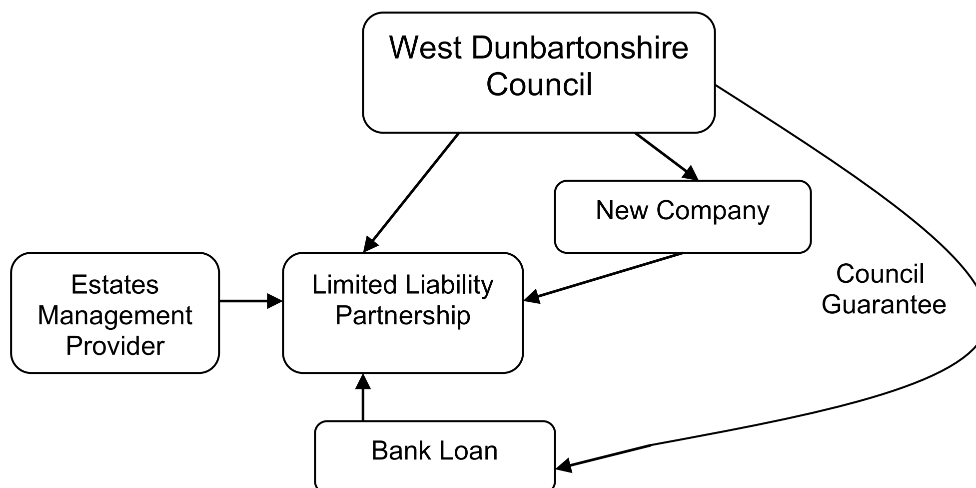
Structure of the Proposal and Governance Issues

3.2 Reduced to basics, the proposal has two elements being:-

- The Council borrows £35.1m secured by a Council guarantee.
- The Council creates a Limited Liability Partnership to manage and approve its rented property portfolio.

These two elements are linked in the proposal, one cannot proceed in the absence of the other.

The structure of the proposal can be summarised in the following diagram:-



3.2.1 The elements of the structure are explained as follows.

Firstly the Council creates a Limited Liability Partnership (LLP) which is 100% owned by the Council. For tax reasons it is more efficient to create an LLP than a company. However a partnership needs to have at least two partners. Thus the Council also creates a new company which is also 100% owned by the Council which provides a second partner. The LLP receives the bank loan and undertakes the estates management functions and the company acts only as a legal body which makes a second partner on the LLP.

3.2.3 There will need to be a Members Agreement between the Council, the new company and the LLP setting out the respective roles and responsibilities of the Members of the SPV and the procedures for the management and administration of the SPV.

The Members Agreement between the Council, the company and the LLP will provide that the Council will be entitled to 99.99% of the income and capital profits of the LLP whereas the new company will only be entitled to 0.01% of the income and profits.

The idea is that these properties would not be transferred to the LLP. Instead the right to receive the rents would be assigned to the LLP. In accounting terms, but not legally, this amounts to a lease.

3.2.4 The LLP would then borrow monies from a bank, with the rents paying the annual loan charges. This is similar to a mortgage, except that the loan is based on the rent levels, not the value of the properties and is not secured on the individual rented properties. Instead it is secured by a guarantee from the Council. The guarantee would provide for “step-in” rights that if the LLP was unable to meet all of its annual repayments to the bank, then the Council would be obliged to do so. To avoid state aid issues the guarantee would need to be limited to 80% of the loan.

3.2.5 Not all of the rents will be needed to repay the loan of £35.1m. Initially only 75% of the rents are needed to meet repayments. This lowers the risk to the Council and also results in a more acceptable risk to the banks. This 75/25% split is commonly referred to as the “gearing”. Over time the rents will rise due to factors such as inflation, improvement of the properties etc. Less of the rents will then be needed to repay the loan. The remaining rents would be used to improve the Council’s rented estate. This is necessary for several reasons. Traditionally the Council has been hard pressed to improve its leased estate and has merely repaired and maintained it where possible. Underinvestment in the estate eventually leads to obsolescence, higher vacancy rates and lowered rents. The costing for the project includes a number of investments into the estate. The level of investment proposed over the first 25 years is such that if it was continued over a 40 year period, it would see the complete rebuild of the total portfolio. The surplus after this expenditure would be paid as a dividend of 99.99% to the Council and 0.01%

to the new company. Changing the gearing (say to 70%) or the term of the lease reduces the amount of the loan.

3.2.6 The loan is then paid by the LLP to the Council. It is treated as capital rather than revenue. At this stage it should be noted that by transferring the Council's rental income to the LLP to pay for the loan and to improve the properties, the Council's revenue budget will lose this income. It is estimated that from 2012/13 onwards there will be a £2.7m shortfall in the Council's revenue budget due to assignation of the rents. The Ernst and Young Business Case emphasises it is essential that the purposes for which the Council spends the £35.1m reduce the Council's revenue budget by at least £2.7m per annum. If it fails to do so the Council will simply have increased the shortfall in its revenue budget. Accordingly potential projects will need to be carefully assessed to identify the revenue savings that they will produce. Audit Scotland have emphasised that receipts of this nature should not be used to plug a recurring gap in a budget, but should instead be used for projects which reduce the Council's revenue budget going forward.

As part of the business case, Harper McLeod Solicitors examined the issue of vires, of whether the Council has power to undertake the project. Their view is that the Council has power to do so in terms of the power to advance wellbeing introduced by the local government in Scotland Act 2003. If relying on this power, it will be necessary to clearly articulate the benefits and the wellbeing to the community that the spend will produce. This notwithstanding, it is the view of the Head of Legal, Administrative and Regulatory Services that independently of the power of wellbeing, that as long as the Council use the loan for a purpose which is within their powers (which it will almost certainly do) that the Council has existing powers to set up the new company and LLP, to procure the loan through the LLP, to guarantee payment of the loan and to procure the estates management of the investment assets through the LLP.

3.2.7 The sums obtained by way of a loan are not dissimilar to those which would be gained if these properties were sold. The difference is that the properties are retained by the Council and at the end of the 25 year period will be in a good condition, better able to contribute to regeneration and economic development of West Dunbartonshire and deliver better rental streams.

3.2.8 As the LLP will be dependent on the rental income to fund the loan, it is unlikely that the lenders will be interested (or if so at a much higher interest rate) unless the rent producing properties are run on a commercial basis. Running the assets on a commercial basis does not necessarily mean higher rents. It includes use of tools such as quicker turnaround of rent reviews and vacant units, improvement to management information systems, wider letting contacts and more focussed investment in properties. As the providers of the loan are dependent on the rent, the Council will need to ensure that the properties are run with a more commercial approach. This would be reflected in the Members' Agreement between the Council, the LLP and the new company. It is likely that the terms of the loan would prohibit certain material

changes to this Membership Agreement, thus committing the Council to managing these assets in a commercial manner for 25 years.

3.2.9 The recommended option is that the estate management function in relation to these properties are bought in by the LLP. The Council would still retain some estates function as areas such as asset management, sales, purchases and valuations will remain in-house. In theory there may be a TUPE transfer or secondment of some estates staff to the estates management or surveying firm which provides services to the LLP. In practice, given the fact that some duties will remain with the Council, and early retirement requests, it is questionable how many, if any, staff will transfer.

3.2.10 The recommended option proposes an Estates Manager post employed by the LLP who, in addition to instructing the estates management contract will provide liaison with the LLP. It is intended that the LLP will purchase other back office services from the Council such as finance, legal, HR, admin and IT. There will need to be a transfer agreement between the Council and the LLP setting out the services which it will transfer to the LLP and its expectations of service delivery.

3.2.11 Finally, it should be noted that there are two further requirements of the proposal:-

There are public procurement issues involved in the Council transferring estates management function to the LLP and in the LLP contracting with a third party to provide such functions. As the LLP will be 100% owned by the Council and since Councillors and Officers will make up most or all of the partners of the LLP, thus exercising day to day control over it, it is likely that the transfer of estates management functions to the LLP will not be subject to public procurement. It falls within what as known as the “Teckal” exemption. Providing the LLP is set up to operate on a commercial basis, the procurement of estates management services by the LLP may not be subject to public procurement (albeit the LLP may well wish to procure these services by way of competition).

3.2.12 Unlike the Council, the LLP will pay VAT on its costs, including construction and maintenance of units. This VAT can be recovered if the Council waive the exemption to VAT for particular properties. The Ernst and Young report recommends that exemption to VAT is waived for all properties where it is likely that the tenants are already VAT registered (and can therefore reclaim any VAT) but is not waived for smaller categories of property where tenants would be unlikely to be VAT registered.

3.3 The Non-Operational Portfolio has 521 properties and ground leases. It would be proposed that with the exception of the 37 Common Good Properties, all other Non-Operational Property Rents would be utilised to raise the debt finance required. Common Good Properties are not included as income. Income from Common Good Properties needs to be used for the benefit of Dumbarton and its inhabitants and it would be extremely difficult to quantify the share of the project which would relate to Dumbarton. In addition, much of

the Common Good rents tend to be used for grants which would make it difficult to withdraw this rental stream from Council budgets. It would be the intention that the SPV managed the common good assets through a service level agreement. The HRA portfolio of 42 retail properties would be part of the securitisation model going forward. The HRA will receive a capital investment proportionate to the properties rental yield.

3.4 The annual net rental income for the Non-Operational Properties which are included in securitisation for the period ending March 2010, was £4,137,090.

3.5 The Council's ownership of its 19.43% share in the Clyde Shopping Centre has been estimated as being worth £24m. In terms of securitisation, it is worth £21.938m to the project overall. This is made up of £14.852m from the securitisation of the leases and it also includes £7.086m in dividend payments to the Council over the 25 year period. The overriding benefits of including Clyde Shopping Centre in the securitisation model is that at the end of the 25 years the Council will still own 19.43% of a refurbished, fit for purpose shopping centre.

3.6 The proposed approach will have a fully funded investment programme for the Non-Operational Property Portfolio. £13.395m of investment is planned over the lifespan of the project. This will include investment in 4 key areas; Clyde Shopping Centre, Alexandria Shopping Centre, The Artizan Centre and the remainder of the business, commercial and industrial property.

3.7 Capital monies could be sourced from the Investment Programme to invest in Clyde Shopping Centre. The Council owns 19.43% of the 5 separate ground leases which cover the centre. The Council receives £1.438m (2009/10) in rental income each year with the potential for this income to increase if the centre remains an attractive proposition for retailers and shoppers alike. The shopping centre will be due a major refurbishment in 2021 and this is when the potential investment could be made. The securitisation model allows for this to be planned for without any further investment from the Council.

3.8 Alexandria Shopping Centre brings in an annual rental income of £599K per year. Within the Alexandria Shopping Centre there are two areas recognised for regeneration, the overall shopping centre itself and the adjoining area of development land. The shopping centre has been valued in the order of £3.5m as it presently stands and includes 38 units on Main Street and Mitchell Way and a stand-alone Somerfield Store. The current weak investment market for non-prime properties means that the value is likely not to be achieved. The area of development land is in the current Alexandria Town Centre Masterplan and is set aside for a foodstore. The value of this site has been set at circa £1.44m. However, the costs associated with this site in terms of realignment of roads and abnormal costs is estimated to be around £1.25m. This would result in a capital receipt of £200K approximately.

3.9 The Alexandria Shopping Centre contributes £5.791m to the £35.1m if included in the securitisation model. It will also contribute £2.881m in additional dividend payments over 25 years if left in. For these reasons it is better if the asset remained in the model moving forward.

3.10 In November 2010, the Council carried out an exercise with Retail Consultants, Colliers, in looking at preparing a Development Brief to market the Alexandria Shopping Centre and development land sites. In their strategic consideration their recommendations to the Council in summary were that the Council should sell the shopping centre and hope that the investor may at a later date, either also invest in the development site, or that the investor may invest a sufficient sum to refurbish the shopping centre, creating more vibrancy in the area and this perhaps making the development site for a foodstore a more attractive opportunity for the development market. This strategy carries a number of risks:

- in the current market it is doubtful that the Council would receive a capital receipt comparable to the value of the shopping centre;

- if the Council was able to obtain an agreeable receipt for the shopping centre, it is at least questionable as to whether the new owner would move immediately to refurbishing their new asset and/or look to purchase the development site.

The current threat to Alexandria Town Centre is that it will have to wait for the development market to pick up. This could take a number of years. At the same time, the fabric and vitality of the area will be declining.

3.11 The commission with Colliers has been put on hold due to the Securitisation Project. Ryden LLP who are Commercial Property Advisors, and are part of the Ernst and Young Team, have looked closely at the Alexandria Shopping Centre and how best it should be taken forward. Ryden have discussed the issues with Colliers and both companies feel that the project would work more effectively for the Council if the Council itself invested in the much needed investment in the Shopping Centre. This investment should take place over the next 2 years and should concentrate on the shopping centre area and assist in making the development area more of an opportunity for any interested foodstore developer. The detailed costings have still to be done but it is recommended that a sum of £770,000 be set aside from the Council's existing capital budget over a 2 year period. Ryden are convinced that this investment is essential to assist raising the level of rents in the shopping centre in the medium to long-term and as stated assist in unlocking the neighbouring development site for a perspective foodstore earlier than it may. It is expected that the physical aspects of this work would commence no later than 2012.

3.12 The Artizan Centre in Dumbarton is a critical component of making Dumbarton a place where retailers wish to be and shoppers wish to visit. Although there is no current defined investment opportunity it is felt prudent to plan within the SPV's Business Plan for Refurbishment, investment in the region of £225,000. For financial modelling purposes this reinvestment has been scheduled to happen in year 5.

3.13 For all remaining properties within the securitisation portfolio, an investment sum of £9.15m has been set aside over the period of the project to the SPV to ensure that all our properties are part of an ongoing refurbishment programme.

3.14 The Investment Programme of £13.395m is an additional investment which means that the Council has a 'fit for purpose' investment portfolio, the benefits which include:

- positive public perception on the Council's stewardship of its property assets;
- attractive shopping and retail centres which are in prominent local communities; and
- industrial, commercial and business properties that support local jobs and help attract and retain local and national businesses in West Dunbartonshire.

3.15 Soft market testing has identified that 3 such institutions have confirmed their interest and willingness to provide the debt finance subject to their normal diligence procedures.

4. People Implications

4.1 During the period of time involved in the preparation of the detailed Business Case and the selection of the preferred financial institution, a substantial amount of senior officer time will have to be allocated and planned for, to enable the effective delivery of this project and the normal demands of the Council to be carried out.

4.2 Due to the nature of this project, the Council will need to procure specialist asset, legal and financial advice. This expertise will be secured through tender and will utilise the catalyst framework for procurement purposes.

4.3 Staff resources will have to be dedicated and focussed on researching and preparing detailed funding proposals over the next 4 months which substantially reduce the Council's current requirements in terms of revenue expenditure and at the same time continue to deliver effective services to the public. It is proposed that these projects would be considered for funding support by utilising the £35.1m loan.

4.4 The securitisation model proposes the transfer of up to three posts within the existing Estates Team. The detail of the exact number of posts and how they will transfer will be considered fully in the detailed business case.

5. Financial Implications

5.1 To access the receipt of £35.1m identified within the business case, the Council would have to transfer the rights to collect rental income along with the liability for associated costs to the LLP.

5.2 The business case assumes a date of implementation of 1 October 2011 and table 12.2 on page 45 of the business case details the net loss to revenue account of £1.271m in 2011/12 and £2.703m in a full year.

5.3 This is slightly greater than the loss of income than the level of £0.684m assumed within the revenue estimates for 2011/12 and Council would have two options available to fund this shortfall in 2011/12. The implementation date could be delayed until 1 January 2012, or the shortfall could be financed from savings elsewhere within the revenue budget or from the modernisation fund.

5.4 Given the financial pressures facing the Council's revenue account, it is considered that the first priority for Council will be to utilise this receipt to generate revenue savings of at least an amount equivalent to the full year revenue loss of £2.703m. This can be achieved in a number of ways – through spend to save proposals, income generation opportunities or by the partial repayment of debt charges.

5.5 Members are reminded that Council will be required to demonstrate "value for money" to its external auditors in relation to the investment of the receipt. To assist with this process, a template (Appendix F in the Business Case Report) has been included within the business case which, if approved, would allow for the revenue benefit of all proposals to be quantified, scored on a consistent basis and assist with the monitoring of the benefit achieved thereafter and would supply transparent audit evidence.

5.6 It is likely that depending on the investment options selected, that the full receipt will not be required in one sum and that a drawdown profile perhaps over a two year period will have to be negotiated with the successful funder. As this would involve payment of a commitment fee, it is recommended that cost benefit analysis is carried out at the relevant time to determine if any advantage may be obtained from accessing the receipt in one sum and using it to temporarily offset the Council's borrowing requirement.

5.7 In relation to the proposal in section 5.3.2 of the business case – Alexandria Shopping Centre, it is recommended that in order to maximise the level of the potential return that the Council earmarks within its core general services capital programme, a commitment to fund the necessary investment works of £0.770m over a 2 year period.

5.8 To maximise the return to the Council through the annual dividend payment it is desirable that the LLP takes full account of the VAT opportunity to "Opt To Tax" (OTT). Based on the planned repair and renewals programme within the cash flow forecast, it would cost the LLP approximately £75,000 pa should it not OTT. Furthermore, the 31% of the draw down monies would be subject to a one off VAT payment (in respect of the Clyde Shopping Centre). OTT would have the effect of increasing rent levels by 20% which would be difficult to promote in a recessionary period, however, this would have no impact on the tenant should they be VAT registered. To minimise this impact, it has been assumed that the LLP will elect to tax only on retail units where it is expected that the majority of the tenants will be VAT registered. In the remaining units, it is proposed that as they may have a number of start-up tenants who could potentially be below the current VAT threshold that they should be exempt and no VAT charged on those premises.

5.9 It is recommended that the Council agrees to provide a guarantee to the funders that should the LLP be unable to meet all the annual repayments in any one year to the bank then the Council would be obliged to make good the shortfall in that year. There would not be a requirement to fund the full outstanding loan balance.

5.10 The value for money assessment of the proposal was demonstrated by developing a Public Sector Comparator (PSC) model which compares the business case against the cost to the Council of borrowing £35m from the Public Works Loans Board in a traditional 25 year annuity loan.

5.11 The details are provided within table 11.1 which indicates that the base case provides a value for money benefit of £0.294m over the length on the project.

5.12 While the base case and the PSC model provide a broadly similar benefit in pure financial terms, it must be reminded that the base case provides a number of additional key benefits:

- £13.395 m additional investment (real terms) in the total asset base;
- a positive public perception on the Council's stewardship of its property assets; and
- the investment means that in 25 years time the Council has a fit for purpose investment portfolio.

5.13 The direct costs incurred to date by this project relate to the preparation of the Feasibility Study (£35,093) and the Business Case (£62,494). These will be funded from the Council Modernisation Fund. Any further direct costs that will be incurred in taking this proposal forward will be funded, depending on their nature, either from the Modernisation Fund or accommodated within the project costs. Full details will be reported to Council.

6. Risk Analysis

6.1 Many of the risks and means of addressing them are addressed in Ernst and Young's business case. Key risks are:-

- the Council uses the loan for purposes which do not cover the £2.7m per annum shortfall in revenue through withdrawal of the rent income. The template prepared by Ernst and Young provides a means of quantifying and scoring the expected benefits of each project in terms of reducing the ongoing revenue budget of the Council;

- there may be conflicts between the LLP having a more focussed commercial approach to these particular properties as opposed to the traditional Council approach which also considers issues of regeneration, needs of community groups and individual constituents. While the commercial focus of the LLP will be tied up by way of a Member's Agreement between the Council and the LLP, as the Council has control of the LLP it would in theory be open to the Council and the LLP to change that agreement going forward. It should however be emphasised that a loan will only be obtained for at best rates if there is a commitment to a more commercial management of these properties for the next 25 years. The lenders are likely to want to have ongoing financial diligence to ensure that this commercial focus remains for the period of the loan. The loan agreement is therefore likely to restrict the ability of the Council and the LLP to amend the Members' Agreement to take a less commercial approach. Therefore Members in agreeing to the project need to understand that the LLP will need to have a commercial approach to these properties as its first consideration;

- in case sale of the Council's interest in Clydebank Shopping Centre as securitisation of the remaining assets is considered an option it should be pointed out that:

  (a) the sale price of £24m is not greatly in excess of the securitisation value of £22m, with the significant difference that after 25 years the Council would still own the asset; and

  (b) it is extremely unlikely that the remaining investment assets would be an attractive option for any lender.

  The remaining stock might have too small a rental value to interest lenders. The length of leases of the remaining stock is not as long as that

of Clydebank Shopping Centre, which would raise the risk profile and cost of loan;

- there is a risk that some lenders might require a break option after say, five years. The Council would then have to refinance the loan, at a potential higher rate. While other lenders may not require such a break option, the certainty that this provides would need to be weighted against the possible extra cost of such a long-term loan;

- if the Council decided not to give a guarantee and to mortgage the properties in security of the loan this would have a number of effects. Firstly it would be treated as a property deal and result in worse terms of loan. Secondly it would result in a significant amount of complex legal work which could delay the project as due diligence to the lender's satisfaction would need to be undertaken on every property. Thus it is recommended that the guarantee is given;

- it is likely that the rate of interest which will be charged on the loan will be more than that charged on a similar loan from the Public Works Loan Board. It should however be emphasised that the commercial approach to managing these rent producing assets is also a key part of the proposal. This should result in the assets being improved with both regeneration/economic development benefits and higher rental stream. At the end of the loan the properties would be returned in a much better condition than if the Council had merely borrowed under PWLB. Chapter 12 of the Ernst and Young Business Case analyses the respective merits of borrowing on PWLB and under this project and shows that this project produces overall better value for money, compared to a PWLB loan;

- the Council occupies a number of properties which are to be included in the project. If, resulting from the Council's Asset Management Strategy it vacates these properties then this will reduce the rent available to pay the loan unless an alternative occupier can be found;

- there are a number of other legal issues which will need to be resolved including the possible TUPE transfer of some staff, the need for a Members Agreement between the Council and the LLP to properly cover issues which may arise and for a Transfer Agreement setting out the transfer of the estates management functions. There are also public procurement and state aid issues which will need to be addressed as part of the structure. The Business Case has involved Harper McLeod Solicitors in giving advice and the project has been structured in such a way as to deal with all of these issues. It should however be noted that changes to the governance structure detailed earlier in this report may have knock on effects on such issues;

- it is also important that competition is maximised between funders and thereafter there is a robust evaluation of submissions; and

- in common with all other cases where Councillors serve on the Board of an external body, such Councillors will require to owe their primary duty to the LLP and declare an interest where there is a clear conflict of interest between the LLP and the Council. If the Board of the LLP is entirely drawn from Councillors this could result in the entire Board having to declare an interest. This issue could be addressed by having an officer or external commercial membership of the Board.

6.2 The interest cost on the facilities is based on the anticipated interest rates that are forecast to be in place at the estimated financial close date of 1 October 2011. There is a risk that the actual rates could be affected either by wider movement in rates than forecast or by a change to the date of financial close. A buffer has been allowed to mitigate against any such movement and full detail will be reported should the proposal progress to financial close.

7. Equalities Impact

7.1 No significant issues were identified in a screening for potential equality impact of this report.

8. Conclusions and Recommendations

8.1 Both the Feasibility and Business Case outlines the suitability of our Non-Operational Portfolio in raising a significant sum of finance - £35.1m through the successful securitisation of these assets with a selected financial institution.

8.2 Soft market testing has identified that 3 such institutions have confirmed their interest and willingness to provide the debt finance subject to their normal diligence procedures.

8.3 Comparison with the costs of servicing this debt through securitisation and a straight forward loan for the same £35.1m through the Public Works Loans Board shows that the former approach is a marginally lower cost option. However, this simple comparison does not take account of the significant reinvestment of £13.395m over the period of the lease to the LLP in the property portfolio, nor does it take into account of the total dividend payments of £16.585m over the 25 years to the Council from the LLP through the securitisation option.

8.4 The commercial focus of the LLP and the approach to the management of the property portfolio has been confirmed as a required element of the model from all the banks interviewed.

8.5 The Loan with the bank will not be with the Council but will be with the LLP, which will be 100% owned by the Council. The Council will be expected to guarantee any shortfall in any repayments in a particular year but would not be asked to guarantee the loan in full.

8.6 The contribution which the Clyde Shopping Centre makes in terms of a 31% share of our overall rental income and the length of the leases relating to the centre, makes it an essential element of this securitisation model going forward from a financial scale and risk management perspective, both for the Council and the potential investor.

8.7 The risks identified would all be considered and mitigated within the detailed Business Plan.

8.8 If the Council wished to progress with this securitisation approach, the next steps would be to identify appropriate external advisors through procurement using the catalyst framework to assist the Council in preparing all the necessary documents, information and legal and financial advice, including the setting up of the LLP. This would then allow the Council to put an invite out to interested financial institutions to submit and discuss with the Council their best terms for providing debt finance through the LLP via a funding competition.

<u>Recommendations</u>

8.9 The Council is recommended:

(i) to procure external advisors by tender under the terms of catalyst to prepare a detailed business case for the project;

(ii) thereafter providing the detailed business case does not reveal any significant changes to the viability of the project as detailed in the business case (in which case a further report should be made back to Council) to invite the investment market to put forward their best terms by way of a funding competition to provide debt finance to the LLP.

(iii) that a report come back to the Council in September 2011, for consideration of the preferred financial institution proposal for consideration and approval;

(iv) that the Council agrees to opt to tax for VAT in accordance with the proposal outlined in paragraph 3.2.12;

(v) to agree that funding £0.770m for the refurbishment of the Alexandria Shopping Centre is included within the committed expenditure of the general services capital programme over a 2 year period;

(vi) to note that an essential component of the project is the creation of a new company and Limited Liability partnership with commercial objects, both of which would be 100% owned by the Council;

(vii) to note that the project involves the assignation of rents from the Council's investment properties (excluding Common Good) to the Limited Liability Partnership for a 25 year period;

(viii) to note that the project involves the Council in guaranteeing the loan provided to the Limited Liability Partnership and authorises the Director of HEED in consultation with the Head of Legal, Administrative and Regulatory Services and the Head of Finance to agree the terms of any guarantee;

(ix) to note that the Limited Liability Partnership would be responsible for the estates management of the investment assets, which would be managed on a commercial basis;

(x) to note that this may involve the transfer under TUPE of some Estates Section staff to the body providing estates management of the assets which transfer;

(xi) to note that the Limited Liability Partnership would procure finance, IT, HR, Legal and administrative support from the Council;

(xii) to note the levels of investment in the assets proposed over the 25 year period as detailed in the report;

(xiii) to note the importance of the loan being spent for purposes which reduce the Council's revenue budget and for purposes which enhance the wellbeing of West Dunbartonshire and its inhabitants; and

(xiv) to note that a report will come to June Council comparing and assessing options for spend of the loan.

Elaine Melrose
Executive Director of Housing, Environmental and Economic Development
Date: 17 January 2011

Person to Contact: Jim McAloon, Head of Housing and Regeneration
Council Offices, Garshake Road, Dumbarton G82 3PU
Tel. No. : 01389 737401
jim.mcaloon@west-dunbarton.gov.uk

David Connell, Head of Finance and ICT
Tel. No.: 01389 737191

Andrew Fraser, Head of Legal, Administrative and Regulatory Services
Tel.No.: 01389 737800

Appendices: Appendix 1: Business Case

Wards Affected: All