

**Manchester City Council
Report for Information**

Report to: Resources and Governance Scrutiny Committee – 18 July 2024

Subject: Review of Development Agreements

Report of: Director of Development

Summary

This report provides an update on the processes regarding development agreements, monitoring arrangements and overages pertaining to new development across the city on Council land and assets. An outline is provided on the governance arrangements along with how agreements are negotiated, managed, and monitored.

Recommendations

The Committee is recommended to note the contents of the report.

Wards Affected: All

Environmental Impact Assessment - the impact of the issues addressed in this report on achieving the zero-carbon target for the city	None
Equality, Diversity and Inclusion - the impact of the issues addressed in this report in meeting our Public Sector Equality Duty and broader equality commitments	Major development agreements or similar contractual arrangements require an Equality Impact Assessment prior to finalising the commercial terms and seeking relevant Council approval. Where the Council's land or property interests are located within an area subject to a Strategic Regeneration Frameworks, or similar, a further EqIA may have been undertaken through the adoption process.

Manchester Strategy outcomes	Summary of how this report aligns to the OMS/Contribution to the Strategy
A thriving and sustainable city: supporting a diverse and distinctive economy that creates jobs and opportunities	N/A
A highly skilled city: world class and home grown talent sustaining the city's economic success	N/A
A progressive and equitable city: making a positive contribution by unlocking the potential of our communities	N/A
A liveable and low carbon city: a destination of choice to live, visit, work	N/A
A connected city: world class infrastructure and connectivity to drive growth	N/A

Full details are in the body of the report, along with any implications for:

- Equal Opportunities Policy
- Risk Management
- Legal Considerations

Financial Consequences – Revenue

N/A

Financial Consequences – Capital

A robust and transparent process governing the negotiation, management and monitoring of the obligations within development agreements is key to achieving delivery outcomes including overage or performance related development payments.

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1.0 Introduction

- 1.1 Development of real estate is a key facilitator of delivering the Council's growth ambitions and facilitating corporate priorities by channelling investment to deliver new housing, employment opportunities and unlocking regeneration. The Council has a long and successful history of promoting regeneration across all parts of the city and the use of its land and building resources is key in achieving that success.
- 1.2 This report looks at the mechanisms the Council uses to support this activity and the governance in relation to development agreements and agreements for lease where the Council agrees to sell or lease assets. It will also set out the steps taken to align this process with the Council's due diligence framework and best practice.

2.0 Background

- 2.1 Where the Council is promoting land for development or regeneration schemes development agreements and agreements for lease have been used extensively as a contractual mechanism to leverage inward investment and retain control for the Council as Landlord. In addition, a number of corporate Joint Venture companies have been created to cover larger multi-phase regeneration schemes, such as Victoria North on Northern Gateway or Mayfield Partnership at Mayfield. Often the JV Company is not directly contracting for the construction of the development, but these arrangements contain profit sharing arrangements, akin to an overage.
- 2.2 Development agreements will contain a contractual framework setting out the parties' obligations in relation to delivering the development or investment contemplated under those arrangements, which generally culminates in a series of conditions that need to be met before a lease or transfer of land will be completed.
- 2.3 On drawdown of the interest in land, there will generally be a further set of development or delivery milestones covering the construction activity. Typically, such agreements will also contain overage or profit related payments on conclusion of the development obligations, along with provisions to terminate arrangements early if the milestones are not achieved by the relevant dates.
- 2.4 Whilst there are a number of common factors in these types of agreements, they are by their nature bespoke, and relate to the investment and development of unique plots of land in areas that require particular solutions to deliver the outcomes the Council wishes to achieve, in line with the Council's strategic aims and objectives.
- 2.5 Procurement of the partner must be undertaken in line with the relevant statutory and legislative frameworks including Public Contract Regulations, subsidy control rules, as applicable, and must satisfy the Council's obligations to secure Best Consideration/Value for its land

3.0 Main issues

3.1 Non-Standardisation of Approach

- 3.1.1 This number and variety of contractual relations results in a lack of standardisation within the agreements the Council has in place. The often-long term and bespoke nature of these agreements means that they will need to contain specific conditionality and milestones to be achieved.
- 3.1.2 This section of the report sets out some of the examples that are in place. Governance arrangements will vary depending on the size and scale of the agreements. The larger, more complex matters, often have a Joint Board arrangement and often it is the Joint Board that takes on the responsibility for requesting and recommending for approval the information required to satisfy the conditionality (for example commercial plans) or signing off milestones. The termination provisions or process to conclude and close out these agreements is also often bespoke to the nature of the underlying development.
- 3.1.3 There are a number of historic agreements, particularly related to activity in and around East Manchester which were entered into as part of the NEM Urban Regeneration Company activity. Most of these have formally concluded or terminated, but there are a small number that remain extant with legacy issues to resolve, such as Beswick and New Islington Waterfront.
- 3.1.4 In addition, there are a number of long-term contractual agreements governing major regeneration schemes in the City Centre, such as Spinningfields, NOMA, Smithfield, First Street, St Michaels that are in various stages of their life cycle and will take years to reach full conclusion.
- 3.1.5 The Council also has formal corporate Joint Venture arrangements with parties to oversee development such as Airport City, Mayfield, Victoria North, Manchester Life, Eastlands Development Company and Manchester Science Park.
- 3.1.6 Joint Venture arrangements are also used as a housing investment vehicle to leverage private funding to kickstart housing delivery, such as Manchester Life and Matrix Homes.
- 3.1.7 There are a number of site-specific development agreements, which take the form of Agreements for Lease and Lease across the City, notable ones include the redevelopment of the Ramada site on Deansgate, Crown Street and Great Jackson Street with Renaker and Central Park with TfGM.
- 3.1.8 The Leasehold & Freehold Act 2024 received Royal Assent before the dissolution of Parliament and will impact on the councils ability in the future to use agreements for lease for residential development – particularly given the ban on the creation of new leases for residential houses for a term of more than 21 years. Apartment leasehold disposals remain unaffected.

- 3.1.9 The above are all forms of agreement between the Council and other parties governing the development of land and/or buildings where the Council has some form of ownership. A number of these relate to schemes where the Council has limited or partial ownership and therefore has to strike a balance in respect of the commercial considerations alongside achieving other corporate objectives.
- 3.2 Whilst there will always be a negotiation to be had with development partners, their funders and investors in relation to the detailed terms and conditions for these agreements, we recognise that simplifying and standardising the main heads of terms would assist in providing a transparent and more efficient approach going forward. A streamlined approach to these agreements with conditionality limited to key issues and development milestones linked to key events will assist in the active management and monitoring of development agreements. These principles form the basis of a template heads of terms for Development Agreements/Agreements for Lease which are a starting point for negotiations. The final terms will be subject to negotiation and will reflect the level of control the Council has over the subject site(s).

3.2.1 **Overage and Performance Related Profit**

- 3.2.2 Development agreements often include a standard clause for the Council where the final scheme is not yet known, or where there are a number of unknowns or variables that would impact the site valuation. This is essentially a way for the vendor of land to protect itself financially should the developer secure a better outcome through planning or achieve a greater level of profitability from the scheme than initially forecast. Whilst a simple concept, contractual arrangements for documenting overage are generally complicated as it relates to future scenarios. The negotiation of overage when triggered becomes even more onerous as it generally requires an open book approach to analysis of development accounts, often multi-phased.
- 3.2.3 Last year PwC were appointed to undertake a peer review of overage arrangements to provide assurance on our practices. This resulted in a due diligence checklist that is now used to inform the basis of standard overage arrangements.

3.3 **Due Diligence**

- 3.3.1 With the implementation of improved commercial governance, new due diligence principles have been adopted. These are:
- 3.3.2 A tailored due diligence checklist and form has been developed for development JVs and agreements. This has been adopted by the service when entering into new agreements. The relevant due diligence information is provided to the decision maker, at the point the decision is made to provide an auditable assurance trail.

- 3.3.3 Adopting these revised arrangements, along with closer working arrangements with colleagues in City Solicitors and Finance will give a greater level of assurance at the point of entry into the agreements and transparency through the life of the agreement.
- 3.3.4 The information stored in the Council's property database, CPAD, including diarising of condition precedent and development milestone dates to provide an automated tracker for officers on key contractual events.
- 3.3.5 The due diligence framework and adoption of best practice provides assurance for new agreements. Work is also underway to apply these standards to existing arrangements to regularise the assurance, management and monitoring and ensure a robust approach is in place. A prioritised approach has been adopted with the top 20 of the Council's major development joint ventures and development agreements prioritised for review.
- 3.3.6 The review will include undertaking a due diligence analysis of the Council's development partner(s) including where appropriate, investigating the status of the parent company and any other party where guarantees exist/are proposed. There will also be a comprehensive review of the relevant contractual documentation, including any variations of the original agreements, detailing party's obligations, project governance arrangements, conditionality and development milestones. This will be subject to a health check with colleagues from the Commercial Governance and Finance teams to ensure scheme and portfolio level risks are documented and managed and monitored. This is an ongoing process and work will be concluded in the Autumn.
- 3.3.7 The enhanced governance approach proposed will ensure best practice is consistently applied and documented to support the corporate risk management and business continuity frameworks. It will also encompass existing project governance arrangements and the efficacy of these in line with best practice.

4.0 Development Agreements Review

- 4.1 In line with our commitments to best practice, a periodic review of our use of development agreements has been completed by Ernst & Young earlier this year. Led by the Head of Commercial Governance with input from the Development, Finance and Legal functions of the Council.
- 4.2 The final report will be submitted for approval to the Councils Commercial Board on the 17th July 2024. Whilst no major issues were identified, broad recommendations have been provided to standardise the management process and ensure continuous improvement:
1. Promote opportunities for learning and development to ensure more officers at the council have the skills to manage the process.
 2. Ensure contracts and processes support each other.

3. Integration of agreements onto the Councils CPAD property management system.
4. Biannual review report to Commercial Board on progress

5.0 Recommendations

- 5.1 It is recommended that the Committee note the contents of the report.