

CABINET

3 March 2015

SILVER HILL – JUDICIAL REVIEW DECISION

REPORT OF CHIEF OPERATING OFFICER – AS MONITORING OFFICER

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RECENT REFERENCES:

CAB2526 – Silver Hill Update and Land Transaction - 4 November 2013

CAB2603 - Silver Hill Regeneration - 10 July 2014

CAB2607 – Silver Hill Affordable Housing Review – 6 August 2014

PDC1012 – Silver Hill 2014 Planning Applications – 11 December 2014

CAB2647(Revised) – Budget and Council Tax 2015/16 – 11 February 2015

EXECUTIVE SUMMARY:

This report outlines the immediate actions for Cabinet to consider in the light of the recent Judicial Review decision affecting the Silver Hill Project, and the ruling that the proposed variations to the Development Agreement authorised by Cabinet on 6 August 2014 are unlawful. A decision will need to be made upon whether an appeal should be lodged by 4 March 2015. Advice from Leading Counsel will be available for Cabinet to consider in exempt session.

The Council's external solicitors, Berwin Leighton Paisner, will also be available at the meeting.

The report indicates that Cabinet should start to consider its options for the future at its meeting on 18 March, which would then be referred to full Council for it to consider.

Cabinet should also consider how the proposed Independent Review should be established.

RECOMMENDATIONS:

- 1 That it be noted that the legal documentation to give effect to the variations to the Development Agreement authorised by Cabinet on 6 August 2014 (CAB2607 refers) should not be executed, in view of the High Court decision that the proposed variations are unlawful, and the authorising Cabinet decision has been quashed by the High Court [unless the Cabinet determines that it wishes to appeal that decision to the Court of Appeal and the appeal is upheld].
- 2 That a report be brought to Cabinet at its meeting on 18 March 2015 to commence consideration of future options for the Silver Hill Project and Cabinet also consult full Council on the way forward.
- 3 That Cabinet consider how an Independent review can be established.
- 4 That consideration be given in exempt session to whether an appeal should be lodged in respect of the High Court decision, noting that the initial papers would need to be lodged with the Court by 4 March 2015.
- 5 That the position with respect to award of costs in respect of the existing litigation be noted and the Chief Executive, in consultation with the Leader, be authorised to determine whether to agree a negotiated figure or to leave the matter to be determined by the Court.

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DETAIL:

1 Introduction

- 1.1 Councillor Gottlieb applied to the High Court for a judicial review of the decision of Cabinet on 6 August 2014 to authorise variations to the Development Agreement with Henderson, which would allow the Silver Hill regeneration scheme to go forward.
- 1.2 Judicial Review is a court hearing in which a judge reviews the lawfulness of a decision or action made by a public body. It deals with the lawfulness of a decision, and is not about the merits, or otherwise, of the Project itself.
- 1.3 The initial application for permission to apply for Judicial Review and to proceed to a full hearing was based on three grounds – that the Council was in breach of EU Procurement Directives, had not complied with EU rules on state aid, and had not obtained best consideration.
- 1.4 Mr Justice Dove dismissed this application on all three grounds on 7 October 2014. A copy of the Order is attached as Appendix 1. Mr Justice Dove at that stage said it was “unarguable that the variations the subject of the decision under challenge required a procurement exercise under Directive 2004/18/EC or the Public Contracts Regulations”. He referred to provisions in the 2004 Development Agreement that allowed variations to be made. He went on to say “The variations did not amount to the creation of a new contract but were within the ambit of the existing agreement”. At that stage the Council was awarded £7,500 costs against Councillor Gottlieb. However, this is no longer applicable in view of the subsequent decision on the Judicial Review.
- 1.5 Councillor Gottlieb re-applied to the High Court on 18 November 2014. On this occasion Mr Justice Lindblom granted permission on the first Ground only to proceed to a full hearing, on the basis that it was arguable that the variations to the Development Agreement were so material that the Council was required to undertake a EU procurement exercise under the Public Contract Regulations 2006. A copy of the Order is attached as Appendix 2.
- 1.6 The hearing took place on 28/29 January 2015 before Mrs Justice Lang. Judgement was delivered on 11 February 2015. The full judgement, including a detailed summary of the facts upon which it is based, is shown as Appendix 3.

1.7 Mrs Justice Lang summarised the respective position of the parties as follows:

“6. The Claimant contends that the variations to the Development Agreement are such as to require a procurement exercise to be undertaken on the ground that they are materially different in character from the original contract and, therefore, are such as to demonstrate the intention of the parties to renegotiate the essential terms of the contract. The variations changed the economic balance of the contract in favour of the developer in a manner which was not provided for in the terms of the initial contract.

7. The Council’s response is that the variations are not materially different in character. They were made in accordance with variation clauses in the Development Agreement, and they do not change the overall nature of it. They still fall within the scope of the original brief. Some of the changes were prompted by external causes; others by changes in circumstances since 2004. The Council has taken independent professional advice which states that the changes do not alter the economic balance in favour of the developer. Indeed, the Development Agreement, as varied, is a more favourable arrangement than the Council would be likely to obtain in the market.”

1.8 Mrs Justice Lang found in favour of Councillor Gottlieb. She held that the Council’s decision on 6 August 2014, to authorise variations to the Development Agreement, without carrying out a procurement process as required by Directive 2004/18/EC and the Public Contracts Regulations 2006, was unlawful and the decision be quashed. The Order is attached at Appendix 4.

1.9 The Council was ordered to pay the claimant’s costs – which would be subject to detailed assessment (taxation through the court) if not agreed between the parties in 21 days.

2 Background to the Council’s Decision

2.1 In 2004 the City Council entered into a Development Agreement with Thornfield Properties (Winchester) Limited to regenerate a large and run-down area of Winchester Town Centre known as Silver Hill. The Council had entered into sole negotiations with Thornfield as it had an agreement with a large landowner within the site – Stagecoach. The Council did not run an EU procurement for a developer as it had advice from its then external solicitors, Decherts, that they were satisfied that the proposed development agreement and lease were essentially a single land transaction that fell outside the scope of the procurement regulations. The Council was also advised by Drivers Jonas (later to be incorporated into Deloitte) that the proposed arrangements satisfied the best consideration requirements. The Council proceeded to enter into the Development Agreement.

2.2 In 2009 the Council granted planning consent for a mixed use redevelopment including approximately 95,000 sq.ft of retail space, 287 residential units 330 public car parking spaces, a new bus station, some office space and public realm improvements.

- 2.3 In 2010 Thornfield Properties plc entered administration and their subsidiary company Thornfield Properties (Winchester) Ltd was acquired by Henderson Global Investors (now known as TH Real Estate). In 2011 the Council made a Compulsory Purchase Order to enable assembly of land and property rights necessary to undertake a development. This was the subject of a public inquiry in 2012 and the Secretary of State's decision to confirm the CPO was made on 20 March 2013.
- 2.4 Henderson and the Council subsequently had discussions, that with changes to the property, housing and retail markets, the scheme needed updating. They had also been advised by Stagecoach, the major local bus operator, that they no longer required a bus station in the form approved. After a thorough review, revised proposals in the form of variations to the scheme approved in 2009 were brought forward. The revised scheme included 148,000 sq.ft of retail space, 184 residential units, 279 public car parking spaces, an on-street bus interchange and alterations to the public realm. These variations were considered by Cabinet and Full Council in July 2014 - CAB2603 refers. They were approved by Cabinet on 6 August 2014 – CAB2607 refers.
- 2.5 CAB 2603 contained an exempt report from Leading Counsel on matters related to the proposed variations, including the procurement issue. Given the Court decision, the exempt status of that advice can be removed – and the document is attached as Appendix 5. The Notes of the Conference were signed off by Leading Counsel – and represent his advice as to the position on procurement as at the time Cabinet made the relevant decision – 6 August 2014.
- 2.6 The revised scheme was awarded a resolution to grant planning permission by the City Council's Planning Committee in December 2014 - PDC1012 refers. A pre-action letter from solicitors on behalf of Councillor Gottlieb had been received in which it was stated that he was considering applying for a judicial review to challenge the Council's planning decision. There have also been requests to the Secretary of State that he should call-in the planning application for his decision. The Council has been informed that the Secretary of State is considering these call-in requests and has issued a direction preventing the Council from issuing the planning permission until the decision has been made. The relevant Minister is unable to give a timeframe for this decision other than it was not imminent. A call-in decision would require a public inquiry. The previous planning decision in 2009 was not called-in by the Secretary of State.

3 Summary of the High Court Decision

- 3.1 Mrs Justice Lang decided that the proposed variations to the Development Agreement approved by Cabinet on 6 August 2014 were:
- (a) materially different in character from the original contract and

- (b) The variations changed the economic balance of the contract in favour of the developer in a manner which was not provided for in the terms of the initial contract.

The comparison to be made was between the 2014 proposals, and the original Development Agreement concluded in 2004. She applied a test of whether the change in terms between the two dates were such that it would have meant that other realistic bidders would have bid at the time of the original contract award in 2004, had it been advertised. Mrs Justice Lang concluded that it was not necessary to show that there would have been alternative bidders, but that it was a realistic possibility. She said:

“137. In the light of all the evidence, I am satisfied, on the balance of probabilities, that a realistic hypothetical bidder would have applied for the contract (as varied), had it been advertised. “

3.2 Some of the key aspects considered by Mrs Justice Lang are set out in paragraphs 139-142 of her judgement as follows:

“139. There were extensive negotiations between the parties, varying many of the terms. The fundamental change which the parties intended to achieve was to increase the potential profit to the Developer so as to make the scheme viable (i.e. achieve more than the 10% threshold return). Both parties believed that the original contract was no longer viable.

140. The removal of the requirements to provide 35% ‘affordable housing’ and civic amenities reduced the Developer’s costs and increased its potential profit margins. The removal of the requirement to sub-contract to listed building contractors, using competitive tendering, was a commercial benefit. The extension of the Site by the addition of another property, and the 50% plus increase in retail space in place of a bus station, increased the Developer’s potential profits, even taking into account increased rental, construction costs etc. The fact that it was a third party, Stagecoach, which decided that it no longer wanted to incur the running costs of a bus station, has no bearing on the test to be applied under *Pressetext*.

141. Although the subject-matter of the contract has remained the same, the terms have become a significantly more attractive commercial proposition for a potential bidder. As I have already indicated, in a concession contract, economic benefit is not to be assessed just on the basis of the financial terms between the Council and the Developer, but also on potential profits from third party contracts. If there had been a procurement process in 2004, I am satisfied, on the balance of probabilities, that the more favourable terms would have enabled other realistic bidders to bid, because of the reduced costs and increased opportunity for profit.

142. Therefore, I conclude that the Council’s decision to authorise variations to the Development Agreement, without carrying out a procurement process as required by Directive 2004/18/EC and the Public Contracts Regulations 2006, was unlawful.”

- 3.3 The Council had not undertaken an open EU competition in 2004 and had concluded negotiations with Thornfield. This took account of the external advice it received at that time that it was a land deal which was outside the EU procurement regulations. This was a common approach at this time. Mrs Justice Lang said:

“50. The Council ought to have complied with the procurement requirements set out above, but did not do so, in reliance on mistaken legal advice. Instead it entered into an agreement with Thornfield Properties because it had a pre-existing commercial relationship with Stagecoach to redevelop its bus station on the site. No other contractors were considered. It is now too late to challenge the lawfulness of the Development Agreement on this basis.”

- 3.4 The application of the EU procurement regulations to the procurement of a developer in a regeneration-type scheme was tested for the first time and clarified in a European Court Case – *Aroux v. Roanne* in 2007. At the time of variations to the Development Agreement in both 2008 and 2010, reports to Members reported advice from Leading Counsel on the implications of the Roanne judgement, the potential risk of challenge, and taking into account such advice, the variations were made. Variations authorised at that time were not challenged and were not relevant to the 2015 High Court decision. At the Judicial review hearing in 2015 the Leading Counsel for the Council accepted that in the light of the case law from 2007, an EU procurement would have been required in 2004, although there was no clear legal authority at that time.

4 Monitoring Officer Statutory Report

- 4.1 The Monitoring Officer is required by S5A Local Government and Housing Act 1989 to make a formal statutory report upon a contravention of any enactment or rule of law. Following the High Court decision it is necessary to make a formal report in this case.
- 4.2 Other Members of the Council have to be notified of the issue of this report to Cabinet – which was done on 26 February 2015. Following Cabinet’s consideration of the report, Cabinet’s response on action to be taken (if any), together with reasons has to be sent to all Members.
- 4.3 The Head of Paid Service (Chief Executive) and Chief Finance Officer have been consulted on the contents of this report, along with other officers on the Council’s Silver Hill Project Team.
- 4.4 The decision affected by the judgement and this statutory report is the implementation of the Cabinet decision on 6 August 2014 to authorise the legal documentation to give effect to the proposed variations to the Development Agreement. Appendix 4 is the Court order and Appendix 6 and 7 are the Cabinet minutes of 6 August 2014 and 10 July 2014 – as the latter were partly incorporated by reference into the 6 August decision. Part of these appendices are exempt. Prior to the Court hearing the drafting of the

proposed documentation had been discussed with Henderson, but had not been concluded or executed, pending the outcome of the Court decision. Given that the High Court ruling is that the variations are unlawful and the Court decision was to quash the decision, the documentation has not been executed. The issue of the Monitoring Officer report prevents the completion of the documentation, until such time as Cabinet has considered how to deal with the matter. In practice, however, implementation could only take place if an appeal against the High Court decision was successful.

5 Potential for Appeal

- 5.1 The Council has 21 days from the date of the Court's judgement in which to consider whether it wants to lodge an appeal to the Court of Appeal. 4 March 2015 is the last date for lodging an appeal.
- 5.2 The advice of Leading Counsel will follow as exempt Appendix 8, to enable Cabinet to consider the issue, and to determine whether it wishes to lodge an application to appeal.
- 5.3 Exempt Appendix 8 is only being supplied to Cabinet, The Chairman of Overview and Scrutiny Committee, The Leader and Deputy Leader of the Principal Opposition Party, and the Leaders of other Groups on the Council. Cabinet will consider release of the exempt status to the document after the period for any interested party lodging an appeal, or if an appeal takes place, after the appeal has been determined.
- 5.4 The Council's costs of an appeal are estimated to be in the order of £90,000 to £95,000. However, if the Council was unsuccessful, and the claimant chose to be represented at the appeal, then it is probable there would be a costs award against the Council which could be of a similar amount.

6 Existing Costs Awards of the Litigation

- 6.1 For the first application for permission to proceed to a judicial review on 7 October 2014, the Council was awarded £7,500 costs against Councillor Gottlieb. This is no longer applicable in view of the subsequent decision on the Judicial Review.
- 6.2 For the subsequent litigation the total costs claimed on behalf of Cllr Gottlieb are £138,500. The Court ordered that these costs should be assessed by the Court if not agreed within 21 days, and then paid by the Council. In addition, the Council's own costs are £123,766. Henderson have offered and agreed to pay 50% of these costs, on the basis that it can allocate these against the development account.
- 6.3 Costs have yet to be agreed, and in the absence of agreement would be subject to taxation by the Court.
- 6.4 Any further advice on these aspects will need to be given in exempt session.

7 Independent Review

- 7.1 The previous Leader Councillor Humby, and the previous Chairman of The Overview and Scrutiny Committee have both referred to an Independent review. The Current Leader, Councillor Pearson, has also referred to the need for such a review at Council on 18 February 2014.
- 7.2 Cabinet will need to consider how this should be taken forward.

8 Possible Future Options

- 8.1 The Council will need to consider its options on how to proceed in the light of the current situation. A further report to start to consider the way forward will be brought to Cabinet at its meeting on 18 March 2015.
- 8.2 The Leader has indicated that the Cabinet will consult full Council on future options for the Silver Hill Project.

OTHER CONSIDERATIONS:

9 SUSTAINABLE COMMUNITY STRATEGY AND CHANGE PLANS (RELEVANCE TO):

- 9.1 The Silver Hill scheme is one of the Council's major projects and represents a major regeneration in the interests of the local economy and social well-being of the District.

10 RESOURCE IMPLICATIONS:

- 10.1 Report CAB2647 (Revised) considered at the Council Budget meeting on 18 February 2015, was a revised budget report reflecting the immediate impact of the findings of the Judicial Review of the Silver Hill scheme. It includes updated figures reflecting the impact on the revenue budget for 2015/16, the forward revenue projections, the capital programme, and the reserves forecasts. Further information on the assumptions made is provided at paragraph 7 of that report. Only the immediate impact of not progressing the scheme as planned has been assessed. Clearly, whatever future action the Council determines to take will need to be brought forward in its own right for consideration.
- 10.2 The immediate budget impact of the direct decisions relating to this report are contained in paragraphs 5 and 6 which relate to the litigation. The cost of the Independent Review will also need to be considered. Further advice will be given at the meeting.
- 10.3 The financial impact of any options on how the Council takes Silver Hill forward in the future will need to be considered in future reports.

11 RISK MANAGEMENT ISSUES

- 11.1 The principal risks arising from the matters in this report are:-

- a) If the development does not proceed, the Council will not receive the rental income which it is entitled to under the Development Agreement. Furthermore, it will incur additional unbudgeted costs in maintaining its assets in the site, and suffer reduced income as a result of the deteriorating condition of those assets, unless and until those assets are re-developed.
- b) If the development does not proceed, it may not be possible to secure an alternative developer for the comprehensive redevelopment of the site (either at all, or on comparable financial terms), again leading to adverse financial effects on the Council. The costs of promoting an alternative development may fall on the Council.
- c) The risk of substantial delay in securing redevelopment of the area by another developer if the development does not proceed which may have an adverse effect on the town centre.
- d) The risk that the Compulsory Purchase Order expires due to delay in developing the site (the Order must be implemented before March 2016), and the consequent risk that it may not be possible to secure confirmation of a replacement CPO.
- e) The risk of challenge to the Council's decisions which are the subject of this report and any future options it may consider on the way forward.
- f) Risks to the Council's reputation depending on the approach it takes on considering its future options.

BACKGROUND DOCUMENTS:

See Appendices set out below

APPENDICES:

Appendix 1 - Order of Mr Justice Dove – 7 October 2014.

Appendix 2 – Order of Mr Justice Lindblom – 18 October 2014

Appendix 3 – High Court Judgement – Mrs Justice Lang – 18 February 2015

Appendix 4 – High Court Order – Mrs Justice Lang – 11 February 2015.

Appendix 5 – Notes of Conference with Leading Counsel - 9 June 2014

Appendix 6 – Minute extract – Cabinet decision of 6 August 2014 (part exempt)

Appendix 7 – Minute extract – Cabinet decision of 10 July 2014 (part exempt)

Appendix 8 – Exempt – Advice of Leading Counsel on the High Court Decision

Exempt Appendix 8 - is only being supplied to Cabinet, The Chairman of Overview and Scrutiny Committee, The Leader and Deputy Leader of the Principal Opposition Party, and the Leaders of other Groups on the Council.

Cabinet will consider release of the exempt status to the document after the period for any interested party lodging an appeal, or if an appeal takes place, after the appeal has been determined.