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To: Corporate Policy Overview Committee - 28 May 2008

Subject: Property Disposals

Classification: Unrestricted

1. Introduction

This report provides the Corporate Policy Overview Committee with information on the property disposal process, followed by a commentary on the disposals outturn for 2007/08 and the indications for the Medium Term Plan period in the light of the sharp and continuing fall in the property market in recent months.

2. Property Disposal Process

2.1 Property disposal decisions, and the process from start to completion, involve officers from Service Directorates, Property Group, Finance, Legal and Members. There are two categories of property disposal, which are accounted for differently:

2.1.1 Earmarked or ‘back to back’ disposals, where the disposal is promoted by a service directorate for reinvestment in a new capital project to provide replacement/enhanced services. The Directorate releases operational land whose capital value goes wholly or partly towards the capital investment project. The identification of this operational land with potential for sale involves joint working between Property Group and Service Directorates in the context of the latter’s development planning/MTP process for new capital projects, and there will be ongoing joint working on the timing and manner of the disposal.

2.1.2 Non-earmarked disposals. These concern the release for sale of non-operational land and property which is surplus to Directorate requirements. KCC owns a significant number of sites of this nature, typically relatively small in size and of small-medium capital value (by comparison with most earmarked disposals), but in aggregate representing significant opportunity for reinvestment of the disposal receipts in new value generating investments or debt repayment. Receipts from sale of this category of disposals are placed in the Property Enterprise Fund, established by County Council in November 2006.

2.2 Prior to a decision to market a site for disposal, the potential suitability of the land/property for other KCC operational purposes by other directorates is assessed. In considering the disposal of any school land, regard is had to the need to retain sufficient provision for current and forecast educational need. Any land disposal (including playing fields) or closure of a school requires central government approval. This involves a rigorous analysis of the remaining land to establish its sufficiency in this context. While there is a need to generate funding locally as far as feasible to resource new school projects, the interests of the local community are taken account of in this review process. Officers from CFHE and Property have consulted with a number of districts in recent years with a view to transferring the occupation and/or management of part of surplus playing fields to districts or town councils.

2.3 Consultation. The Property Management Protocol requires the Director of Property to consult with the Cabinet Member for Finance on all disposals and to inform him/her of the comments of local Members before final decisions are taken. Accordingly, Property Group send out consultation letters to local Members no less than 6 weeks before a sale of any property interest is due to be concluded. In the case particularly of earmarked capital receipts, the capital projects to which the disposal of land is inextricably linked will typically have been several years in gestation, and the subject of consultation with users and local Members and in the public domain generally.

2.4 In all cases, Property Group ensures that best value is achieved through competitive, open marketing via sale at auction or marketing through external property agents.

3. Disposals in 2007/08

3.1 Earmarked disposals. The property market began to slow down in the third quarter of last year, and this accelerated steeply in the fourth quarter. A number of previously agreed sales were lost or renegotiated by the purchasers during February and March. Nonetheless, some £23m of disposals were completed by the year end. With one of these disposals, following consultation with the Cabinet Member for Finance, it was agreed with the purchaser to accept deferred payment of £4.5m in the current financial year. Contracts were also exchanged on the sale of Senacre school, with an agreed completion date of September 2008 which will bring in a further committed £21.63m.

3.2 Property Enterprise Fund. Property Group has embarked on a vigorous disposals strategy aimed at unlocking the Council's non-operational asset base. By the end of 2007/08, a total of 100 surplus, non-operational sites had been disposed of with a value of £9.4m. This achievement was helped significantly by an extremely buoyant market for small development sites at auction for the first half of the year. Three investments have so far been made via the Property Enterprise Fund. Two are designed to stimulate regeneration and economic development in East Kent through the acquisition of the Manston Business Park and the forward funding of the Eurokent spine road, in the vicinity of Westwood Cross. The third is the acquisition of a strategic land parcel at Upper Stone Street, Maidstone to add KCC's ownership of Wren's Cross. A comprehensive redevelopment is now being worked up.

4. MTP and current property market

4.1 The 2008-11 Medium Term Plan sets a challenging programme of earmarked disposals, notably in support of the CFHE capital programme. The Appendix to this paper lists the principal sales which Property Group are currently working on, representing some £140m of receipts over the three year period of the MTP, based on estimates in January 2008 prior to the finalisation of the MTP for Cabinet and County Council Approval. A further £40m of receipts over the medium term plan period were at that time identified on an aspirational basis by Directorates, but which were not yet in a position to be actively worked up by Property Group.

4.2 Until the autumn of last year, the property market had enjoyed successive years of growth in values and volumes, supported by a strong economy, pent-up demand for new housing, and relatively easy credit terms. As noted above, a change in market sentiment was evident by the end of the last year, but was generally assumed at that time to represent a market adjustment to values which had become over-inflated. The adjustment was reckoned to be between 5%-15%, and some disposals at the end of the last financial year were concluded on this basis (and/or by accepting deferred payment of receipts as also noted above) following a judgment call on the opportunity costs and risks of withdrawing sales and going through the marketing process a second time. At this point all predictions indicated a relatively short dip in the market with recovery through the remainder of 2008.

4.3 The collapse of Northern Rock, and the well publicised difficulties of other financial institutions with major exposure to property lending and adverse press coverage regarding market sentiment, catalysed not only a further rapid fall in values but a crisis of confidence across all sectors of the property market and a severe tightening of lending terms (the “credit crunch”). In March house prices experienced their biggest monthly fall since 1992. The number of transactions has fallen rapidly, and some major housebuilders have ceased work on new starts. Most housebuilders (who have been the mainstay of KCC’s earmarked sales in recent years) have now withdrawn from acquisitions at the present time. We have local market evidence of a major site where bids have recently been returned at only 60% of predicted value. Not surprisingly given this rapidity of change over such a short period, there is little agreement by market analysts on the likely length and depth of the downturn, although the general prediction is at least a 2 year period. It is therefore conceivable that it could last for much of the period of the MTP. Even if lending terms to new borrowers are eased in a shorter timeframe, this will not of itself restore pre-2008 property values (or capital receipt expectations) given the prognosis for the health of the wider UK economy.

4.4 Property Group’s response to the current realities of the property market will be broadly characterised over the coming months by the following factors and approaches:

i) Each property site has different characteristics in the market and will not be equally affected in terms of value. Careful assessments will be made over the optimum approach to taking each site to the market, and in the light of remaining alert to changing market conditions and sentiments. This will include greater willingness to enter into transactions which spread the receipt across financial years, and negotiation of higher levels of overage (a further return to KCC once development is complete, in recognition of a lower initial receipt).

ii) Joint decisions will need to be made with directorates over the priority they attach to different levels of potential capital receipt over different timescales, in relation to their capital project commitments and aspirations. In some cases, directorates may have the straight choice of deferring capital projects which depend on a level of capital receipt unachievable currently. Judgements will need to be made in each case over the pros and cons of holding on to the asset versus selling now, and then whether to accept the reality of what the market bids for sites.

iii) Directorates may also be able to discuss with Finance proceeding with the capital project on the basis that funding can still be provided now (eg from prudential borrowing) pending sale of the property asset at a later, more favourable date.

iv) The approaches at ii) and iii) are considered inherently preferable to undertaking ‘fire sales’ at less than the real underlying value of the county council’s assets.

v) Although many investors and purchasers, including most of the major housebuilders, have withdrawn from the market we are already seeing a return of those investors who were active in the 1990s such as private property companies, private and overseas investors and overseas funds. We will be crafting development and marketing briefs to draw in these potential purchasers. The Housing Association sector also remains an active purchaser of sites (and has bought a significant number of unsold completed private housing units)

vi) The current market, with its time lag before building activity will realistically start, lends itself to exploring joint venture arrangements under which the county council could share with a third party investor the costs and risks of working up more complex property sites (including securing planning consents) and then sharing in the value created by the eventual disposal or joint development when the market returns. A number of sites are being considered for this approach with those known to operate in the market.

vii) This approach has the advantage of potentially releasing a capital receipt now in return for an enhanced shared capital value. The disadvantage which needs to be assessed is the extent of the risk premium required by the JV partner, and the superiority of the arrangement in enhancing asset value compared to the county council simply retaining the asset for disposal itself when healthy market conditions eventually return. The establishment of a Special Purchase vehicle to package a number of sites together to facilitate such JV’s is also being considered. The legal and tax implications of this option will need to be carefully evaluated.

viii) There are a number of complex sites in the MTP whose capital receipt is not scheduled until years 2 and 3. This applies especially to those identified as part of the Building Schools for the Future funding. Property Group are working closely with CFHE and the Cabinet Member for Education to conclude the work necessary to secure certainty on site availability and to maximise site values before actual marketing can start in, possibly, more favourable market conditions.

ix) All the issues listed above will be the subject of ongoing meetings with senior officers and Cabinet Members as appropriate across Directorates and with Finance. They are also due to be fully addressed at the next meeting of the Property Board chaired by the Chief Executive in early July.

Mike Austerberry
Director of Property

APPENDIX
2008-11 MTP CAPITAL RECEIPTS
EARMARKED SALES AGREED WITH PROPERTY GROUP
Sturry Depot site, Canterbury
Preston Depot (Faversham)
Middlefield/Rusthall, Tunbridge Wells
SS Housing Portfolio, across County
Houses on the former Edenbridge School site (once new community is built)
Newington Library (once vacated), Ramsgate
Associate House, Ashford - Linked to new Ashford Gateway Plus
Memorial Hall, Gravesend (once service ceases)
Southdowns Respite Centre - property now closed, Doddington
Former St Leonard's Junior School, Hythe
Swinford Manor, adjacent to Goldwyn School, Ashford
22 Skinners Rd (Right to Buy application), Lydd
Land adjacent to Herne Bay Junior School, Herne Bay
Land adjacent to Hugh Christie School, Tonbridge
Doddington Primary school - closed school
Dartford Campus Site 3
Former Millstream Junior School, East Malling
Senacre Site (Surplus school) - exchanged
Land adjacent to Pembury School
land next to Minster in Sheppey Primary School
Leigh City Tech College, Dartford
South School, Ashford
Crockenhill CPS (Red House), Swanley
Land adjacent to Downsview School, Swanley
South Deal School (once closed)
Former Birchwood School, Swanley
Kingsmead - inc 9 St John Place, Canterbury (linked to new school)
Surplus land following Isle of Sheppey School review
Montgomery/Spires Academy (linked to new Academy)
Land adjacent to Phoenix School, Ashford
Surplus land to be decided at Beaver Green/Hopewell School, Ashford
Axton Chase School (surplus land linked to new school), Longfield
Surplus land at Foxwood & Highview Schools following new school construction, Folkestone
Land adjacent to the former Channel School, Folkestone
Hereson School (following amalgamation with Ellington School), Broadstairs
The Mount, Wilmington
Mountwood/Horizons , Westerham