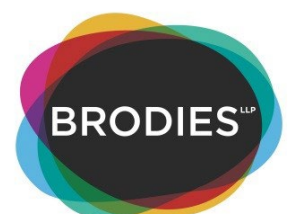


# Advice note for Scottish Futures Trust on CBRS case studies

June 2023



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## 1 INTRODUCTION

- 1.1 We have been asked to provide advice to Scottish Futures Trust ("SFT") in relation to five notional case studies it has prepared to inform a new approach to Council Built Homes for Market Rent and Sale ("CBRS"), based on the power of Councils under section 20 of the Local Government in Scotland Act 2003 ("the 2003 Act") to advance wellbeing.
- 1.2 This legal opinion follows-on from earlier work prepared for SFT that considered the use of the power to advance wellbeing (as set out at Section 20 of the 2003 Act) as an appropriate basis for the delivery of Council-built homes for market level rent and/ or sale (see paragraph 2.1). These earlier legal opinions considered the use of the wellbeing power and the different legal structures that could be used for CBRS to ensure that robust and protective legal structures can be put in place by Councils to enable successful delivery of new homes for market rent and sale by them and to manage and mitigate legal risks and challenges.
- 1.3 This advice builds on that earlier work and provides legal opinion on a series of practical questions relating to the delivery of five notional case study projects. The objective is to understand the practical application of the wellbeing power by Councils through provision of legal opinion on potential project delivery issues that have been raised by Councils.
- 1.4 We have prepared this note on SFT's instructions. It is the client in respect of this advice, and the holder of privilege. A third party may not rely on this advice without our consent. This does not prevent SFT publishing this note, or sharing excerpts of it as it sees fit. SFT will appreciate that divulgence of legal advice can lead to a loss of the protection of privilege.
- 1.5 In sections 2 – 8 of this note we set out our views in relation to key, common themes arising from the five notional case studies we have been asked to consider. The views we express in this section are applied in practice to the case studies later in this note.
- 1.6 Common themes we have identified in the case studies relate to:
- 1.6.1 use of the power to advance wellbeing: best value and assessing risk;
  - 1.6.2 the concept of "market failure" and the need for an appropriately robust evidence base;
  - 1.6.3 consultation;
  - 1.6.4 structuring, and considerations in the securing of a joint venture ("JV") partner;
  - 1.6.5 restricting occupancy of houses to people with particular characteristics;
  - 1.6.6 tenure in houses held for rent by Councils; and

## 1.6.7 subsidy control.

1.7 In sections 9 – 13, we set our answers to the questions we have been asked in connection with each case study. Notwithstanding the degree of overlap in some of the answers, we have produced each in full for ease of readability.

## 2 POWER TO ADVANCE WELLBEING

2.1 As Councils are faced with modern challenges, and look to implement innovative solutions, they are increasingly considering use of the power in section 20 of the 2003 Act. SFT has previously been provided with detailed legal advice in relation to the power to advance wellbeing provided for in section 20, including the statutory and common law constraints on the use of that power.<sup>1</sup>

2.2 Section 20 of the 2003 Act provides:

- 1) *A local authority has power to do anything which it considers is likely to promote or improve the well-being of—*
  - a) *its area and persons within that area; or*
  - b) *either of those.*
- 2) *The power under subsection (1) above includes power to—*
  - a) *incur expenditure,*
  - b) *give financial assistance to any person,*
  - c) *enter into arrangements or agreements with any person,*
  - d) *co-operate with, or facilitate or co-ordinate the activities of, any person,*
  - e) *exercise on behalf of any person any functions of that person, and*
  - f) *provide staff, goods, materials, facilities, services or property to any person.*
- 3) *The power under subsection (1) above may be exercised in relation to, or for the benefit of—*
  - a) *the whole or any part of the area of the local authority;*
  - b) *all or some of the persons within that area.*
- 4) *The power under subsection (1) above includes power to do anything—*
  - a) *in relation to, or for the benefit of, any persons or place outwith the area of the local authority; or*
  - b) *in any such place, if the authority considers that doing so is likely to achieve the purpose set out in that subsection.*
- 5) *The Scottish Ministers may, by order, extend the meaning of “well-being” for the purposes of this section.*
- 6) *Such an order shall be made by statutory instrument but not unless a draft of it has been laid before and approved by resolution of the Scottish Parliament.*
- 7) *Before laying such a statutory instrument, the Scottish Ministers shall consult such associations of local authorities as they think fit.*

<sup>1</sup> See "Legal Opinion – Council Built Homes for Market Rent and Sale", May 2022 ("the May 2022 Opinion"). Available here:

<https://www.scottishfuturetrust.org.uk/storage/uploads/councilbuilthomesformarketrentandsalelegalopinionmay2022.pdf>.

- 2.3 The section 20 power is broad but should not be regarded as a means of circumventing ordinary statutory or other restrictions.<sup>2</sup>
- 2.4 When a Council is considering the exercise of the power a key question will always be around the presence of benefit to the area and/or persons within it. A Council wishing to use the section 20 power should be clear, at the outset, what it is it wants to achieve, and why achieving this would promote or improve the well-being of an area, persons within that area, or both. The less direct or proximate the benefit to the people or area, the greater the level of risk associated with the (purported) exercise of the section 20 power.
- 2.5 A key aspect of lawful exercise of the section 20 power will be proportionality. Councils will wish to consider, and balance:
- 2.5.1 the scale of the opportunity pursued in discharge of the section 20 power;
  - 2.5.2 the resources required in pursuit of that opportunity;
  - 2.5.3 prospects of the opportunity being realised; and,
  - 2.5.4 other risk.
- 2.6 A Council would also be entitled to consider the likely outcomes if it did not exercise the section 20 power, although any such consideration would need to have a reasonable basis supported by reliable evidence (e.g., forecasting of the practical effects of non-exercise of the power undertaken by suitably qualified advisors).
- 2.7 Other risks might include: (i) a failure by a Council to comply with other statutory duties, particularly in respect of housing (an argument may be advanced that Councils ought reasonably to discharge those duties, before considering other, discretionary spending/ activity); (ii) potential opposition or challenge to use of the section 20 power (for example, from housebuilders).
- 2.8 A Council considering use of the section 20 power should take steps to mitigate risk. That might involve:
- 2.8.1 **Seeking to ground a proposal in policy frameworks** – for example, is there Scottish Government guidance or policy commitments that can be referred to? Is the proposal consistent with regional and/or local housing / transport / planning policy?
  - 2.8.2 **Community support** – consider what sources are available to evidence community support – that might, for example involve, ascertaining the

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<sup>2</sup> May 2022 Opinion, in particular sections 2.3 – 2.4. The detailed discussion in the May 2022 Opinion should be considered alongside the general advice tendered in this note.

views of community planning partners. We deal with consultation requirements more generally below at section 4.

2.8.3 **Cost-benefit analysis** – this should seek to include all relevant factors and might include, for example, considering costs, market values and what return a sensible investor might expect to return if undertaking the operations proposed to be carried out under the section 20 power. It may also include consideration of non-economic indirect factors, although all factors considered will need to have a reasonable evidential basis and, the less direct any likely outcome likely to be is, the less weight can properly be placed upon it. In assessing relative weight, a Council would be entitled to have regard to local priorities, as reflected in the policy frameworks we discuss above at 2.8.1. There may be factors that are of greater significance for one Council area than for others.

- 2.9 A Council contemplating use of the section 20 power is likely to benefit from securing expert support. We discuss what expertise might be useful in more detail below (see sections 3 and 4).
- 2.10 Any challenge to the use of the section 20 power would likely proceed by way of judicial review in the Court of Session. Grounds of challenge could include: (i) that the Council was not entitled to use the section 20 power in the manner proposed (for example, because of some statutory prohibition), (ii) that the Council was using the section 20 power for an improper purpose, or (iii) the Council had failed to carry out sufficient consultation in advance of implementing its proposals. Almost invariably judicial review will also include a reference to inadequate reasons for a decision as a ground of challenge. Where the section 20 power is engaged it is recommended that the rationale for the decision is carefully recorded.
- 2.11 Use of the power to advance wellbeing does not bring with it particular additional obligations for the purposes of procurement law. However, appropriate use of procurement processes (even if not a statutory requirement in particular circumstances) may be helpful for Councils in complying with best value obligations borne by them.

### 3 MARKET FAILURE

- 3.1 "Market failure" is a key aspect of the interventions envisaged in the case studies. Any business case supporting the interventions proposed in the case studies would need to carefully consider market failure, although it is of note that the Scottish Government's guidance on best value does not use the term.<sup>3</sup> In this document references to market failure include all instances of where the market is not delivering in accordance with identified local need.

<sup>3</sup> Local Government in Scotland Act 2003 – Best Value: Revised Statutory Guidance 2020, available here: <https://www.gov.scot/binaries/content/documents/govscot/publications/advice-and-guidance/2020/03/best-value-revised-statutory-guidance-2020/documents/best-value-revised-statutory-guidance-2020/best-value-revised-statutory-guidance-2020/govscot%3Adocument/best-value-revised-statutory-guidance-2020.pdf>.

- 3.1.1 Councils will wish to consider how "market failure" is defined and how it will be evidenced.
- 3.1.2 While existing planning and housing documents may be useful as supporting evidence in relation to market failure, expert input in any given case is likely to be essential. Councils will want to define: (i) what the market they are concerned with is, (ii) what is the "failure", (iii) what is contributing to this failure and (iv) how each of these is evidenced. Part of the evidence base for intervention is likely to involve working with developers to understand what it is that is preventing or deterring them from operating in the market with which the Council is concerned or from delivering in accordance with identified local need.
- 3.1.3 Councils should be aware that market failure (given its more common meaning) may not be the root cause of unmet demand. The market may be responding to factors that, taken together, may have the effect that certain types of development (including development in particular areas) are not attractive to the market in which case the market, acting in accordance with established practice will look elsewhere.
- 3.1.4 It will be important for any business case (informed by expert input) to demonstrate not only that development of viable sites for housing has not taken place, but that there is demand for such housing that is going unmet. That is because, in the absence of evidence of such demand, it would be (much) more difficult to demonstrate that the proposal was a lawful use of the section 20 power. It would also go towards whether the development of homes for market rent and sale is, in a given set of circumstances, an appropriate use of Council time and resources that could otherwise be diverted to (for example) social housing. Councils undertaking this kind of assessment would, however, reasonably have regard to a range of other factors including funding sources in respect of social housing and other housing tenures.

## 4 CONSULTATION

- 4.1 Councils will be familiar with the need, in certain circumstances, to consult. Consultation is, for example, a regular feature in decision making processes aligned to budget setting and changes in service provision. The general principles applicable to consultations in other contexts will be useful reference points in devising a consultation strategy for any CBRS proposal.
- 4.2 In general, in relation to the matters considered in this report. It will normally be appropriate to consult with (at least) community planning partners, housebuilders and developers. Community planning partners are

likely to have an interest in issues such as the availability of housing locally and housebuilders will have an interest in the market generally, if not locally. The exact design of consultation and engagement with stakeholders will depend upon the precise proposals under consideration. A typical consultation process is likely to engage a range of media including social media.

- 4.3 The following key principles will apply to any consultation undertaken in respect of a CBRS proposal:
- 4.3.1 The consultation should be carried out when the CBRS proposal is still at a formative stage – in practice that might be after a preferred option has been adopted (and this is entirely legitimate) but before a decision is taken that that option will be implemented. It is, however, permissible to consult on a preferred option subject to the caveats mentioned at 4.3.2 below.
  - 4.3.2 The consulting Council should provide sufficient reasons for the proposal for consultees to understand the rationale behind it including a summary of any alternatives that have been considered and the reasons why other options are not preferred. The consultation document should also set out what factors inform the Council's decision-making.
  - 4.3.3 The Council should provide adequate time for responses – at least 28 days from first notice of consultation for responses will generally be the minimum appropriate period but the Council will wish to consider whether a longer period is required depending on the complexity of the proposal and taking account of holiday periods. That said, where a Council has undertaken extensive, prior consultation, it could take the view that a shorter period was appropriate.
  - 4.3.4 Responses should be conscientiously considered – the Council will need to demonstrate that it has considered responses to the consultation and either adjusted the proposal as a result or provided reasons justifying why it has elected not to do so.
  - 4.3.5 The Scottish Government has published decision making by public authorities<sup>4</sup> which contains useful guidance on consultation exercises.
- 4.4 While consultation can be resource intensive, we do think (even if it is not required), appropriate consultation may be beneficial in connection with a CBRS scheme. Consultation could assist the Council to understand the thinking of others – including developers – in relation to matters it is considering and where

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<sup>4</sup>, *Right First Time*, available here: <https://www.gov.scot/binaries/content/documents/govscot/publications/advice-and-guidance/2021/01/right-first-time-practical-guide-public-authorities-scotland-decision-making-law-second-edition/documents/right-first-time-practical-guide-public-authorities-scotland-decision-making-law/right-first-time-practical-guide-public-authorities-scotland-decision-making-law/govscot%3Adocument/right-first-time-practical-guide-public-authorities-scotland-decision-making-law.pdf>.



responses are favourable, the exercise may strengthen the basis for the Council's decision. It may also raise issues (including concerns and / or potential benefits) that have not previously been identified.

- 4.5 Councils may wish to consider integrating the consultation process with obtaining expert support. This would mean that consultation responses could inform the assessment of the existence (and extent) of market failure and/or other factors that are impacting on the delivery of housing units.
- 4.6 In general, while "anecdotal" evidence can help in developing the scope of consultation exercises, it should not be founded upon to any significant extent to inform decision-making in relation to a CBRS proposal.
- 4.7 Alongside consultation, Councils will generally wish to carry out impact assessments in discharge their Public Sector Equality Duty and, likely, the Fairer Scotland Duty. They should take legal advice on the need for such assessments and, where assessments are deemed appropriate, it is recommended that they are reviewed to ensure that they are sufficiently robust. In-house legal teams should be able to assist with that.

## 5 STRUCTURING

- 5.1 Decisions around structuring should be informed by the objectives of a CBRS proposal. Consideration should be given at an early stage to the treatment of any profits arising from a CBRS proposal and the extent of any ringfencing required to avoid profits "coming back" to a Council. Councils considering possible delivery structures may wish to consider Clause 4 and Annex 1 to the May 2022 Opinion obtained by SFT.
- 5.2 Councils will need to have a clear rationale for any business structure set up in connection with a CBRS proposal. If the only purpose of an entity set up by a Council is to circumvent statutory restrictions upon the Council itself, then there would be a real risk that a court, if considering a challenge to the use of the business structure, would regard the arrangement as unlawful.<sup>5</sup>
- 5.3 Where a Council wishes to enter into a JV, it is not always necessary to run a procurement process. That is because an agreement to form a JV is not a "public contract" as defined in regulation 2 of the Public Contracts (Scotland) Regulations 2015.<sup>6</sup> Only if the JV is to be *contracted* by a Council to deliver something to it (e.g., to build properties for the Council) then a procurement process is likely to be necessary either for the JV partner or in order to select the JV to perform that contract. Where goods, services or works are to be delivered to the Council under contractual arrangements, and a JV route to

<sup>5</sup> See e.g., in an English context, *Crédit Suisse v Allerdale Borough Council* [1996] 4 All ER 129.

<sup>6</sup> A public contract is "a contract for pecuniary interest concluded in writing between one or more economic operators and one or more contracting authorities and having as its object the execution of works, the supply of products or the provision of services". As the formation of a JV does not have as its object the execution of works, supply of products or provision of services (notwithstanding that the ultimate *aim* of the formation of a JV may be for the JV to enter into one or more contracts that *do* have one or more of those objects) the agreement to form a JV is not itself subject to the Regulations.

delivery is desired, then the Council will need to procure the JV partner, because otherwise the JV cannot itself be guaranteed any contract award.

- 5.4 In addition, there may be benefits to the use of a suitably tailored procurement process, in terms of a Council's control over any JV and, in particular, over the projects that it develops. Such a process will also be helpful in demonstrating the value for money and the quality that might be expected of the Council's choice of partner. Any JV established by a Council for the purpose of pursuing an activity authorised by the section 20 power is likely itself to be subject to procurement obligations as a contracting authority.<sup>7</sup>
- 5.5 Where a JV is established, there will be limits upon the use to which any profits it derives can be used, in particular upon the extent to which profits can return to the Council.

## 6 RESTRICTING OCCUPANCY

- 6.1 There are a variety of matters to have regard to in circumstances in which a Council wishes to restrict eligibility to occupy houses it builds.
- 6.2 Generally, it is difficult to regulate for the changing circumstances of occupiers following the completion of a sale and or the grant of a lease. For example, where allocations criteria stipulate that tenant occupiers work in a specific industry, if during the course of the tenancy, the tenant moves to work in a different industry this would not in and of itself be a ground to recover vacant possession. Similarly, where allocations criteria provide an income cap (and/or collar) which must be met for allocation of a house, if during the course of the tenancy, the tenant's income levels increase to a level higher than the cap, this would not in and of itself be a ground to recover vacant possession.
- 6.3 In respect of houses for sale, the tried and tested approach for securing purchaser obligations post sale is by way of a personal contract between the seller and the purchaser regulating particular activities which is backed up by a standard security granted by the purchaser in favour of the seller. This is the approach used in, for example, New Supply Shared Equity arrangements.
- 6.4 In addition to the contractual approach mentioned above at 6.3, we have considered the use burdens which could be useful for controlling the occupation and sale of homes by second and subsequent owners to purchasers who meet the initial eligibility criteria set.

- 6.4.1 **Economic development burden ("EDB")** – these are already in relatively regular use by Scottish public sector organisations in order to ensure land

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<sup>7</sup> The test for the JV constituting a contracting authority has three parts: (i) it has legal personality, (ii) it is established for the specific purpose of meeting needs in the general interest not having an industrial or commercial character, and (iii) it is financed mostly by a public body, subject to management supervision by a public body, or has an administrative, managerial or supervisory board mostly chosen by a public body. On the basis that any JV established to pursue an activity authorised by the section 20 power will (i) have legal personality, (ii) be established for that general interest purpose, and (iii) be subject to management supervision by the Council (whether or not it is also mostly financed by the Council, or most of its directors are appointed by the Council), it will constitute a "body governed by public law" under the Public Contracts (Scotland) Regulations 2015 and therefore a contracting authority subject to procurement rules.

for which they provide funding is used for a specified purpose over a long term and surviving changing ownership. In general, EDBs are given teeth by way of a requirement to make a significant financial payment that falls due if the land is used other than for that purpose. Councils and economic development agencies can have powers of enforcement under EDBs. Any EDB would be recorded on the title sheet for the piece of land to which it related. As such, its existence would become apparent to any prospective buyer through the conveyancing process.

We are not aware of EDBs previously having been imposed in relation to residential properties. Careful consideration would need to be given as to whether an EDB could be appropriately used in any given CBRS context. In particular, we consider that a Council wishing to use EDBs in that context would need to be able to demonstrate that the development and marketing of houses for sale was sufficiently ancillary to supporting economic development in their area, such that the EDB would be capable of application. An amendment to the legislation<sup>8</sup> to provide expressly that housing is ancillary to economic development, and therefore that an EDB is capable of application in a housing delivery context, would be required to put the question of enforceability beyond doubt. We do not anticipate that this is likely to be a priority for the Scottish Government at this time<sup>9</sup>.

- 6.4.2 **Health care burden** – these operate in a broadly similar way to EDBs. The Title Conditions (Scotland) Act 2003 ("2003 Act") expressly envisages use of healthcare burdens in relation to the provision of accommodation for staff employed to provide healthcare. As such, we consider this type of burden potentially of significant utility for those CBRS proposals which aim to provide housing for key workers working in the NHS.

An important point to note in relation to health care burdens is that they can only be enforced by a health board or by the Scottish Ministers.

- 6.4.3 **Rural housing burden** ("RHB") – RHBs operate quite differently from EDBs and health care burdens. In effect they afford a right of pre-emption<sup>10</sup> exercisable prior to each and every disposal over rural land (and everything on that land from time to time, including housing) to a "rural housing body", which can be a Council. One important point to note is that the right of pre-emption is only going to be effective in ensuring houses

<sup>8</sup> Title Conditions (Scotland) Act 2003

<sup>9</sup> We note that there is currently no ongoing law reform project being undertaken in this regard by the Scottish Law Commission.

<sup>10</sup> Pre-emption entitles the holder to have first refusal in the event of the property coming up for sale.

developed under a CBRS scheme are not, for example, sold to a third party as a holiday home, if the RHB in fact exercises the right of pre-emption. The price payable on exercise of the pre-emption will be stipulated (usually with reference to a mechanism for calculation) within the terms of the RHB itself – likely full or discounted open market value.

- 6.5 In addition to (pure) burdens, Councils may wish to consider the use of agreements under section 75 of the Town and Country Planning (Scotland) Act 1997 ("the 1997 Act") to control the occupation and sale of houses developed under a CBRS scheme. Any applicable section 75 agreement term would appear on the title sheet for the relevant house and would be helpful in dissuading prospective buyers who did not meet the condition from progressing a purchase (particularly if they were relying upon borrowed funds to do so). The Section 75 agreement could prescribe a percentage discount to be applied to the price payable on sale and secure the long-term availability of the housing at this discount by prescribing criteria which apply to permitted (or qualifying) purchasers entitled to benefit from the discount. Each prospective purchaser (including second and subsequent purchasers) would be referred by the seller (whether the first seller or subsequent owners) to the Council for consideration against the criteria. Sales to prospective purchasers who are assessed as meeting the criteria will be referred to the then seller to proceed with the sale. In the event that there are no purchasers in the market who meet the criteria, the s.75 Agreement can provide for alternative permitted disposal (e.g., to a Council), and finally can permit sale on the open market (usually subject to an overage payment to mitigate any windfall received by the seller against the restricted price paid). Section 75 agreements could be imposed in addition to burdens. This may provide increased certainty that the Council will be able to achieve its objectives.
- 6.6 It is likely to be (comparatively) more straightforward for Councils (or any business structure established as part of a CBRS scheme) to restrict occupancy of rented properties at the point of letting, so long as a well-designed allocations policy is in place. However, given the broad move towards security of tenure both in the affordable and private rented sectors (in the form of SSTs and PRTs being the default in each sector respectively), Councils will wish to consider the role of alternative tenure models (e.g., occupancy agreements or SSSTs) for houses designed to accommodate persons who meet criteria on a medium-term, but not permanent, basis (such as young care leavers). As alternative models afford comparatively less by way of security of tenure, they are likely to be more attractive for a Council seeking to provide non-permanent accommodation for example by avoiding issues such as succession to tenancy.
- 6.7 In all cases, it will be essential for any CBRS houses designed for particular types of occupants to be underpinned by a practical and effective framework which regulates occupation as intended in so far as possible and practicable. Models which involve the ownership and landlord's interest being held by a joint venture vehicle between the Council and a third party for primary purposes around risk sharing and allocation of profits and losses, will also benefit from greater flexibility in terms of the availability of the PRT tenure by virtue of the default SST position not applying.

## 7 TENANCIES IN PROPERTIES OWNED BY COUNCILS

- 7.1 Subject to limited exceptions contained in Schedule 1 to the Housing (Scotland) Act 2001, houses owned by Councils or registered social landlords will be SSTs. Section 31 of the Housing (Scotland) Act 2010 requires Councils (and registered social landlords) to aim to meet the standards and outcomes contained within the Scottish Social Housing Charter ("SSHC") in the performance of housing activities, including the Scottish Housing Quality Standard ("SHQS"). They are subject to the oversight of the Scottish Housing Regulator ("SHR") in relation to their attainment of those standards and outcomes. Councils maintaining properties for (at least, affordable) rent will also need to establish a Housing Revenue Account.
- 7.2 Where the proposed structure envisages that the ownership of completed homes will be held by an entity which is neither a Council nor a registered social landlord (for example an ALEO, which could be a company limited by guarantee, or a limited liability partnership with third parties) the tenancy will not be an SST. Tenancies granted will instead be Private Residential Tenancies, which would generally be the tenure of homes leased for mid-market and market rent and may be desirable for operational reasons (particularly where private sector partners are involved). However, the setting up of such a business structure would raise other considerations (including as discussed elsewhere in this note) in relation to funding, profits and control.

## 8 SUBSIDY CONTROL

- 8.1 In relation to any CBRS proposal, Councils will need to be mindful of their subsidy control duties. There may be particular circumstances in which a Council considers that an element of subsidy control is necessary to make a CBRS proposal attractive to, for example, a potential JV partner.
- 8.2 A subsidy is defined in the Subsidy Control Act 2022 as:

*"financial assistance which—*

*(a) is given, directly or indirectly, from public resources by a public authority,*

*(b) confers an economic advantage on one or more enterprises,*

*(c) is specific, that is, is such that it benefits one or more enterprises over one or more other enterprises with respect to the production of goods or the provision of services, and*

*(d) has, or is capable of having, an effect on—*

*(i) competition or investment within the United Kingdom,*

*(ii) trade between the United Kingdom and a country or territory outside the United Kingdom, or*

*(iii) investment as between the United Kingdom and a country or territory outside the United Kingdom."*

- 8.3 Financial assistance, and a specific economic advantage, can be conferred directly or indirectly, including where an investment is made by a public body on terms that are better than the enterprise could obtain in the market. The converse of such preferential terms is typically referred to as the "Commercial Market Operator" or "CMO" principle – i.e., if a public body is investing or supplying a good or service to an enterprise on market terms, that will not constitute a subsidy. The simplest way to demonstrate that an investment is being made on CMO terms is where it is made on "*pari passu*" terms, i.e., the Council invests in a JV on the same terms as another investor (the JV partner) who is investing at the same time. The other investor does not need to contribute and receive the same as the public authority, but each should receive a return that is in proportion to its investment.
- 8.4 Assistance provided by a public body which meets the above definition (i.e., which is not on CMO terms) is subject to conditions specified in the 2022 Act. That is not a bar to providing that assistance – there will be many instances in which there will be strong public policy arguments for providing a subsidy, however (and in particular), a Council must not provide a subsidy unless and until it has satisfied itself (acting reasonably) that the "subsidy control principles" are met. These principles are:
- 8.4.1 The subsidy pursues a specific policy objective in order to (a) remedy an identified market failure, or (b) address an equity rationale (such as local or regional disadvantage, social difficulties or distributional concerns);
  - 8.4.2 The subsidy is proportionate to its specific policy objective and limited to what is necessary to achieve it;
  - 8.4.3 The subsidy is designed to bring about a change of economic behaviour of the beneficiary which is (a) conducive to achieving its specific policy objective, and (b) something that would not happen without the subsidy;
  - 8.4.4 The subsidy does not compensate for the costs the beneficiary would have funded in the absence of any subsidy;
  - 8.4.5 The subsidy is an appropriate policy instrument for achieving its specific policy objective and that objective cannot be achieved through other, less distortive, means;
  - 8.4.6 The subsidy is designed to achieve its specific policy objective while minimising any negative effects on competition or investment within the United Kingdom; and
  - 8.4.7 The subsidy's beneficial effects (in terms of achieving its specific policy objective) should outweigh any negative effects, including in particular negative effects on (a) competition or investment within the United Kingdom and (b) international trade or investment.

- 8.5 Councils should apply their mind, at an early stage, to potential subsidy issues throughout the lifetime of any CBRS project, including in relation to a future exit strategy.
- 8.6 A subsidy may arise in a number of ways in a JV structure, and in particular at any point where the Council and JV partner are required (or not required) to contribute towards the JV's activities either financially or in kind or are permitted to withdraw capital or revenue from the JV. For example, where a Council proposes to contribute disproportionately to capital works as part of a JV (in comparison to the stake that it holds in the JV), it should consider how any resultant profits will be distributed, having regard to subsidy control rules vis-à-vis the JV partner, as well as statutory restrictions on trading by Councils.<sup>11</sup> Subsidy issues may also arise through the provision of any additional financial or other support to a JV, including with regard to the disposal of land or provision of guarantees or loans.
- 8.7 While different business structures may be subject to subsidy control rules in different ways, it will not be possible for a Council to circumvent the application of such rules altogether. That is likely the case, even if the Council was to build houses itself – where a public body is engaged in a market activity, subsidy rules can be triggered through the provision of funding by the body to itself for such purposes.

## 9 CASE STUDY ONE

*A Council in a large urban area (not a city) wishes to develop CBRS on a large, allocated brownfield housing site (15 hectares) via JV with private developer in the form of a Limited Liability Partnership. The JV partner will be procured via competitive tendering with full disclosure of the site conditions (site investigations are available) but before detailed planning permissions are secured (masterplan consent for the site is in place). The JV will procure the consultant and contractor teams on competitive tendering basis to align with Council requirements.*

*The site is located in a large town (population 10,000) and is currently owned by the Council – it will be transferred to the JV at open market value. Site investigations have confirmed that the site is contaminated. There are other 'readily developable' housing sites allocated on the LDP that have not been taken up by the private sector. There has been no private sector housebuilding in the town, or in adjacent towns within a 10 mile radius, in the past 5 years.*

*500 new homes will be delivered in phases over 5 years on a site that has been allocated for housing (referenced in LDP/ SHIP/ HNDA) – 250 houses will be at open market value (20% rented/ 80% sold), 100 will be mid-market value (50% rented/ 50% sold), 150 will be at a 'locally affordable' value (50% rented/ 50% sold).*

*The Council is a stock transfer authority but wants to retain full ownership of the properties for rent (market, mid and affordable values). The project is expected to be financially viable in totality, with income generated from the market value housing used to offset the cost of the affordable homes. The Council has not undertaken any consultation or*

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<sup>11</sup> See detailed discussion in the May 2022 Opinion, in particular section 2.

*engagement with local stakeholders beyond one local drop-in event to inform preparation of the masterplan – 50 local people attended.*

**9.1 What are the timescale options for remediation of the site and transfer to the JV – does the site need to be fully remediated in advance of any market testing to procure the JV partner?**

- 9.1.1 There is no legal obligation to fully remediate the site in advance of market testing to procure the JV partner. However, the Council is likely to receive more interest (and more fully appraised proposals) for a fully remediated site than for one that leaves remediation to the JV partner, because this will reduce the level of risk that the JV partner is adopting. Changes to the balance of risk between the Council and a development partner cannot be made once a contract is in place, so un-remediated sites can suffer from inflated price proposals from the start. In any event whether the Council is likely to get a better deal for a remediated site is something that should be assessed before deciding on how to proceed.
- 9.1.2 An un-remediated site that has lower land value may however have one advantage which is that the "open market value" of what the Council will be transferring into the JV will be lower. This will allow a lower contribution (or higher equity share) from the JV partner as subsidy control rules will not be triggered provided that the Council and partner invest in the JV on the same terms. Contrastingly, because the value of a remediated site will be higher, if the Council transfers a remediated site to the JV, then either (i) the JV partner will have to contribute more, (ii) the JV partner will have to reduce its share of the equity, or (iii) the Council will be providing a subsidy to the JV partner (by boosting the value of its share in the JV) and will require to ensure that the subsidy control principles are satisfied before doing so.
- 9.1.3 With regard to timescale, we cannot comment on how long remediation works would take themselves, however assuming that remediation works would themselves be of a value that would require a regulated works contract, and that before that the Council will require site surveys and assessments that would require a regulated services contract, we would expect that the procurement of those would take respectively three and six months as a rough approximation.
- 9.1.4 We would also note that the Council is proposing a JV here – whether a JV partner would require to be procured, and indeed whether a JV would itself constitute a contracting authority subject to public procurement duties, are



questions that turn on the specific structure of a JV and its relationship with the Council as detailed in paragraphs 5.3 and 5.4 of this note.

9.2 **How can the Council ensure a small proportion of the houses are allocated for occupation by only key workers and/or for principal home occupancy [across the market values and tenures] and that these homes remain occupied on this basis for at least the next ten years, but preferably in perpetuity? What legal options are there to secure this?**

9.2.1 Although the justification for allocating homes to people with specific characteristics will vary depending on the facts and circumstances, e.g., a shortage of homes for workers in specific industries, a shortage of homes for people with specific needs etc., the principles and available mechanisms for the allocation of homes to individuals who meet a set of predetermined criteria apply across all case studies consistently.

Securing long term availability of housing for specific groups for rent

9.2.2 The allocation of homes for **rent** to target groups who meet specific criteria is an established practice in the context of housing for mid-market rent ("MMR") and affordable housing for sale (particularly new supply shared equity), therefore there is precedent available to the CBRS model for the practice of allocating homes to individuals who meet specific criteria.

9.2.3 The preferential allocation of homes to key workers for either rent<sup>12</sup> or sale will depend on the establishment of clear criteria against which all applications received can be considered. These criteria would be set down in an allocations policy which would be available for review<sup>13</sup> externally.

9.2.4 Traditionally, in the context of housing for MMR, criteria have centred around household income level (i.e., a maximum household income threshold) as the determining factor of need, given that MMR is aimed at assisting people on low and modest incomes to access affordable rented accommodation, and helps those who have difficulty accessing social rented housing, buying their own home or renting privately on the open market.

9.2.5 Where housing is to be allocated based on applicants' key worker status, it may be the case that multiple criteria need to be developed and satisfied prior to allocation as opposed to a singular criterion that an applicant is a

<sup>12</sup> We assume that properties would be leased in terms of private residential tenancy agreements ("PRTs") in terms of the Private Housing (Tenancies) (Scotland) Act 2016.

<sup>13</sup> See, for example, Manor Estates Housing Association's allocations policy for MMR <https://www.manorestates.org.uk/wp-content/uploads/2021/04/MMR-Allocation-Policy-September-2019.pdf>, and LAR Housing Trust's policy <https://lar.scot/what-is-mid-market-rent%3F>. NSSE criteria are available here: <https://www.mygov.scot/new-supply-shared-equity-scheme>

key worker. This is because many key worker roles attract a wide range of salaries – for example – a teacher could earn between £28,113 and £99,609 depending on grade and role, therefore key worker status alone may not sufficiently identify housing need and should be supplemented with additional, traditional income criteria.

9.2.6 There is no legal restriction on the criteria which can be applied to individuals and households seeking housing, however allocations policies imposed by Councils (or their SPVs) are likely to require the approval of elected members. Generally, allocations policies should not be discriminatory however necessary and proportionate indirect discrimination to achieve a legitimate purpose (such as providing affordable housing for disadvantaged groups) is permissible. The availability and/or requirement for Housing Association Grant funding will also be relevant, as will questions of Subsidy Control<sup>14</sup> and human rights issues (for example the avoidance of discrimination).

9.2.7 Notwithstanding that there are no/limited restrictions on allocations criteria which can be applied once a PRT is granted, there are limited statutory grounds for recovering vacant possession, which do not include a change to tenant circumstances such that initial allocation criteria are no longer satisfied. This means that in every scenario where the tenant's right of occupancy is in terms of a PRT, it would be difficult to recover vacant possession in the event of a change in a tenant's circumstances resulting in them no longer meet allocations criteria which applied at the point in time when they took entry. However, there is provision<sup>15</sup> for the First-tier Tribunal to find (at its discretion) that it is an eviction ground that a tenancy was entered into to provide an employee with a home and the tenant is no longer an employee. This is subject to the condition that the tenancy was granted to the tenant in consequence of the tenant being an employee of the landlord<sup>16</sup>.

#### Options for securing availability of housing for specific groups for sale

9.2.8 Options for securing homes for **sale** as key worker accommodation and as the principal home of the owner<sup>17</sup> in the longer term (i.e., for successive

<sup>14</sup> Particularly in scenarios where local authority loans are to be advanced on non-standard/non-market terms.

<sup>15</sup> s. 8, Schedule 3 Private Housing (Tenancies) (Scotland) Act 2016.

<sup>16</sup> Therefore, where the landlord will be a Council or an SPV of a Council, the tenant would need to be an employee of the Council or the SPV for this to be an available ground for eviction. This ground is not available where the employer and the landlord is Police Scotland.

<sup>17</sup> The alternative to a positive obligation to occupy as a primary residence would be a restriction on use as a second home or a holiday home or as commercial holiday accommodation.

disposals following the first disposal) can broadly be split into two categories, being "legal" and "contractual". In each case, these mechanisms could secure the use of housing as key worker accommodation and principal homes both on sale of individual units and on the bulk disposal of multiple units into a new single ownership.

- 9.2.9 "Legal" options for maintaining the availability of housing are to apply title conditions ("burdens") restricting the use of the land on which the housing is built to the specific purpose of providing housing for key workers and securing their occupation as principal homes. This could be achieved by way of the constitution of particular burdens against the title to the land on which the properties are to be developed or planning obligations imposed by way of a section 75 Agreement.
- 9.2.10 With regard to burdens, legislation provides for three types of personal real burden (being burdens which can be enforced against a title holder by a third party who does not necessarily hold an interest in neighbouring ("benefitted") property) which could achieve this outcome. These are Healthcare Burdens, Economic Development Burdens ("EDBs") and Rural Housing Burdens ("RHBs").
- 9.2.11 Generally, burdens are self-policing in that any prospective owner would become aware of their terms during the standard conveyancing process and therefore know if they were about to purchase a home which included a condition which was contrary to their intended use. If the home was being purchased with mortgage finance, the presence of a burden on terms which could potentially restrict the open market value of the property would require to be reported to the mortgage provider. Burdens are also enforceable by the benefitted party or proprietor entitled to enforce the terms in the event that they become aware of a breach.
- 9.2.12 **Healthcare Burdens** can be created in favour of (and enforceable by) a health board, or the Scottish Ministers for *the purpose of promoting the provision of facilities for health care*<sup>18</sup>. Healthcare Burdens can be created other than by the health board or the Scottish Ministers with the consent<sup>19</sup> of the health board or the Scottish Ministers<sup>20</sup>.

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<sup>18</sup> s. 46 (1) Title Conditions (Scotland) Act 2003.

<sup>19</sup> Consent to be narrated within the terms of the constitutive deed.

<sup>20</sup> s. 46 (2) Title Conditions (Scotland) Act 2003.

- 9.2.13 "Facilities for health care" specifically includes facilities ancillary to health care, and the example given in the Act is "accommodation for staff employed to provide health care"<sup>21</sup>.
- 9.2.14 Healthcare Burdens therefore offer a clear route to secure housing for key workers who are employed to provide health care<sup>22</sup>. The Healthcare Burden would be registered against the title to housing for sale and would restrict occupation of the housing to health care workers. Provision could be included restricting letting of the housing by owner occupiers without consent of the health board or Scottish Ministers. In the event of disposal to a non-health care worker, provision could be made for payment of a sum (equivalent to overage) to the health board or the Scottish Ministers reflecting the difference between the price of the house as affected by the use restriction contained in the title, and the open market value without the restriction, however this would result in the burden ceasing to apply in respect of future disposals.
- 9.2.15 It is possible for Healthcare Burdens to be created by a landowner which is not a health board or the Scottish Ministers for the benefit of a health board or the Scottish Ministers with their consent. This means that housing could be developed by the JV or another third party for the purpose of providing key-worker accommodation for health care workers and burdened with a Healthcare Burden which would be enforceable by the health board or Scottish Ministers with their agreement.
- 9.2.16 Healthcare Burdens, when validly created and registered against the title to the affected land will bind successor owners to their terms and therefore could be effective in securing the long -term availability of housing for key workers involved in the provision of health care.
- 9.2.17 **Economic Development Burdens** ("EDBs") are available for the purpose of "*promoting economic development*" and are often used by enterprise agencies, for example, Scottish Enterprise, as a means of ensuring that land which is sold for the purposes of generating economic development will be subject to a payment of overage if the original disposal purpose is not achieved<sup>23</sup>.

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<sup>21</sup> s. 46 (6) Title Conditions (Scotland) Act 2003.

<sup>22</sup> However, the enforcement of healthcare burdens has not been tested.

<sup>23</sup> s. 45 (3) Title Conditions (Scotland) Act 2003 provides that an economic development burden may comprise an obligation to pay a sum of money (the sum or the method of determining it being specified in the constitutive deed) to the Council or the Scottish Ministers as the case may be.

- 9.2.18 Like Healthcare Burdens, EDBs could operate to restrict use of burdened property to a specific purpose (i.e. for the provision of housing for workers (although not necessarily key-workers, see further comment at 9.2.20 below) who meet the pre-determined criteria set out in the burden), and in the event of disposal to a subsequent purchaser who does not meet the worker criteria, an overage payment would be due to the party entitled to enforce. The right of the owner to lease the house to a third party would also be restricted.
- 9.2.19 While it is reasonably clear that, in the case of Healthcare Burdens, given the definition of "*facilities for healthcare*", there is potential for Healthcare Burdens to be used to achieve the long-term availability of housing for health care key workers (noting that Healthcare Burdens can only be created in favour of health boards and the Scottish Ministers), it is less clear whether EDBs could be used to achieve the long-term availability of housing for key workers. The purpose of an EDB must be to "promote economic development". Unfortunately, this expression is not defined in the legislation or the explanatory notes. Institutional writers Gretton and Reid refer to EDBs as being "a rather vague notion which will no doubt be tested in the courts" and also "intriguing and mysterious".
- 9.2.20 Our (caveated) proposition is that EDBs could be used to restrict the use of burdened land to the provision of housing for workers employed to work on a specific site ("the employment land") which is deemed to comprise an economic development. This is an extension of the rationale applied to Healthcare Burdens where accommodation for staff employed to provide health care is ancillary to the provision of health care. In our view, accommodation for staff employed to work as workers on employment land is ancillary to economic development. A strong link between the housing land burdened with the EDB and relevant employment site could be established if the employment site was also subject to an EDB. Given that the development on the employment land would need to be deemed to be an economic development to be burdened with the EDB, we think that a straightforward reading of the legislation would require economic activity to be undertaken on the employment land as its principal use which could preclude some traditional key-worker industries such as health care and education. In addition, given the existence of Healthcare Burdens, our assumption is that the legislative intention was that these would be the route used to deliver housing associated with healthcare delivery rather than EDBs.

- 9.2.21 We have not been able to identify anything definitive to support the idea that EDBs could be used to support the retention of key worker housing. A review of the limited case law and legal commentary available indicates some points in favour, but also some against. In our view, a Council looking to rely on EDBs to support the delivery of key worker housing would need to be comfortable that a burden requiring land to be used for housing for key workers would in fact promote (or at least be conducive to) economic development long-term, and that economic development would in reality be a "material and important" purpose of the burden, and/or a main intention of the parties.
- 9.2.22 Following our proposition above at 9.2.20, EDBs, when validly created and registered against the title to the affected land will bind successor owners to their terms and therefore could be effective in securing the long-term availability of housing for key workers employed on employment land.
- 9.2.23 **Rural Housing Burdens ("RHBs")** are personal real burdens over rural land<sup>24</sup> which incorporate a right of pre-emption in favour of a rural housing body<sup>25</sup>. The meaning of "rural land" is very broad – notwithstanding the name, it is possible to create RHBs on urban land subject to there being an appropriate rural housing body agreeing to accept the right to enforce. The Scottish Ministers have prescribed a list of rural housing bodies<sup>26</sup> who can benefit from the right to enforce RHBs.
- 9.2.24 As with Healthcare Burdens, it is possible for RHBs to be created other than by the benefitting rural housing body entitled to enforce it, provided that the consent<sup>27</sup> of that body to the creation of the burden in its favour is obtained. This means that RHBs can be created on sites owned by the JV rather than a rural housing body.
- 9.2.25 The effect of creation of an RHB is that prior to each disposal of a burdened house, the nominated rural housing body would have the opportunity to buy the property prior to it being sold on the open market<sup>28</sup> in exchange for a consideration calculated with reference to criteria set out in the RHB

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<sup>24</sup> "Rural land" means land other than excluded land ("excluded land" having the same meaning as in Part 2 of the Land Reform (Scotland) Act 2003 (asp 2)). The definition of "excluded land" is narrow, therefore "rural land" applies to rural but also urban land.

<sup>25</sup> s. 43(1) Title Conditions (Scotland) Act 2003

<sup>26</sup> Title Conditions (Scotland) Act 2003 (Rural Housing Bodies) Order 2004/477. The list includes Argyll Community Housing Association. The list also includes some registered social landlords.

<sup>27</sup> Consent to be narrated within the constitutive deed.

<sup>28</sup> This is unlike pre-emption real burdens discussed at paragraph 9.2.28 below, which expire if not exercised at the first opportunity arising.

constitutive deed. On exercising its pre-emption, the rural housing body could then sell the house to a third party who meets the key worker criteria.

- 9.2.26 RHBs would be a relatively expensive mechanism for the preservation of housing for key workers as the rural housing body would need to hold funds to exercise the pre-emption right (including purchase price, Land and Buildings Transaction Tax<sup>29</sup> and legal costs) – however this could be managed by way of a back to back disposal to a third party purchaser chosen by the rural housing body (this would be subject to the timescales involved in the operation of the pre-emption), facilitated by the rural housing body maintaining a waiting list of prospective purchasers who meet the allocation criteria.
- 9.2.27 Unlike most pre-emption rights, where the property is offered back only on the first occasion on which it is sold, RHBs are not extinguished for future disposals, so can secure the availability of the housing on a long-term basis.
- 9.2.28 **Pre-emption burdens:** For scenarios where there is benefitted property available (for example, where the JV was developing part of a larger, mixed tenure development site where a portion would be retained for social rent) a more straightforward **pre-emption burden** would be available. Similar to the RHB pre-emption, a pre-emption burden would require the first purchaser of each home to make an offer to the JV entitling it to buy back the home. This could be at a pre-determined fixed price (which could also be subject to increases for inflation). There would be no requirement for a rural housing body to be involved. However, a pre-emption burden would only be capable of exercise once – if the JV as the party with the right to receive the offer to purchase declined to exercise it (or otherwise waived the option) then the pre-emption right would be lost forever<sup>30</sup>. If, however the pre-emption was exercised, the party exercising it would be able to impose a fresh pre-emption burden on the title to the home on its subsequent disposal. The pre-emption burden would also only be available to the JV for as long as the JV held the ownership of the benefitted property.
- 9.2.29 **s.75 Agreements**<sup>31</sup> also offer a mechanism by which the use of land could be restricted to key worker accommodation and occupation of each house as a principal residence. In terms of s75(1) "A person may in

<sup>29</sup> Land and Buildings Transaction Tax is payable by the purchaser of property although, there may be mitigations available, for example Charities Relief where the RHB meets Revenue Scotland's charity criteria.

<sup>30</sup> This is different to RHB pre-emption rights, which continue to apply notwithstanding the right may not be exercised by the rural housing body entitled to enforce.

<sup>31</sup> Being Section 75 of the consolidated Town and Country Planning (Scotland) Act 1997 as amended in 2006 and came into force in February 2011

respect of land in the district of a planning authority (a) by agreement with that authority, or (b) unilaterally, enter into an obligation restricting or regulating the development or use of land".

- 9.2.30 S.75 obligations restricting the use of land to housing for key workers could either be imposed by the JV directly, or by the planning authority.
- 9.2.31 In the former scenario, the JV would put forward a planning application which would specify that all or part of the development will deliver housing for identified key workers (or another special category of occupier class). Any grant of consent would be supported by a planning obligation/s.75 agreement which would restrict the use of the specified units to key worker accommodation and as owners' principal residences, and those restrictions would be tied to the land and therefore bind successor owners.
- 9.2.32 In the latter scenario, the planning authority would impose a planning obligation on the JV to deliver affordable housing as part of the larger development for which planning permission is sought. NPF4 directs planning authorities to seek a minimum of 25% affordable units as part of any new residential developments. A higher or lower percentage can be justified at local level. Where the local planning authority has identified housing targeted at key workers (or another special category of occupier class) as affordable housing in terms of its affordable housing policy, the obligation could specify housing for key workers as a category of affordable housing within the policy.
- 9.2.33 Often the s. 75 agreement will require the affordable housing to be provided as accommodation for social rent and transferred to a local authority or RSL as that tenure. However, there is not a requirement for the drafting to specify a specific tenure, and it is not unusual for the s. 75 agreement to simply require "an affordable housing scheme" to be submitted as part of the first application for approval of matters specified in conditions with the specific affordable tenures being identified at this stage, which would be when the key-worker criterion would be incorporated.
- 9.2.34 In each case, the planning obligation would prescribe a percentage discount to be applied to the price payable on sale and secure the long-term availability of the housing at this discounted price for key workers by prescribing criteria which apply to permitted (or qualifying) purchasers entitled to benefit from the discount. Each prospective purchaser (including second and subsequent purchasers) would be referred by the seller (whether the first seller or subsequent owners) to the Council for



consideration against the criteria. Sales to prospective purchasers who are assessed as meeting the criteria will be referred to the then seller to proceed with the sale. In the event that there are no purchasers in the market who meet the criteria, the s.75 Agreement can provide for alternative permitted disposal (e.g. to a Council or an RSL), and finally can permit sale on the open market (usually subject to an overage payment to mitigate any windfall received by the seller against the restricted price paid)<sup>32</sup>.

- 9.2.35 Although s. 75 Agreements are open to variation after the grant of the associated planning permission, variations to the provisions dealing with the delivery of affordable housing are not generally challenged. Where the planning application is made on the basis that the development will be for affordable housing, the principle of the development is founded on the housing being delivered as affordable homes so there will be very limited grounds for challenge on the basis of the restriction of the use of the land for affordable housing. Where a planning obligation is imposed by the planning authority requiring the delivery of affordable housing as a percentage of the overall development, the percentage will be supported by national/local policy and will usually have been factored into the developer's cost analysis and therefore will generally not be subject to challenge.
- 9.2.36 If the Council wanted to convert housing which was delivered in terms of the s.75 agreement from affordable housing to market housing, the s.75 agreement will usually incorporate a clause which allows an affordable house to be sold as market housing if there is no demand from the identified group of priority purchasers, and the Council does not want to purchase itself. The developer will be obliged to pay a commuted sum in lieu of providing the house for affordable housing and sell it at market value. This would also apply to subsequent proprietors. If a landowner wanted to remove the obligation, they would apply to the Council to vary it either by agreement or under a s75A application. Where the house has been transferred to the Council, technically the Council could not vary the s. 75 agreement as it could not enter into an agreement with itself, it would simply stop enforcing the s. 75 agreement. However, where the Council has acquired the house from a developer at affordable housing value, it

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<sup>32</sup> Note that where the planning authority has identified housing targeted at key workers (or another special category of occupier class) as affordable housing, in terms of NPF4 Policy 16(F) a planning application for a proposed development of new homes on land not allocated for housing in the Local Development Plan will be supported provided the proposal is for less than 50 units.

would likely need to pay to the developer an uplift on the price reflecting the difference between the affordable and market values.

- 9.2.37 **Contractually**, the occupation of housing by people meeting key-worker criteria and who also satisfy the requirement to occupy the housing as their principal residence could be secured at the point of disposal, by way of a personal contract between the JV and purchaser, backed by a standard security. This is the mechanism used to secure obligations in help to buy/new supply shared equity schemes.
- 9.2.38 Effectively, the JV would retain an equity interest in the property sold which would notionally reflect the difference between the open market value (i.e., without any occupancy restriction) and the value taking account of the restriction. In exchange of the JV's equity, the purchaser would undertake to perform particular obligations, which could include obligations restricting the onward sale of the house— generally by way of an option to buy back the property prior to open market disposal either for the seller or their nominee.
- 9.2.39 The registration of a standard security in favour of the JV would act as a "red flag" to any third-party purchaser considering purchasing the property that there are continuing obligations affecting the property to be considered<sup>33</sup>. The security also prevents the property being sold without the consent of the JV who would need to sign a discharge of the standard security prior to completion of any disposal.
- 9.2.40 Usually, shared equity arrangements permit the purchaser to "tranche up" their equity interest, often up to 100% at which point the obligations due to the equity holder (including the standard security would be discharged). This can be avoided by use of the "golden share" mechanism whereby there would be a limit on the extent to which the purchaser can tranche up – usually up to 80% of open market value.
- 9.2.41 Another contractual mechanism would be the use of **personal pre-emption rights** ("PPERs"). PPERs are similar to pre-emption burdens and the pre-emption rights which form part of an RHB in that they will offer the original seller of homes the option to buy-back housing prior to disposal on the open market. The differences are that PPERs are contractual in nature between the original seller and purchaser and therefore the right to enforce PPERs

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<sup>33</sup> The Land Reform (Scotland) Act 1974 provides that the owner of secured property can receive a discharge of the standard security at year 20 provided that the balance of their loan, plus any interest and fees due, is paid. This is known as 'the 20 year security rule'. To mitigate this risk Scottish Ministers put in place legislation which removes this right in certain circumstances for certain named schemes (these include the New Supply Shared Equity Scheme, Help to Adapt and Help to Buy (Scotland)).

could not be transferred to a third party. Unlike pre-emption burdens, PPERs do not require a benefitted property to be enforceable and therefore offer a helpful alternative where the housing site is not adjacent to other land owned by the party seeking to enforce the pre-emption. Unlike with RHBs, there is no limit on the type of party who can enforce the pre-emption, i.e., there is no requirement for a rural housing body to be involved. The obligation to offer the PPER to the party entitled to receive it could be secured by a standard security, however the security itself will only be enforceable for a period of 20 years<sup>34</sup>, creating a practical timescale for the enforceability of the PPER. The security would be created over the house in question.

9.2.42 Title conditions and s.75 agreements could both be very effective mechanisms for securing the availability of housing for purchasers who meet specific criteria in the long term. These mechanisms also, in theory, offer a means of enforcing conditions during occupation, although it would generally be relatively resource intensive to monitor the changing circumstances of occupiers during the period of occupation. It is generally accepted practice that it is only on change of occupier that criteria are applied<sup>35</sup>.

### 9.3 **At what stage does the Council need to set up a Housing Revenue Account in order to retain ownership of the properties for rent?**

9.3.1 While the Council (in this case study) is not under any current obligation to maintain a Housing Revenue Account ("HRA"), we think it inevitable that, if the Council intended to maintain any properties for rent in its ownership, it would need to re-establish an HRA. As outlined in the case study, at the point at which the Council is considering the project proposal, it is a "stock transfer authority", meaning it does not have any housing stock and, therefore, because of an Alteration to Housing Finance Arrangement Order the prior (default) requirement to maintain an HRA is no longer in effect. We would expect Scottish Ministers to revoke or amend that Order at the point at which the Council wished to exercise relevant functions under Housing (Scotland) Act 1987 ("1987 Act") again (i.e., at the point at which

<sup>34</sup> As noted above, in terms of the Land Reform (Scotland) Act 1974, at year 20 year the homeowner would be entitled to receive a discharge of the standard security provided that they have performed the secured obligations, being in this case to offer the pre-emption. If the pre-emption wasn't exercised at this point, the standard security would be discharged.

<sup>35</sup> Scenarios could conceivably arise whereby a house is owned by 2 individuals, one of whom met the criteria at the point of purchase and that person dies and a third party who does not meet the criteria succeeds to the ownership interest, or otherwise ceases to be in occupation leaving an occupier who does not meet the criteria. In these scenarios, the party entitled to enforce would want the option to recover possession by way of enforcement action, although may not do so for policy reasons.

it began to provide (at least) affordable housing for rent) as this would re-engage the requirement to ringfence housing revenue.

- 9.3.2 Assuming the obligation is revived, a property has to be accounted for within the HRA if it is provided under Part 1 of the 1987 Act (entitled Provision of Housing) and various earlier equivalents. Any land which the Council acquires or appropriates for the purpose of Part 1 of the 1987 Act will also need to be accounted for within the HRA.
- 9.3.3 While the situation is less clear in respect of housing for open market rent (and, as such, not provided under the Council's 1987 Act functions), on balance, we consider it likely that such housing would also need to be accounted for within the HRA. This is because, in broad terms, the purpose of an HRA account is to ensure that there is transparency in accounting for income and expenditure in relation to the housing and the other functions undertaken by Councils and that one does not subsidise the other.
- 9.3.4 As such, the obligation to set up an HRA would arise as soon as: (i) the Council acquired or appropriated land for use for affordable housing or (ii) the properties built by the JV were conveyed by the JV to the Council and the Council allocated them for housing purposes.
- 9.3.5 We recommend that the Council enters into discussions with Scottish Ministers in relation to the re-establishment of an HRA prior to the JV returning ownership of properties to the Council. Those discussions should take place at the point at which the project proposal has crystallised but before it is commenced. Given the legislative uncertainty we have flagged above at 9.3.3, we recommend that the Council engages with Scottish Ministers to understand, if an HRA is to operate, whether the Scottish Ministers understand that the accounting requirements would apply not only to affordable homes (which we take to include social renting housing and mid-market rent) but also to homes leased at open market value. A shared understanding amongst the Council and the Scottish Ministers of any obligation (or lack thereof) to account for open market rented houses maintained by Councils in an HRA would mitigate legal risk, although legal certainty as to the extent of any such obligation could only be delivered by a court. Having said that, if the Scottish Ministers are in agreement with what is being proposed it is not evident that a third party is likely to challenge whatever arrangement is adopted.

#### 9.4 **Must homes for affordable rent be offered at the established LHA rental value, or can a different, locally affordable rental value be determined?**

9.4.1 If the Council will raise the price payable to the JV for homes using an element of grant funding allocated through the Affordable Housing Supply Programme, then we would expect grant funding conditions to provide for rents to be set with reference to the prevailing SG guidance<sup>36</sup> which provides that in most cases, the starting rent level for each mid-market rent home (including any service charge) will be no more than the relevant Local Housing Allowance rate for the property size in question. There is a degree of flexibility available "on an exceptional basis" to starting rent levels being more than the relevant Local Housing Allowance rate if the following cumulative conditions are met:

9.4.1.1 the grant applicant (which would be the Council) can demonstrate that, in a particular local market area, conditions are materially different from the relevant Local Housing Allowance rate; and

9.4.1.2 the starting rent levels do not exceed the mid-point of market rent levels for the property sizes in question in the relevant Broad Rental Market Area (as assessed by the Scottish Government).

9.4.2 During the operation of housing as MMR, rents can be increased, but must not at any time exceed (a) the mid-point of market rent levels for the property sizes in question in the relevant Broad Rental Market Area<sup>37</sup> (as assessed by the Scottish Government) or (b) where agreed in writing with the Scottish Government and the Council or – in the case of Glasgow and Edinburgh – the relevant City Council, the mid-point of market rent levels for the property sizes in question in a particular local market area – where this is demonstrated and accepted as being materially different from the relevant Broad Rental Market Area.

9.4.3 If the acquisition of properties by the Council from the JV is being funded to any extent by way of a loan from either the Council or Scottish Government on terms which are more advantageous than generally

<sup>36</sup>

MHDGN2022/02 [https://www.gov.scot/binaries/content/documents/govscot/publications/correspondence/2022/11/affordable-housing-supply-programme-process-and-procedures-mhdgn-2022-02/documents/mhdgn-2022-02---affordable-housing-supply-programme-ahsp-process-and-procedures/mhdgn-2022-02---affordable-housing-supply-programme-ahsp-process-and-procedures/govscot%3Adocument/Guidance%2Band%2BProcedures%2B-%2BMHDGN%2B2022\\_02%2B-%2BAffordable%2BHousing%2BSupply%2BProgramme%2B%2528AHSP%2529%2BProcess%2Band%2BProcedures.pdf](https://www.gov.scot/binaries/content/documents/govscot/publications/correspondence/2022/11/affordable-housing-supply-programme-process-and-procedures-mhdgn-2022-02/documents/mhdgn-2022-02---affordable-housing-supply-programme-ahsp-process-and-procedures/mhdgn-2022-02---affordable-housing-supply-programme-ahsp-process-and-procedures/govscot%3Adocument/Guidance%2Band%2BProcedures%2B-%2BMHDGN%2B2022_02%2B-%2BAffordable%2BHousing%2BSupply%2BProgramme%2B%2528AHSP%2529%2BProcess%2Band%2BProcedures.pdf)

<sup>37</sup> SG guidance does not specify whether this is the 30<sup>th</sup> or 50<sup>th</sup> percentile.

available on the lending market, then Subsidy Control will be a consideration.

- 9.4.4 If the purchase price is being funded by commercial finance or from Council reserves, there are no strict requirements for rent levels – rents can be set at whatever level the local market can bear.

9.5 **What is the legal basis, and processes, for the Council to secure full ownership of the houses for rent (open market, mid-market and affordable) i.e. acquisition from the JV**

- 9.5.1 Depending on project arrangements, there would likely be a pre-determined process for the transfer of ownership from the JV to the Council which would be set out in contractual terms – likely among the other contract terms agreed between the JV and the Council. These transfer provisions should include:

- 9.5.1.1 Where the price payable by the Council has not been pre-determined, a mechanism for calculating the price. This could be calculated with reference to variety of factors, including residual land value and development cost (including the cost of remediating abnormalities) depending on the wider commercial terms agreed between the parties;
- 9.5.1.2 Where the date of entry/completion has not been pre-determined, a mechanism for determining this – which could be with reference to the satisfaction of conditions precedent, such as practical completion of the housing being certified;
- 9.5.1.3 Conveyancing obligations, which would include delivery of the title transfer document (the disposition) and any security release documentation relating to charges granted by the JV to the Council together with documentation included housebuilder warranty documentation (e.g. NHBC/Premier Guarantee policy documents), evidence of statutory consents having been granted and complied with, collateral warranties from appropriate members of the construction team, and any other documentation required reflecting site specific issues (in particular, delivery of a title insurance policy if relevant);
- 9.5.1.4 Diligence obligations which would oblige the JV to either deliver all diligence documentation required to enable the Council to satisfy itself on title (this would include the title deeds, conveyancing searches (legal report, plans report, property enquiry certificate, road adoption plan, coal authority report (if relevant), charges search, RCIL search, planning information and other consents). Alternatively, the JV could be required to certify that good title to

the property would be conveyed to the Council, by way of a Certificate of Title;

- 9.5.1.5 Provisions dealing with normal conveyancing mechanics, such as Land Registration of Advance Notices and provision of additional documentation required by the Keeper for completion of Land Register will be required.

9.6 **Once it takes ownership, can the Council manage the open market value homes for rent through its existing housing service, or does it need to establish a separate arm's length entity?**

- 9.6.1 We do not consider there would be any obligation upon the Council to manage open market value homes for rent through its existing housing service, although there may be advantages to such an arrangement particularly if there is in-house capacity coupled with relevant experience and expertise. It would also be open to a Council to retain ownership of open market value homes but to outsource the management thereof to a third party although this would not change the status of the leases granted by the Council.
- 9.6.2 However, in terms of section 11 of the Housing (Scotland) Act 2001 (subject to limited exceptions), a tenancy of a house is an SST if it is: (a) let as a separate dwelling, (b) the landlord is a local authority landlord, and (c) the tenant is an individual and the house is the tenant's only or principal home. The Council will wish to consider whether it wishes the open market value homes (and indeed the MMR homes) to be SSTs. Use of a separate entity would allow for the granting of PRTs.
- 9.6.3 We would caution against the creation of a separate entity solely for the purpose of granting PRTs, as that arrangement might be open to challenge on the basis that it is intended to circumvent the default statutory position (i.e. that Council homes are occupied under SSTs). The issue would be less likely to arise where the separate entity was a JV (unless, of course, the JV, was a registered social landlord). There may be a range of reasons why a Council would wish to create a separate entity. These might include separating out management of socially rented housing from mid-market or full market rent, including the requirement to bring in any additional expertise or to simplify key decisions e.g. in relation to setting of rents where these are subject to a number of different considerations.

9.7 **What market failure rationale(s) could be applied to the project?**

- 9.7.1 We note the comments in the question regarding the lack of private sector development in the area in the past 5 years. The Best Value Guidance

issued by the Scottish Government under section 2(1)(a) of the 2003 Act, to which Councils must have regard when exercising the s.20 power (and any other power) requires the Council to work in partnership with "a wide range of national, regional and local agencies and interests across the public, third and private sectors". It should be able to demonstrate "how its partnership arrangements lead to the achievement of best value". The requirement in the Guidance for a Council to make best use of its financial and other resources, and to work with partners to maximise the use of their respective resources, should be read in this context.

9.7.2 We consider the implication of section 1 of the 2003 Act, read alongside the Best Value Guidance, to be that the Council should carefully consider, in circumstances in which it is engaging in an activity which may displace the private sector (particularly local businesses), whether doing so is reasonable, proportionate and consistent with its best value obligations. In order to do that it will be necessary for the Council to establish what the relevant market(s) in which it seeks to intervene are, and the reasons for a lack of private activity in those markets. For example, we note that there has been no private sector housebuilding within a 10-mile radius in 5 years – if a lack of private sector housebuilding was attributable to difficulty obtaining detailed planning permission (notwithstanding that the land is described as "readily developable"), planning permission on terms acceptable to private developers (with particular regard to section 75 obligations) or a lack of demand, then the Council could not be said to be remedying a market failure.

9.7.3 However, given that there are readily developable housing sites allocated on the LDP it may be that there are other reasons for a lack of private sector housebuilding. The Council will need to consider (with the benefit of specialist advice) what the reasons for that are, but if the answer is simply that any that profit stands to be made from the sale or rental prices achievable in the locality is not attractive to commercial sector developers, then the Council could determine that to be a market failure, on the basis that the returns being sought are more than the local market will bear (even if the national housing market would bear them on average). Markets can also, with appropriate justification, be drawn more narrowly with regard to tenure type.

9.8 **In relation to the wellbeing power, can the profit generated from the development (allowing for cross-subsidy of the affordable housing) be used to support the Council's general functions, or is there a requirement to ring-fence the profit for activities that deliver wellbeing for the local area?**



- 9.8.1 While there is no impediment to the JV generating profits, any profit that the Council's share in the JV would entitle it to, could not be removed from the JV in this way or for this purpose. The 2003 Act provides that the power to advance wellbeing cannot be used for the purpose of raising money – this extends beyond circumstances where profit generation is the primary purpose of the project and includes any circumstances where profit generation is a foreseeable outcome. The Council accordingly cannot proceed on the basis that profits (which in this case are anticipated and would therefore not be unforeseen if they were realised) can be used to generate revenue to provide or support other Council services. Moreover, the 2003 Act only allows reasonable charges to be imposed, which would limit the generation of a profit. It may be worth taking financial advice to assist in determining whether the building of houses for market rent and sale would qualify as trading under the Local Authorities (Goods and Services) Act 1970. If the Council concluded that the project proposal *would* amount to trading, but nonetheless considered there was a compelling case for its pursuit, the appropriate path, in our view, would not be to rely on the section 20 power, but instead to seek Scottish Ministers' consent for the proposed trading, in terms of the 1970 Act.
- 9.8.2 Given the 'gatekeeping' role of the Scottish Ministers in relation to local authority trading under the 1970 Act, the Council might wish to broach this point with the Scottish Ministers at an early stage. There would be no obligation for the Scottish Ministers to engage in a hypothetical or anticipatory discussion, and they might take the view that it was for the Council to satisfy itself as to the legality of its proposed actions albeit the Scottish Ministers would have to take their own view on whether trading ought to be something they would permit depending on the case before them.
- 9.8.3 A steer from Scottish Ministers as to: (i) what they considered would (and would not) amount to trading for the purposes of the 1970 Act and (ii) their likely attitude to any request for consent to such trading may, however, provide a level of assurance for the Council in progressing the project proposal. Nonetheless, even with such assurance, the possibility of challenge from others, including private sector developers, could not be ruled out completely.
- 9.8.4 The ring-fencing of any surplus generated to support the activities of the JV, in particular further developments, would avoid problems regarding withdrawal of profits. The JV partner will however wish to withdraw profits, so a mechanism will be required to avoid the reinvestment of the Council's

profits constituting a subsidy – an equity ratchet mechanism would be one approach, where the Council receives additional shares in lieu of a dividend. Clearly the corollary of this will be dilution of the partner's own shareholding, which may be difficult to agree. The Council could also explore a wholly owned intermediary between itself and the JV, where the intermediary ALEO could take dividends from the JV and reinvest those in further CBRS projects outside the JV. Alternative options might include a Registered Social Landlord or charitable body interposed between the Council and the JV with the Council's profit share being diverted to the interposed body.

**9.9 Does the proposed route to procure the JV partner, and the JVs subsequent procurement of its consultant/ contractor team, meet procurement rules? Are there any additional requirements associated with the use of the wellbeing power that need to be considered?**

9.9.1 The fact that the Council is proposing to use powers under s.20 of the 2003 Act does not imply additional procurement considerations. Considerations regarding best value can be incorporated into the design of the procurement process in both quality and price award criteria in order to achieve the "most economically advantageous tender" as set out in the Public Contracts (Scotland) Regulations 2015.

9.9.2 As noted above, whether or not the appointment of the JV partner and appointment by the JV of the consultant/contractor team need to follow a regulated procurement process (and, if so, which regulated process will apply) will depend on the nature of the proposed relationship between the Council and the JV and on how the JV is structured, as well as on the value of each contract. Legal advice on the applicability of the regulated procurement rules should be assessed on a case by case basis, however, a properly structured procurement process may, in any event, provide an opportunity to drive out best value.

**9.10 What consultation and engagement will be needed to demonstrate and evidence local stakeholder support – who, what, when, how etc?**

9.10.1 At a minimum we consider that the Council should be consulting with private sector housebuilders (albeit we note the lack of recent interest) and community planning partners. We also consider consultation should be carried out with the local community at large – that may involve working with community councils or other local groups, as well as convening further engagement events (we note a prior drop-in event has been held).

- 9.10.2 The Council should produce a consultation document which sets out the proposals in a reasonable degree of detail, and the rationale for them. It should also set out what (if any) alternatives have been considered and discounted. The consultation document (as well as any events or other engagement activities) should seek to obtain information which will help the Council to assess the extent of unmet demand for housing of the type proposed in the area. It would be desirable for the consultation process to align with the obtaining of specialist consultant support. That may involve the consultant themselves engaging with housebuilders to understand their lack of interest in development, and the reasons for this. If the Council is imposing, for example, a 'gold standard' in relation to new-build (such as with regard to indoor or outdoor space, energy efficiency or other parameters), the Council should seek to understand whether private sector delivery would be viable if a lesser, (but nonetheless lawful) standard was required.<sup>38</sup> Otherwise, the question may arise as to whether the market is not failing to deliver homes, but homes that meet the Council's standards, which will carry different considerations as to the Council's justification for intervention. Put another way – if such engagement indicates that the primary reason for the market not delivering homes is that the Council is requiring those homes to meet a standard, over and above the legal minimum, that could not be delivered profitably by market providers, then the Council would need to consult specifically on the need for it to provide homes *at that standard* (and not homes *per se*).
- 9.10.3 The consultation process should be completed prior to the Council taking a decision to commence the project that is proposed or any step that might reasonably be regarded as putting the outcome of the consultation beyond doubt. That does not mean preparatory work cannot be undertaken, but any such work should not treat as a foregone conclusion that the project proposal will be implemented, at all, or in the fashion currently anticipated.
- 9.10.4 Responses should be collated and conscientiously considered by the Council. The Council should be open minded to adjusting the proposals in light of consultation responses (including, if appropriate, by making significant changes to the proposals). While it will always be a matter of fact and degree, if a Council adjusts its proposals significantly in light of consultation responses, it will wish to consider whether a further round of consultation is needed.

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<sup>38</sup> This is only an example of the kind of feedback that may be received and, if so, taken account of by the Council (alongside all other relevant factors).

- 9.10.5 Any consultation exercise takes time and requires resource. It can though deliver significant benefit. As well as providing an evidence base, consultation can also demonstrate public support for project proposals. We consider that Councils are entitled to have regard to demonstrated local support when considering whether, and how, to use their section 20 power.
- 9.10.6 The Council needs to have regard to the Public Sector Equality Duty, the Fairer Scotland Duty, and other overarching obligations. We recommend that the Council carries out impact assessments in respect of these overarching obligations prior to consultation and invites representations on the assessed impacts as part of the consultation. Impact assessments should be updated as required in light of consultation responses.
- 9.10.7 We think a Fairer Scotland Impact Assessment, in particular, has the potential to be a source of assistance to the Council in the context of this case study, as it may demonstrate that adopting the proposal would contribute to reducing inequalities of outcome caused by socio-economic disadvantage.

## 10 CASE STUDY TWO

*A Council in a rural area wishes to purchase former Council housing stock in a failing housing estate of 100 homes where only 25 have remained in Council ownership, the other 75 homes will be acquired from individual private homeowners, giving the Council ownership of all homes in the estate. The estate is located within a small town with a population of 3,500 people.*

*The housing is of mixed quality, with poor lifecycle maintenance on 90% of the privately owned homes, of which half are below tolerable standard and need substantial investment. The private owners are unwilling, or unable, to fund the improvement works due to the low market value of the houses – on an individual basis, the cost of improving each house is higher than the net increase in value of the improved home following the works; on an aggregate basis, the Council will achieve cost savings on the construction works due to economies of scale, and will also benefit from enhanced values as all homes will be improved and works completed at the same time. The Council has been unable to bring sufficient numbers of the private owners together to act on a combined project that will create a financially viable delivery model.*

*The project is expected to make a small financial profit – this will be invested in common area landscaping in the estate. Financial viability will, however, depend on the acquisition price of the homes, as determined by the District Valuer.*

*The Council has consulted with tenants and owners on the estate and there is strong, but not unanimous, support – five homeowners intend to submit formal objections, 95 intend to submit formal letters of support.*

*The primary rationale for the project is to improve the quality of the housing stock. In addition, the Council wishes to address growing anti-social behaviour issues and will also use the project as a demonstrator for Net Zero Retrofit that other owners (public and private) can use in similar housing types elsewhere (1970s terraced two storey homes).*

*Existing Council tenants will be relocated over the duration of the works, thereafter, returning to their homes on the same tenancy agreement. Homeowners, and private tenants, will not be offered alternative accommodation. Of the 75 homes acquired, 25 will be retained by the Council and rented at mid-market value, the remaining 50 will be sold on the open market at mid-market level value housing.*

*Through a direct delivery model approach, the Council will procure consultants and contractors to design and deliver the project through one, or more, existing Framework agreements.*

## 10.1 **Whether the project outlined sufficiently demonstrates market failure?**

- 10.1.1 Before turning to whether the project sufficiently outlines market failure, it is necessary to address a preliminary question of whether, if demonstrated, a market failure could provide a basis in any event for the use of the s.20 power or other Council powers. In our view it would not. The Council does not have control of the site and would need to acquire it. Given opposition from some owners, the Council may struggle to demonstrate that it has reasonable prospects of gaining control of the site. This is because there are no powers of compulsory purchase that empower local authorities to acquire land (which includes houses) for the purpose of improving the quality of housing stock (unless the existing stock is below the tolerable standard) or that empowers local authorities to acquire land by means of compulsory purchase as a means of dealing with anti-social behaviour. There are other powers of compulsory purchase available but none that would appear to be appropriate to the circumstances described in this case study.
- 10.1.2 Even if that issue could be resolved, and it was possible to assemble the site without compulsory purchase powers, it is not clear how the acquisition of the properties would, on its own, result in a diminution of anti-social behaviour and thereby advance the well-being of the area or of people living in the area unless as part of a wider and clearly developed strategy. In relation to demonstrating the potential of Net Zero Retrofit there would need to be a clear rationale for this that is linked to the purpose of the section 20 power which again is the advancement of well-being.

- 10.1.3 It may also be difficult to anticipate how the Council could justify intervention to improve the overall housing stock of the area under the s.20 power when there is no intention for current residents to return to the renovated homes and if the net benefits of the intervention do not stack up against the cost of the intervention.
- 10.1.4 In light of the above, not therefore currently possible in our view for the project to sufficiently demonstrate the failure of the market to address these issues in a way that would permit the Council to do so using statutory powers – whether or not the market has failed to do so, the Council cannot.
- 10.1.5 We further note that if it was possible to assemble the site without compulsory purchase powers, then the direct delivery of the renovation of 75 homes (or such smaller number as could be acquired) would constitute a works contract (or a works contract and preliminary design services contract) that would need to be procured in accordance with the Public Contracts (Scotland) Regulations 2015. That could in principle be done through one or more existing Framework agreements, but the Council would need to ensure that those frameworks were suitable for use (in terms of the works covered by them, the "headroom" remaining in terms of how much of the advertised value of the framework had already been used up by call-off contracts, and the suitability of contractors available to be appointed).
- 10.2 **Whether there is a justification for CBRS as an appropriate route for the project, in particular the potential use of Compulsory Purchase Orders?**
- 10.2.1 See above at 10.1 re compulsory purchase powers. If that was removed as an obstacle (for example because all current owners were willing to sell at a price that the district valuer determined as appropriate), then CBRS using the s.20 power could be justified with respect to the first rationale (i.e. the general improvement of housing stock in the Council's area). It could not be justified with respect to the other rationales because they are too remotely connected to the requirement to advance wellbeing. Following the English court's decision in *Brent*<sup>39</sup>, the use of the power has to be directly linked to the advancement of wellbeing. We do not consider that this could underpin any sort of pilot project of the Net Zero Retrofit category.

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<sup>39</sup> *R (on the application of Risk Management Partners Limited) v Brent London Borough Council* [2009] EWCA Civ 490

10.2.2 In promoting the use of powers of compulsory purchase the Council will have to consider the range of powers available to it in respect of which CPO powers can be applied. Guidance issued by the Scottish Government sets out details of CPO powers available to Councils (and other public bodies) and the conditions that need to be satisfied for any of those powers to be used. If the Council considers that a CPO may be required, then it should consider what objectives to prioritise in order that the objectives are capable of being pursued using powers to which CPO powers attach. For example, where the Council's objectives are ones for which the Council's power to acquire land for housing can be used (such as the need for *additional* housing), that will in turn bring the potential for use of CPO powers where the conditions for those can be satisfied.

**10.3 If all three rationales for the project are aligned with the wellbeing power.**

10.3.1 A Council has the power to do anything which it considers is likely to promote or improve the well-being of its area and persons within that area. There must be a clear link between what is done under the section 20 power and the resultant impact on wellbeing. We consider that improving the quality of local housing stock in the area is (subject to the comments above) likely to be capable of being pursued using the section 20 power in the manner that is proposed but that tackling anti-social behaviour may not (although it might be tackled in other ways using the section 20 power). It may be possible to incorporate both of these things into the overall rationale for exercising powers of compulsory purchase, but tackling anti-social behaviour, is not a primary objective permitted by any statute that confers CPO powers on a Council and could only ever constitute a secondary purpose or objective.

**10.4 What, and if so where/how, might any conflicts arise with local stakeholders?**

10.4.1 We consider there are a number of potential conflict points with stakeholders:

10.4.1.1 Certain properties may be in negative equity, meaning any compensation they are entitled to in respect of the purchase of their properties will not be sufficient to discharge their liabilities. This may provoke conflict because, where there is a heritable creditor in respect of a property subject to CPO, the promoter of the CPO must discharge that debt prior to paying any amount out to the owner.

- 10.4.1.2 Existing Council tenants may be resistant to the offers of alternative accommodation made available to them for the duration of the works.
- 10.4.1.3 Private tenants may be resistant to being evicted from properties even though the owners of those properties are content with the works involved in implementing the project proposal.
- 10.4.1.4 The Council will wish to devise a strategy to minimise, mitigate and respond appropriately to these sources of potential conflict.
- 10.4.1.5 In relation to private owners and tenants (in respect of whom any CPO is likely to directly affect their rights) we recommend that the Council carries out an integrated impact assessment ("IIA").
- 10.4.1.6 An IIA will be particularly important where (as appears likely in this case study) the proposed CPO relates to properties owned or occupied by persons with low-income levels and/or owned by those in negative equity. We think it will be necessary to show that these factors have been considered along with appropriate mitigation measures in order to fully demonstrate that there is a compelling case that the CPO should proceed.
- 10.4.1.7 Our experience is that the carrying out of an IIA in these circumstances often indicates a need for adaptations to a Council's relocation strategy. In this case study, we note that the Council does not intend to make any tailored arrangements for alternative accommodation for private owners or their tenants. If it maintains this position, we consider the Council may face pushback from private owners and tenants, including at the point at which it seeks confirmation of the CPO from Scottish Ministers. The Scottish Ministers will likely have concerns where tenants may become homeless because of a decision to progress a CPO and where owners in negative equity are likely to be impacted upon if a CPO is confirmed. The Scottish Ministers may seek assurances that all reasonable mitigations have been considered before confirming the CPO. We refer to our comments in the preceding paragraph.
- 10.4.1.8 We recommend that the Council engages from an early stage with its social tenants, with a view to: (i) explaining the benefits of the project proposal to them, (ii) ensuring the project design is informed by their views and (iii) where possible, securing their support for the project proposal.

**10.5 If the proposed route to procure the design/ delivery team via an existing Framework(s) complies with procurement rules? Are there any additional requirements for procurement associated with the use of the wellbeing power?**



10.5.1 There is in principle no reason why this could not be delivered via an existing framework provided that the framework is one that is suitable for use and available for these contracts. A framework cannot be used for a call-off that a reasonably well informed and normally diligent tenderer would not have foreseen being awarded under the framework at the time at which it was advertised. A framework would not be suitable for anything more complex than a narrow design and build contract – for example if the Council was looking for more innovative delivery options this would generally point to a standalone procurement. The fact that the Council is proposing to use powers under s.20 of the 2003 Act does not imply additional procurement considerations.

## 10.6 Other legal issues

10.6.1 In this case study, we note that the project is expected to make a small financial profit. This raises a question of whether this activity would be struck at by the trading restrictions in the 1970 Act. It may be worth taking financial advice to assist in determining whether the building of houses for market rent and sale would qualify as trading under the 1970 Act. Given the 'gatekeeping' role of Scottish Ministers in relation to local authority trading under the 1970 Act, the Council might also wish to broach this point with the Scottish Ministers.

10.6.2 Subject to the views of financial advisors (and, if consulted and willing to express a view, the Scottish Ministers) we would have thought that the landscaping of common areas within the estate could itself be accounted for in the expenditure for the project proposal. This may reduce the likelihood of any profit being, in fact, realised, and therefore mitigate any risk that the Council contravenes the 1970 Act restrictions. Ultimately, only a court, faced with a challenge to the Council's actions could ultimately determine whether any unlawful trading had occurred.

## 11 CASE STUDY THREE

*A Council wishes to acquire and refurbish commercial town centre premises to create new mid-market and market value flats in a large town with a population of 35,000 people. There is an active housebuilding market in the provision of open market value housing in the area.*

*Five commercial office buildings will be acquired from four different public and private owners to be redeveloped to create 100 new residential flats – 60 at mid-market value and 40 at open market value. To deliver the project, the Council will establish a new subsidiary model (Council owned limited liability company) to undertake project development and delivery before the housing is sold on the open market to owner occupiers.*

*Market analysis has been undertaken that confirms demand for the project but anecdotal feedback from developers/ investors shows that there is no interest from the private sector in delivering these homes. A Town Centre Strategy was completed and published two years ago by the Council – this involved stakeholder consultation (local people, businesses, and relevant organisations) which confirmed support for the Council to deliver housing in the town centre.*

*The Council wishes to use the project as a demonstrator for other towns with similarly high levels of vacant office space – proving demand and technical viability.*

*The Council has determined the wellbeing rationale in two ways – firstly, meeting unmet demand for accessible town centre living; and secondly, as sustaining and safeguarding existing town centre (public and private sector) services through increased usage.*

*The Council will procure consultants and contractor(s) to design and deliver the project through standard Council procedures.*

*The Council's initial project appraisal confirms that the project is not financially viable without substantial levels of grant funding, or acknowledgement that the project will not generate a net inflow.*

*The Council wishes to ring-fence the income generated from the sale of the flats to fund similar future projects in its other town centres – this could be via projects delivered by the Council (gap funding), or by a Housing Association/ Registered Social Landlord/ private developer (grant funding).*

**11.1 How the purchaser criteria for the mid-market flats needs to be determined to align with the wellbeing and market failure rationales? What protocols and procedures need to be put in place to establish this approach?**

- 11.1.1 The allocation of homes for rent to target groups who meet specific criteria is an established practice in the context of housing for mid-market rent ("MMR") and affordable housing for sale (particularly new supply shared equity).
- 11.1.2 The initial allocation of homes to groups who meet specific criteria will depend on the establishment of clear criteria against which all applications received can be considered. These criteria would be set down in an allocations policy which would be available for review externally.
- 11.1.3 Traditionally, in the context of housing for MMR, criteria have centred around household income level (i.e., a maximum household income threshold) as the determining factor of need, given that MMR is aimed at assisting people on low and modest incomes to access affordable rented accommodation, and helps those who have difficulty accessing social

rented housing, buying their own home or renting privately on the open market.

11.1.4 Where housing is to be allocated based on applicants' status as a member of a group meeting specific criteria, it may be the case that multiple criteria need to be developed and satisfied prior to allocation as opposed to a singular criterion dealing with the primary requirement. This is because many key worker roles attract a wide range of salaries – for example – a teacher could earn between £28,113 and £99,609 depending on grade and role, therefore key worker status alone may not sufficiently identify housing need and should be supplemented with additional, traditional income criteria.

11.1.5 There is no legal restriction on the criteria which can be applied to individuals and households seeking housing, however allocations policies imposed by Councils (or their SPVs) are likely to require the approval of elected members. Generally, allocations policies should not be discriminatory however necessary and proportionate indirect discrimination to achieve a legitimate purpose (such as providing affordable housing for disadvantaged groups) is permissible. The availability and/or requirement for Housing Association Grant funding will also be relevant, as will questions of Subsidy Control and human rights issues.

11.1.6 Notwithstanding that there are no/limited restrictions on allocations criteria which can be applied once a PRT is granted, there are limited grounds for recovering vacant possession, which do not include a change to tenant circumstances such that initial allocation criteria are no longer satisfied. This means that it would be difficult to recover vacant possession in the event of a change in a tenant's circumstances which mean they no longer meet allocations criteria which applied at the point in time when they took entry.

**11.2 Does the new stock created, and subsequently sold, need to meet the quality standards of development that would be required by a Council if it was developing new homes for social rent?**

11.2.1 There would be no requirement for homes built for sale to comply with the SHQS. That said, as a risk mitigation measure, to enable the properties to be readily sold to a registered social landlord or operated as social housing by the Council, in the event that open market sale turned out not to be possible, the Council may wish to consider whether to align with that standard from the outset rather than to look to redesign at a later date.

There would be a balance to be struck between any initial outlay and the risk of the properties being transferred to the Council.

- 11.3 **What market testing and evidence is required – who / when / how much – to demonstrate that there is no interest from the private sector in undertaking the project? Also, what, if any, local stakeholder engagement is required – who / when / how much – to demonstrate local support. [Questions 3.3 and 3.4 (answered together because of degree of overlap)]**
- 11.3.1 We note that anecdotal feedback from developers/investors shows that there is no interest from the private sector in delivering these homes. We also note that a town centre strategy was completed and published two years ago by the Council, which involved stakeholder consultation.
- 11.3.2 This existing engagement is a useful starting point, but in our view, is not a substitute for proper consultation in relation to the proposals now in contemplation.
- 11.3.3 At a minimum we consider that the Council should be consulting with private sector housebuilders and community planning partners. In relation to housebuilders, if it is indeed the case that they have no interest in developing the homes now proposed, the Council should be seeking to understand why that is the case. If the Council is imposing, for example, a 'gold standard' through the planning system in relation to new-build, the Council should seek to understand whether private sector delivery would be viable if a lesser, (but nonetheless lawful) standard was required.<sup>40</sup> Otherwise, the question may arise as to whether the market is not failing to deliver homes of the *type* the Council considers are required, but homes that meet the Council's standards, which will carry different considerations as to the Council's justification for intervention.
- 11.3.4 We also consider consultation should be carried out with the local community at large – that may involve working with community councils or other local groups, as well as convening engagement events (e.g. 'town hall' meetings).
- 11.3.5 The Council should produce a consultation document which sets out the proposals in a reasonable degree of detail, and the rationale for them. It should also set out what (if any) alternatives have been considered and discounted. The consultation document (as well as any events or other engagement activities) should seek to obtain information which will help

<sup>40</sup> This is only an example of the kind of feedback that may be received and, if so, taken account of by the Council (alongside all other relevant factors).

the Council to assess the extent of unmet demand for housing of the type proposed in the area. We note that existing market analysis suggests that there is unmet need – we are not aware of the age / scope / full results of that work. It may be that the consultation process can be aligned with the obtaining of expert consultant support, so that the consultant themselves engages with housebuilders to understand their lack of interest in the proposed development, and the reasons for this.

- 11.3.6 The consultation process should be completed prior to the Council taking a decision to commence the project that is proposed or any step that might reasonably be regarded as putting the outcome of the consultation beyond doubt. That does not mean preparatory work cannot be undertaken, but any such work should not treat as a foregone conclusion that the project proposal will be implemented, at all, or in the fashion currently anticipated.
- 11.3.7 Responses should be collated and conscientiously considered by the Council. The Council should be open minded to adjusting the proposals in light of consultation responses (including, if appropriate, by making significant changes to the proposals). While it will always be a matter of fact and degree, if a Council adjusts its proposals significantly in light of consultation responses, it will wish to consider whether a further round of consultation is needed.
- 11.3.8 Any consultation exercise takes time and requires resource. It can though deliver significant benefit. As well as providing an evidence base, consultation can also demonstrate public support for project proposals. We consider that Councils are entitled to have regard to demonstrated local support when considering whether, and how, to use their section 20 power.
- 11.3.9 The Council needs to have regard to the Public Sector Equality Duty, the Fairer Scotland Duty, and other overarching obligations. We recommend that the Council carries out impact assessments in respect of these overarching obligations prior to consultation and invites representations on the assessed impacts as part of the consultation. Impact assessments should be updated as required in light of consultation responses.
- 11.3.10 We think a Fairer Scotland Impact Assessment, in particular, has the potential to be a source of assistance to the Council in the context of this case study, as it may demonstrate that adopting the proposal would contribute to reducing inequalities of outcome caused by socio-economic disadvantage.

#### 11.4 Does the project rationale demonstrate wellbeing – are there other rationales?

11.4.1 A Council has power to do anything which it considers is likely to promote or improve the well-being of its area and persons within that area. There must be a clear link between what is done under the section 20 power and the resultant impact on wellbeing. We consider that the purposes relating to: (i) meeting unmet demand for accessible town centre living and (ii) sustaining and existing town centre services through increased usage are likely to be capable of being pursued using the section 20 power. Whether it is an appropriate use of the section 20 power will be affected by the Council's engagement and its analysis in terms of market failure and best value we discuss below at 11.5.

#### 11.5 Does the project sufficiently demonstrate market failure?

11.5.1 The Best Value Guidance issued by the Scottish Government under section 2(1)(a) of the 2003 Act, to which Councils must have regard when exercising the section 20 power (and any other power) requires them to work in partnership with "a wide range of national, regional and local agencies and interests across the public, third and private sectors". A Council should be able to demonstrate "how its partnership arrangements lead to the achievement of best value". The requirement in the Guidance for a Council to make best use of its financial and other resources, and to work with partners to maximise the use of their respective resources, should be read in this context.

11.5.2 We consider the implication of section 1 of the 2003 Act, read alongside the Best Value Guidance, to be that the Council should carefully consider, in circumstances in which it is engaging in an activity which may displace the private sector (particularly local businesses), whether doing so is reasonable, proportionate and consistent with its best value obligations. That will involve the Council satisfying itself: (i) what the relevant market(s) in which it seeks to intervene are, and (ii) the reasons for a lack of private activity in those markets. In this case, we note there is an active housebuilding market in the provision of open market housing in the local area but that anecdotal feedback suggests no interest from the private sector in developing the homes provided for in the proposal. It will be essential for the Council to understand why this is the case. If for example, difficulty obtaining planning permission was the source of the difficulty, then that would not represent, in our view, an obvious example of *market* failure.

11.5.3 We note that the Council's initial project appraisal confirms that the project would not be financially viable without substantial levels of grant funding, or acknowledgment that the project will not generate a net inflow. That being so, it would not be surprising if the reason for the lack of interest in developing the homes provided for in the proposal was not an anticipated lack of demand, but rather a commercially unattractive (or no) profit stood to be made at the point of sale. If that was borne out by the analysis carried out in a specialist consultant report, the Council could, in our view, conclude that there was a market failure, in the sense we discuss above at section 3.

**11.6 Does the financial basis for the project (i.e., starting from the point of knowledge that there will be a financial loss for the public sector) impact on the rationale for the use of the wellbeing power? Can the wellbeing power be used where a project is making a loss?**

11.6.1 That a financial loss is likely to be occasioned to the Council does not necessarily conflict with use of the section 20 power, although it would be relevant to the proportionality analysis the Council would need to carry out. The Council is entitled to have regard to likely wider benefits associated with use of the section 20 power. Where benefits are identified they ought to have an evidential basis and, the less direct any such benefit is, the less weight can properly be placed upon it.

11.6.2 If a very significant loss was likely to be incurred by implementing the project proposal and the level of benefit to the area, or to people within it, limited, then we think the question would arise as to whether the Council, consistent with its best value obligations, could lawfully use the section 20 power. While we do not exclude a lawful application of the section 20 power in such circumstances, we consider the Council would wish to be satisfied of likely substantial, direct benefit(s) to the area (or any substantial direct disbenefits), or to the people within it before exercising the power, and to record carefully why it considered use of the section 20 power was appropriate, notwithstanding the likelihood of a very significant loss being incurred.

11.6.3 Another factor that may be relevant to the proportionality assessment is the Council's discharge of its statutory duties. If a Council was not fulfilling its statutory duties (in particular in the area of housing – e.g., homelessness obligations), or was doing so inadequately, we consider it would be more difficult for it to be satisfied that it was appropriate to exercise its section 20 powers in the manner contemplated, in the knowledge of the likelihood of a very significant loss.

- 11.6.4 That said, we expect a court would be reasonably deferential to the Council as to what was (or was not) proportionate, so long as the Council could demonstrate it had carefully considered the competing considerations.
- 11.6.5 Where a Council is able to show that implementation of the project proposal would not only benefit the wellbeing of the local area and/or persons within it but also that the project proposal was in line with national, regional or local policy commitments, it will be better placed to counter any argument that the likely financial loss means that the section 20 power cannot be lawfully used.

**11.7 Does the intended use of any income generated from the project to support future Council projects in other town centres conflict with the use of the wellbeing power?**

- 11.7.1 There is a distinction to be drawn between a surplus (which we do not understand is anticipated here) and recovery of (some) costs already incurred by the Council. There is no difficulty arising from the general law, or use of the section 20 power, with the Council recovering some of its costs. In that scenario, no charge is being imposed. The Council is restricting its financial model to include cost recovery only.
- 11.7.2 There is no legal prohibition on the monies coming back to the Council on a cost- recovery being ring-fenced for internal budgetary purposes which might include ring-fencing of funds in relation to broadly similar projects. The Council would wish to clear internally (including with its Finance Team) that such ring-fencing was not inconsistent with accounting principles, or the expectations of Audit Scotland. Any proposed ring-fencing should be reflected in the project documentation. However, it would be open to a Council to amend its position in relation to ring-fencing in the light of changing priorities/budgetary considerations.
- 11.7.3 If any grant funding was being used in connection with the project, the terms of such funding may make alternative provision for cost-recovered funds, for example, payment to the grantor.

**11.8 If the homes do not achieve a pre-set reserve price on the open market, what are the alternative options? Does this create any conflicts for the use of the wellbeing power and/ or subsidy control?**

- 11.8.1 Where the homes do not achieve the desired price on the open market, the Council-owned limited liability company, as a Council subsidiary, can sell to the Council but (in addition to the need for the directors of the company to satisfy themselves that the terms are in the best interests of the



company itself), the terms of that are subject to subsidy control rules, so if the Council pays more to acquire the relevant portfolio of properties than a "market buyer" in its position would then the difference may constitute a subsidy to the subsidiary. What will constitute "market value" for those purposes will of course turn partly on the potential letting or resale value of the properties taking into account any occupier restrictions. The Council-owned company could also sell to an RSL, subject to the same considerations.

- 11.8.2 If the Council is concerned that the reserve price cannot be achieved, then this will require to be taken into account in the initial assessment of using the s.20 power and in particular with regard to whether the proposals achieve best value. However, the test is that the exercise of the section 20 power is likely to advance well-being. It is not that the advancement of well-being is guaranteed. Where the power is under consideration it requires the exercise of a measure of judgement that is informed by appropriate professional advice.

## 12 CASE STUDY FOUR

*A Council wishes to develop CBRS on a small brownfield site to meet demand from people with special needs (e.g., disabled access, dementia friendly, young care leavers, etc). The Council is located in an urban city-region hinterland with a total population of c. 100,000 people across numerous small and medium-sized settlements.*

*The Council wishes to use a JV delivery structure with a local Housing Association – each investing 50% of all costs – to deliver 20 new build homes in a single phase development on a site to be acquired from a private owner. Half of the homes will be sold on the open market; the other half will be rented at open market value.*

*The JV will procure consultant and contractor teams on a competitive tendering basis. The rented stock will be retained by the JV and managed by the Housing Association.*

*There is an active private housebuilding market in the area but no interest in providing special needs housing. The Council owns such stock that is rented to tenants who are eligible and on the housing waiting list; market testing for the HNDA confirms that there is demand for, but no supply of, open market value homes.*

*No specific stakeholder engagement has been undertaken on the project, but the Council intends to undertake local public consultation as part of the project's pre-planning stage. The site is, however, identified within key strategic policy documents (including SHIP, HNDA and LDP) as being relevant for special needs housing development. There has therefore been an element of local consultation on the project.*

*The development is expected to be financially viable – the JV will distribute profit equally between the Council and HA, after agreed expenses have been met.*

## 12.1 What options are available to secure the HA partner (i.e. competitive procurement or direct appointment)?

12.1.1 This will depend on the nature of the Council's relationship with the JV and HA partner. If the JV will involve a specific obligation on either the JV entity or the HA partner to deliver specific requirements (i.e., the Council wishes to retain some control over the quantity and type of housing rather than leaving this to the discretion of the joint venture itself) then the HA will need to be procured. The "public-public" exemptions<sup>41</sup> will not apply in this scenario because of the lack of structural relationship between the Council and HA (i.e. the HA is not Council-owned) and the nature of the proposals and in particular the fact that the activities that the JV will be pursuing are not ones which the parties have a legal obligation to provide. However, if the Council is content that there will be no obligations on the JV or HA to do anything, then a JV structure can be formed with the Council's choice of HA under a direct appointment because no public contract will be established that would require to be procured (see paragraph 5.3 above).

12.1.2 The procurement of contractors etc. by the JV will require to be procured because the JV will be wholly controlled by contracting authorities. With an RSL as a partner the Council may be more prepared to invest without imposing any obligation to deliver specific outcomes.

## 12.2 How does the criteria for purchasers/tenants, based on the specific needs of the people that will occupy the homes, need to be defined? What needs to be put in place to establish this approach?

12.2.1 The allocation of homes to target groups who meet specific criteria is a well-established practice in the context of housing for mid-market rent and affordable housing for sale (particularly new supply shared equity), there is therefore precedent for the practice which will be helpful for CBRS housing.

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<sup>41</sup> Regulation 13 of the Public Contracts (Scotland) Regulations 2015 permits a contracting authority to directly award a contract to another public body in three circumstances:

- (i) where the contractor is controlled by the contracting authority (or by the same person who controls the contracting authority, or itself controls the contracting authority), provided that the contractor does not have any private sector owner and provides more than 80% of its services to the contracting authority (the "Teckal exemption");
- (ii) where the contracting authority controls the contractor jointly with one or more other contracting authorities, provided that the contractor does not have any private sector owner and provides more than 80% of its services to the contracting authorities that control it; and
- (iii) where the contracting authority and the contractor are seeking, for reasons of public interest alone, to jointly provide a public service that they both have an obligation to provide, and more than 80% of their activities in the relevant space are provided otherwise than on the open market (the "Hamburg Waste exemption").

- 12.2.2 The initial allocation of homes to groups who meet specific criteria for either rent or sale will depend on the establishment of clear criteria against which all applications received can be considered. These criteria would be set down in an allocations policy which would be available for review externally.
- 12.2.3 Traditionally, criteria have centred around household income level (i.e., a maximum household income threshold) as the determining factor of need.
- 12.2.4 Where housing is to be allocated based on applicants' status as a member of a group meeting specific criteria, it may be the case that multiple criteria need to be developed and satisfied prior to allocation as opposed to a singular criterion dealing with the primary requirement.
- 12.2.5 There is no legal restriction on the criteria which can be applied to individuals and households seeking housing, however allocations policies imposed by Councils (or their SPVs) are likely to require the approval of elected members where the Council has an interest in the JV. Generally, allocations policies should not be discriminatory however necessary and proportionate indirect discrimination to achieve a legitimate purpose (such as providing affordable housing for disadvantaged groups) is permissible. Questions of Subsidy Control and human rights issues will also be relevant.

**12.3 How can the Council ensure that in future these homes remain occupied (through onwards sale or rent) by people that meet the criteria? What legal options are there to secure this?**

Securing long term availability of housing for specific groups for rent

- 12.3.1 The initial allocation of homes to members of the target group for rent<sup>42</sup> will depend on the establishment of clear criteria against which all applications received can be considered. These criteria would be set down in an allocations policy which would be available for review<sup>43</sup> externally.
- 12.3.2 Notwithstanding that there are no/limited restrictions on allocations criteria which can be applied once a PRT is granted, there are limited grounds for recovering vacant possession, which do not include a change to tenant circumstances such that initial allocation criteria are no longer satisfied. This

<sup>42</sup> We assume that properties would be leased in terms of private residential tenancy agreements ("PRTs") in terms of the Private Housing (Tenancies) (Scotland) Act 2016.

<sup>43</sup> Although relating to MMR housing, see, for example, Manor Estates Housing Association's allocations policy for MMR <https://www.manorestates.org.uk/wp-content/uploads/2021/04/MMR-Allocation-Policy-September-2019.pdf>, and LAR Housing Trust's policy <https://lar.scot/what-is-mid-market-rent%3F>. NSSE criteria are available here: <https://www.mygov.scot/new-supply-shared-equity-scheme>

means that it would be difficult to recover vacant possession in the event of a change in a tenant's circumstances which mean they no longer meet allocations criteria which applied at the point in terms when they took entry.

#### Options for securing availability of housing for specific groups for sale

- 12.3.3 Options for securing homes for sale to people with special needs in the longer term (i.e., for successive disposals following the first disposal) can broadly be split into two categories, being "legal" and "contractual". In each case, these mechanisms could secure the ownership and occupation by groups who met specific allocations criteria related to special needs both on sale of individual units and on the bulk disposal of multiple units into a new single ownership.
- 12.3.4 "Legal" options for maintaining the availability of housing are to apply title conditions ("burdens") restricting the use of the land on which the housing is built to the specific purpose of providing housing for specific groups. This will in our view be best achieved by way of planning obligations imposed by way of a section 75 Agreement.
- 12.3.5 **s.75 Agreements<sup>44</sup>** also offer a mechanism by which the use of land could be restricted to accommodation for people with special needs. In terms of s75(1) "A person may in respect of land in the district of a planning authority (a) by agreement with that authority, or (b) unilaterally, enter into an obligation restricting or regulating the development or use of land".
- 12.3.6 S.75 obligations restricting the use of land to housing for people with special needs could either be imposed by the JV directly, or by the planning authority.
- 12.3.7 Given the terms of the case study, we anticipate that it will be the former scenario which will be relevant. The JV would put forward a planning application which would specify that all or part of the development will deliver housing for identified for people with special needs. Any grant of consent would be supported by a planning obligation/s.75 agreement which would restrict the use of the specified units to special needs accommodation and that restriction would be tied to the land and therefore bind successor owners.

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<sup>44</sup> Being Section 75 of the consolidated Town and Country Planning (Scotland) Act 1997 as amended in 2006 and came into force in February 2011

- 12.3.8 In the latter scenario, the planning authority would impose a planning obligation on the JV to deliver housing for people with special needs<sup>45</sup>.
- 12.3.9 In each case, the planning obligation would prescribe that each prospective purchaser (including second and subsequent purchasers) would be referred by the seller (whether the first seller or subsequent owners) to the Council for consideration against the predetermined allocations criteria. Sales to prospective purchasers who are assessed as meeting the criteria will be referred to the then seller to proceed with the sale. In the event that there are no purchasers in the market who meet the criteria, the s.75 Agreement can provide for alternative permitted disposal (e.g., to a Council), and finally can permit sale on the open market.
- 12.3.10 **Pre-emption Burden:** For scenarios where there is benefitted property available (for example, where development of special needs housing is part of a larger, general needs development site) a pre-emption burden would also be available as a mechanism for securing the long-term availability of the housing. A pre-emption burden would require the first purchaser of each home to make an offer to the JV entitling them to buy back the home. This could be at a pre-determined fixed price (which could also be subject to increases for inflation). However, a pre-emption burden would only be capable of exercise once – if the JV declined to exercise it (or otherwise waived the option) then the pre-emption right would be lost forever. If, however, the pre-emption was exercised, the JV would be able to impose a fresh pre-emption burden on the title to the home on its subsequent disposal.
- 12.3.11 **Contractually,** housing for sale can be secured for occupants requiring special needs accommodation at the point of disposal, by way of a personal contract between the JV and purchaser, backed by a standard security. This is the mechanism used to secure obligations in help to buy/new supply shared equity schemes.
- 12.3.12 Effectively, the purchaser would undertake to be bound by the obligation to occupy the home and otherwise perform particular obligations, which could include obligations dealing with resale – generally an option to buy back the property prior to open market disposal either for the JV or their nominee.

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<sup>45</sup> Housing for special needs is identified as a type of housing provision in terms of Policy 16 of National Planning Framework 4, but there is not a specific policy dealing with this type of accommodation. Usually, it is subsumed under affordable housing as it is often the type of housing most in need and hardest to provide for (although the other criteria for affordability also need to apply for it be classified as affordable housing).

- 12.3.13 The registration of a standard security<sup>46</sup> in favour of the seller acts as a "red flag" to any third-party purchaser considering purchasing the property that there are continuing obligations affecting the property to be considered. The security also prevents the property being sold without the consent of the JV who would need to sign a discharge of the standard security prior to completion of any disposal.
- 12.3.14 Another contractual mechanism would be the use of personal pre-emption rights ("PPERs"). PPERs are similar to pre-emption burdens in that they will offer the JV the option to buy-back housing prior to disposal on the open market. The differences are that PPERs are contractual in nature between the JV and purchaser and therefore the right to enforce PPERs could not be transferred to a third party. Unlike pre-emption burdens, PPERs do not require a benefitted property to be enforceable and therefore offer a helpful alternative where the housing site is not adjacent to other land owned by the party seeking to enforce the pre-emption. The obligation to offer the PPER to the party entitled to receive it could be secured by a standard security, however the security itself will only be enforceable for a period of 20 years<sup>47</sup>, creating a practical timescale for the enforceability of the PPER.
- 12.3.15 Title conditions and s.75 agreements could both be very effective mechanisms for securing the availability of housing for purchasers who require special needs housing in the long term. These mechanisms also, in theory, offer a means of enforcing conditions during occupation, although it would generally be relatively resource intensive to monitor the changing circumstances of occupiers during the period of occupation. It is generally accepted practice that it is only on change of occupier that criteria are applied<sup>48</sup>.

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<sup>46</sup> The Land Reform (Scotland) Act 1974 provides that the owner of secured property can receive a discharge of the standard security at year 20 provided that the balance of their loan, plus any interest and fees due, is paid. This is known as 'the 20 year security rule'. To mitigate this risk Scottish Ministers put in place legislation which removes this right in certain circumstances for certain named schemes (these include the New Supply Shared Equity Scheme, Help to Adapt and Help to Buy (Scotland)).

<sup>47</sup> As noted above, in terms of the Land Reform (Scotland) Act 1974, at year 20 year the homeowner would be entitled to receive a discharge of the standard security provided that they have performed the secured obligations, being in this case to offer the pre-emption. If the pre-emption wasn't exercised at this point, the standard security would be discharged.

<sup>48</sup> Scenarios could conceivably arise whereby a house is owned by 2 individuals, one of whom met the criteria at the point of purchase and that person dies and a third party who does not meet the criteria succeeds to the ownership interest, or otherwise ceases to be in occupation leaving an occupier who does not meet the criteria. In these scenarios, the party entitled to enforce would want the option to recover possession by way of enforcement action, although may not do so for policy reasons.

- 12.4 **Can the Council rely on the HNDA market testing to demonstrate demand, or is detailed market analysis/ testing required to support the demand analysis and demonstrate lack of interest from the private sector? Does the project sufficiently demonstrate market failure? Is further local consultation and engagement required, or can the Council rely on the work already completed (for SHIP/ HNDA/ LDP) and that proposed for the pre-planning stage? [Question 4.4 – 4.6 (answered together because of degree of overlap)]**
- 12.4.1 The HNDA market testing, depending on its: (i) age, (ii) scope, (iii) reliability and (iv) relevance to the project proposal is potentially a useful starting point in demonstrating demand. However, we would recommend that it is supported by further analysis – preferably carried out by a specialist consultant related to the specific project proposal under contemplation, which specifically addresses demand for housing for the various "special needs" identified. We suggest that that further analysis is undertaken as part of the work the Council carries out to be satisfied that this project proposal is an appropriate use of the section 20 power.
- 12.4.2 The Best Value Guidance issued by the Scottish Government under section 2(1)(a) of the 2003 Act, to which Councils must have regard when exercising the section 20 power (and any other power) requires the Council to work in partnership with "a wide range of national, regional and local agencies and interests across the public, third and private sectors". A Council should be able to demonstrate "how its partnership arrangements lead to the achievement of best value". The requirement in the Guidance for a Council to make best use of its financial and other resources, and to work with partners to maximise the use of their respective resources, should be read in this context.
- 12.4.3 We consider the implication of section 1 of the 2003 Act, read alongside the Best Value Guidance, to be that the Council should carefully consider, in circumstances in which it is engaging in an activity which may displace the private sector (particularly local businesses), whether doing so is reasonable, proportionate and consistent with its best value obligations. That will involve the Council satisfying itself: (i) what the relevant market(s) in which it seeks to intervene are, and (ii) the reasons for a lack of private activity in those markets. In this case, we note there is an active housebuilding market in the provision of open market housing in the local area but "no interest" in providing special needs housing. It is not clear what evidence underpins this assessment of (lack of) interest. It will be essential for the Council to understand (and be able to demonstrate): (i) that there is, indeed, not interest from the private sector in providing these homes and (ii) if so, why this is the case. As discussed, elsewhere in this

note, we consider analysis carried out by a specialist in respect of the local market would be necessary in order for the Council to arrive at this conclusion. It would make sense to align this analysis with the consultation process, discussed further below.

### Consultation

- 12.4.4 We note that the site has been identified within key strategic policy documents (including SHIP, HNDA and LDP) as "relevant" for "special needs housing development". We also note that there is an intention to consult at the pre-planning stage. This existing and planned engagement is useful, but itself is unlikely to be sufficient in our view.
- 12.4.5 At a minimum we consider that the Council should be consulting with private sector housebuilders, community planning partners and those with the "special needs" whom the project proposal is intended to benefit. The Council should consider any reasonable adjustments which may be needed to enable individuals with "special needs" to meaningfully engage in the consultation process.
- 12.4.6 We also consider consultation should be carried out with the local community at large – that may involve working with community councils or other local groups, as well as convening engagement events (e.g. 'town hall' meetings).
- 12.4.7 The Council should produce a consultation document which sets out the proposals in a reasonable degree of detail, and the rationale for them. It should also set out what (if any) alternatives have been considered and discounted. The consultation document (as well any events or other mediums) should seek to obtain information which will help the Council to assess the extent of unmet demand for housing of the type proposed in the area. We note that existing market analysis suggests that there is unmet need – we are not aware of the age / scope / full results of that work. It may be that the consultation process can be aligned with the obtaining of expert consultant support, so that the consultant themselves engages with housebuilders to understand their lack of interest in the proposed development, and the reasons for this. If the Council is imposing, for example, a 'gold standard' in relation to new build through the planning system, the Council should seek to understand whether private sector delivery would be viable if a lesser, (but nonetheless lawful) standard was



required.<sup>49</sup> Otherwise, the question may arise as to whether the market is not failing to deliver homes for those with "special needs", but homes for those with "special needs" that meet the Council's standards, which will carry different considerations as to the Council's justification for intervention.

- 12.4.8 The consultation process should be completed prior to the Council taking a decision to commence the project that is proposed or any step that might reasonably be regarded as putting the outcome of the consultation beyond doubt. That does not mean preparatory work cannot be undertaken, but any such work should not treat as a foregone conclusion that the project proposal will be implemented, at all, or in the fashion currently anticipated.
- 12.4.9 Responses should be collated and conscientiously considered by the Council. The Council should be open minded to adjusting the proposals in light of consultation responses (including, if appropriate, by making significant changes to the proposals). While it will always be a matter of fact and degree, if a Council adjusts its proposals significantly in light of consultation responses, it will wish to consider whether a further round of consultation is needed.
- 12.4.10 Any consultation exercise takes time and requires resource. It can though deliver significant benefit. As well as providing an evidence base, consultation can also demonstrate public support for project proposals. We consider that Councils are entitled to have regard to demonstrated local support when considering whether, and how, to use their section 20 power.
- 12.4.11 The Council needs to have regard to the Public Sector Equality Duty, the Fairer Scotland Duty, and other overarching obligations. We recommend that Council carries out impact assessments in respect of these overarching obligations prior to consultation and invites representations on the assessed impacts as part of the consultation. Impact assessments should be updated as required in light of consultation responses.
- 12.4.12 We think a Fairer Scotland Impact Assessment, in particular, has the potential to be a source of assistance to the Council in the context of this case study, as it may demonstrate that adopting the proposal would contribute to reducing inequalities of outcome caused by socio-economic disadvantage.

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<sup>49</sup> This is only an example of the kind of feedback that may be received and, if so, taken account of by the Council (alongside all other relevant factors).

- 12.5 **Is the rationale for the project aligned with the wellbeing power, and if so is CBRS an appropriate route?**
- 12.5.1 Under section 20, a Council has power to do anything which it considers is likely to promote or improve the well-being of its area and persons within that area. There must be a clear link between what is done under the section 20 power and the resultant impact on wellbeing.
- 12.5.2 We consider that the provision of housing to those in the local area with "special needs" is likely to be capable of being pursued using the section 20 power. Whether: (i) CBRS and (ii) use of the section 20 power are the appropriate mechanisms will be affected by the Council's engagement and its analysis in terms of market failure and best value we discuss above at 12.4.
- 12.6 **What, and if so where/how, might any conflicts arise with local stakeholders?**
- 12.6.1 We do not consider that the implementation of project proposal itself gives rise to particularly unusual conflict points. Therefore, the likely conflict points are those that would apply to development projects generally (e.g., objections to planning permission from neighbouring landowners).
- 12.6.2 The allocations policy implemented in respect of the houses forming part of this project proposal may also be a source of conflict. We recommend that any allocations policy is informed by consideration of the Public Sector Equality Duty (and potentially, depending on the role of the Council in connection with allocations, the Fairer Scotland Duty).
- 12.6.3 The management of those houses retained for young care leavers also represents a particular challenge.
- 12.6.4 We anticipate that houses designated for young care leavers will be intended to act as medium-term transition properties, rather than permanent accommodation. There is likely to be a time at which the Council will wish to move an existing occupant out of a house designated for a young care leaver, in order to allow a new care leaver to occupy the house. If the existing occupant does not wish to move out of the house, that is likely to lead to conflict. The Council's ability to recover possession in these circumstances will be affected by the type of occupancy rights it has granted.
- 12.7 **Other legal issues**

- 12.7.1 While there is no impediment to the JV generating profits, any profits that the Council's share in the JV would entitle it to, could not be removed from the JV in this way. The 2003 Act says that the power to advance wellbeing cannot be used for the purpose of raising money – this extends beyond circumstances where profit generation is the primary purpose of the project and includes any circumstances where profit generation is a foreseeable outcome. The Council accordingly cannot proceed on the basis that profits (which in this case are anticipated and would therefore not be unforeseen if they were realised) can return from the JV to the Council.
- 12.7.2 Moreover the 2003 Act only allows reasonable charges to be imposed, which would limit the generation of a profit. It may be worth taking financial advice to assist in determining whether the building of these houses for rent would qualify as trading under 1970 Act. If the Council concluded that the project proposal would amount to trading, but nonetheless considered there was a compelling case for its pursuit, the appropriate path, in our view, would not be to rely on the section 20 power, but instead to seek Scottish Ministers' consent for the proposed trading, in terms of the 1970 Act.
- 12.7.3 Given the 'gatekeeping' role of the Scottish Ministers in relation to local authority trading under the 1970 Act, the Council might wish to broach this point with the Scottish Ministers at an early stage. There would be no obligation for the Scottish Ministers to engage in a hypothetical or anticipatory discussion, and they might take the view that it was for the Council to satisfy itself as to the legality of its proposed actions.
- 12.7.4 A steer from Scottish Ministers as to: (i) what it considered would (and would not) amount to trading for the purposes of the 1970 Act and (ii) its likely attitude to any request for consent to such trading may provide a level of assurance for the Council in progressing the project proposal. Nonetheless, even with such assurance, the possibility of challenge from others, including private sector developers, could not be excluded.

## 13 CASE STUDY FIVE

*A Council wishes to develop a CBRS Programme via JV with a private developer over numerous mixed tenure development sites across several of its islands with the aim of delivering 200 new homes over a ten -year period. Some sites have been identified (and are in both Council and private ownership) but others need to be found. The aim is that, at Programme level, site development would be prioritised on the basis of maximising wellbeing, rather than the easiest/ quickest/ most profitable being developed first.*

*There is private sector interest in building market value housing in the more accessible locations, but insufficient delivery of affordable/ mid-market/ and remote rural housing stock. There is also insufficient delivery of open market value housing for rent across the whole of the Council's area.*

*The Council wishes to use the CBRS approach to ensure that sufficient housing across all tenures, market values, and locations is provided to meet the needs of its existing population. The Council also wishes to create housing choice that will attract new residents to live in its island communities.*

*The Council wishes to deliver wider social/ community/ economic outcomes i.e. a community wealth building approach (CWB) that builds market capacity in the SME contractor base and delivers recognised construction skills/ qualifications for local people.*

*The CBRS Programme is expected to be financially viable in total but there is a need for cross-subsidy between the housing types/ tenures/ locations (e.g., profit from the open market value housing in an accessible site will be used to fund loss-making housing elsewhere). There may, however, be a need for gap funding related to specific site locations and/ or to specific housing developments – this gap will be met by the Council or other public sector body.*

*The JV will agree a profit-sharing mechanism – at Programme and at individual site level. A level of profit will need to be retained within the JV to cover delivery of future phases/ sites that may be loss making.*

*The JV partner will be procured on an open market basis. The JV will procure its consultant/ contractor teams on a project-by-project basis using established procurement arrangements that align with Council procedures.*

*The JV will retain ownership of the housing for rent (across the different market value sectors including affordable) until the development of the full Programme has been completed but thereafter will sell this housing stock as an investment opportunity. The Council's share of the income generated will be used to fund investment in other housing projects – this could be either affordable social rented homes or further CBRS activity.*

*There is anecdotal evidence of demand for housing across all of the identified islands, but no specific or detailed community consultation at Programme or specific site project level.*

**13.1 How the criteria for the affordable/mid-market (for rent and sale)/special needs housing is to be determined? Does this need to be based on the Council's established criteria or can the JV determine site (or location) specific criteria based on local needs?**

13.1.1 The allocation of homes to target groups who meet specific criteria is an established practice in the context of housing for mid-market rent ("MMR") and affordable housing for sale (particularly new supply shared equity) therefore there is precedent available to the CBRS model for the practice of allocating homes to individuals who meet specific criteria.

13.1.2 The preferential allocation of homes to groups who meet specific criteria for either rent or sale will depend on the establishment of clear criteria

against which all applications received can be considered. These criteria would be set down in an allocations policy which would be available for review externally.

- 13.1.3 Traditionally, in the context of housing for MMR, criteria have centred around household income level (i.e., a maximum household income threshold) as the determining factor of need, given that MMR is aimed at assisting people on low and modest incomes to access affordable rented accommodation, and helps those who have difficulty accessing social rented housing, buying their own home or renting privately on the open market.
- 13.1.4 Where housing is to be allocated based on applicants' status as a member of a group meeting specific criteria, it may be the case that multiple criteria need to be developed and satisfied prior to allocation as opposed to a singular criterion dealing with the primary requirement.
- 13.1.5 There is no legal restriction on the criteria which can be applied to individuals and households seeking housing, however allocations policies imposed by Councils (or their SPVs) are likely to require the approval of elected members. Generally, allocations policies should not be discriminatory however necessary and proportionate indirect discrimination to achieve a legitimate purpose (such as providing affordable housing for disadvantaged groups) is permissible. The availability and/or requirement for Housing Association Grant funding will also be relevant, as will questions of Subsidy Control and human rights issues.
- 13.1.6 Notwithstanding that there are no/limited restrictions on allocations criteria which can be applied once a PRT is granted, there are limited statutory grounds for recovering vacant possession, which do not include a change to tenant circumstances such that initial allocation criteria are no longer satisfied. This means that in every scenario where the tenant's right of occupancy is in terms of a PRT, it would be difficult to recover vacant possession in the event of a change in a tenant's circumstances resulting in them no longer meeting allocations criteria which applied at the point in terms when they took entry.
- 13.1.7 In terms of whether the Council is bound by existing criteria or can determine site (or location) specific criteria based on local needs, the Council would be free to develop site specific criteria. However, if it was going to be advantageous for the housing to meet the Council's classification of affordable housing in terms of its affordable housing

policy<sup>50</sup>, then the Council should consider ensuring that the affordable housing policy does recognise the criteria to be applied as a category of affordable housing within the policy.

**13.2 How can the Council allocate a small portion of the houses for key workers and/or for principal home occupancy to ensure that these homes remain occupied on this basis for at least 10 years, but preferably in perpetuity? What does the Council need to put in place to secure this?**

- 13.2.1 Options for securing homes for sale as key worker accommodation and as the principal home of the owner<sup>51</sup> in the longer term (i.e., for successive disposals following the first disposal) can broadly be split into two categories, being "legal" and "contractual". In each case, these mechanisms could secure the use of housing as key worker accommodation and principal homes both on sale of individual units and on the bulk disposal of multiple units into a new single ownership.
- 13.2.2 "Legal" options for maintaining the availability of housing are to apply title conditions ("burdens") restricting the use of the land on which the housing is built to the specific purpose of providing housing for key workers and securing their occupation as principal homes. This could be achieved by way of the constitution of particular burdens against the title to the land on which the properties are to be developed, or planning obligations imposed by way of a section 75 Agreement.
- 13.2.3 With regard to burdens, legislation provides for three types of personal real burden (being burdens which can be enforced against a title holder by a third party who does not necessarily hold an interest in neighbouring ("benefitted") property) which could achieve this outcome. These are Healthcare Burdens, Economic Development Burdens ("EDBs") and Rural Housing Burdens ("RHBs").
- 13.2.4 Generally, burdens are self-policing in that any prospective owner would become aware of their terms during the standard conveyancing process and therefore know if they were about to purchase a home which included a condition which was contrary to their intended use. If the home was being purchased with mortgage finance, the presence of a burden on terms which could potentially restrict the open market value of the property would require

<sup>50</sup> Where the planning authority has identified housing targeted at a special category of occupier class as affordable housing, in terms of NPF4 Policy 16(F) a planning application for a proposed development of new homes on land not allocated for housing in the Local Development Plan will be supported provided the proposal is for less than 50 units.

<sup>51</sup> The alternative to a positive obligation to occupy as a primary residence would be a restriction on use as a second home or a holiday home or as commercial holiday accommodation.

to be reported to the mortgage provider. Burdens are also enforceable by the benefitted party or proprietor entitled to enforce the terms in the event that they become aware of a breach.

- 13.2.5 **Healthcare Burdens** can be created in favour of (and enforceable by) a health board, or the Scottish Ministers for *the purpose of promoting the provision of facilities for health care*<sup>52</sup>. Healthcare Burdens can be created other than by the health board or the Scottish Ministers with the consent<sup>53</sup> of the health board or the Scottish Ministers<sup>54</sup>.
- 13.2.6 "Facilities for health care" specifically includes facilities ancillary to health care, and the example given in the Act is "accommodation for staff employed to provide health care"<sup>55</sup>.
- 13.2.7 Healthcare Burdens therefore offer a clear route to secure housing for key workers who are employed to provide health care<sup>56</sup>. The Healthcare Burden would be registered against the title to housing for sale and would restrict occupation of the housing to health care workers<sup>57</sup>. Provision could be included restricting letting of the housing by owner occupiers without consent of the health board or Scottish Ministers. In the event of disposal to a non-health care worker, provision could be made for payment of a sum (equivalent to overage) to the health board or the Scottish Ministers reflecting the difference between the price of the house as affected by the use restriction contained in the title, and the open market value without the restriction, however this would result in the burden ceasing to apply in respect of future disposals.
- 13.2.8 It is possible for Healthcare Burdens to be created by a landowner which is not a health board or the Scottish Ministers for the benefit of a health board or the Scottish Ministers with their consent. This means that housing could be developed by the JV or another third party for the purpose of providing key-worker accommodation for health care workers and burdened with a Healthcare Burden which would be enforceable by the health board or Scottish Ministers with their agreement.

<sup>52</sup> s. 46 (1) Title Conditions (Scotland) Act 2003.

<sup>53</sup> Consent to be incorporated within the constitutive deed.

<sup>54</sup> s. 46 (2) Title Conditions (Scotland) Act 2003.

<sup>55</sup> s. 46 (6) Title Conditions (Scotland) Act 2003.

<sup>56</sup> However, the enforcement of healthcare burdens has not been tested.

<sup>57</sup> The market value of the homes would likely be suppressed due to the restriction on use to accommodation for staff employed to provide healthcare.

- 13.2.9 Healthcare Burdens, when validly created and registered against the title to the affected land will bind successor owners to their terms and therefore could be effective in securing the long-term availability of housing for key workers involved in the provision of health care.
- 13.2.10 **Economic Development Burdens** ("EDBs") are available for the purpose of "*promoting economic development*" and are often used by enterprise agencies, for example, Scottish Enterprise, as a means of ensuring that land which is sold for the purposes of generating economic development will be subject to a payment of overage in the event that the original disposal purpose is not achieved<sup>58</sup>.
- 13.2.11 Like Healthcare Burdens, EDBs could operate to restrict use of burdened property to a specific purpose (i.e. for the provision of housing for workers (although not necessarily key-workers, see further comment at 13.2.12 below) who meet the pre-determined criteria set out in the burden), and in the event of disposal to a subsequent purchaser who does not meet the worker criteria, an overage payment would be due to the party entitled to enforce. The right of the owner to lease the house to a third party would also be restricted.
- 13.2.12 While it is reasonably clear that, in the case of Healthcare Burdens, given the definition of "*facilities for healthcare*", there is potential for Healthcare Burdens to be used to achieve the long-term availability of housing for health care key workers (noting that Healthcare Burdens can only be created in favour of health boards and the Scottish Ministers), it is less clear whether EDBs could be used to achieve the long-term availability of housing for key workers. The purpose of an EDB must be to "promote economic development". Unfortunately, this expression is not defined in the legislation or the explanatory notes. Institutional writers Gretton and Reid refer to EDBs as being "a rather vague notion which will no doubt be tested in the courts" and also "intriguing and mysterious"...
- 13.2.13 Our (caveated) proposition is that EDBs could be used to restrict the use of burdened land to the provision of housing for workers employed to work on a specific site ("the employment land") which is deemed to comprise an economic development. This is an extension of the rationale applied to Healthcare Burdens where accommodation for staff employed to provide health care is ancillary to the provision of health care. In our view,

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<sup>58</sup> s. 45 (3) Title Conditions (Scotland) Act 2003 provides that an economic development burden may comprise an obligation to pay a sum of money (the sum or the method of determining it being specified in the constitutive deed) to the local authority or the Scottish Ministers as the case may be.



accommodation for staff employed to work as workers on employment land is ancillary to economic development. A strong link between the housing land burdened with the EDB and relevant employment site could be established if the employment site was also subject to an EDB. Given that the development on the employment land would need to be deemed to be an economic development to be burdened with the EDB, we think that a straightforward reading of the legislation would require economic activity to be undertaken on the employment land as its principal use which could preclude some traditional key-worker industries such as health care and education. In addition, given the existence of Healthcare Burdens, our assumption is that the legislative intention was that these would be the route used to deliver housing associated with healthcare delivery rather than EDBs.

- 13.2.14 We have not been able to identify anything definitive to support the idea that EDBs could be used to support the retention of key worker housing. A review of the limited case law and legal commentary available indicates some points in favour, but also some against. In our view, a Council looking to rely on EDBs to support the delivery of key worker housing would need to be comfortable that a burden requiring land to be used for housing for key workers would in fact promote (or at least be conducive to) economic development long-term and have reasonable evidence for this taking account of the specific circumstances, and that economic development would in reality be a "material and important" purpose of the burden, and/or a main intention of the parties.
- 13.2.15 Following our proposition above at 13.2.13, EDBs, when validly created and registered against the title to the affected land will bind successor owners to their terms and therefore could be effective in securing the long-term availability of housing for key workers employed on employment land.
- 13.2.16 **Rural Housing Burdens ("RHBs")** are personal real burdens over rural land<sup>59</sup> which incorporate a right of pre-emption in favour of a rural housing body<sup>60</sup>. The meaning of "rural land" is very broad – notwithstanding the name, it is possible to create RHBs on urban land subject to there being an appropriate rural housing body agreeing to accept the right to enforce. The

<sup>59</sup> "Rural land" means land other than excluded land ("excluded land" having the same meaning as in Part 2 of the Land Reform (Scotland) Act 2003 (asp 2)). The definition of "excluded land" is narrow, therefore "rural land" applies to rural but also urban land.

<sup>60</sup> s. 43(1) Title Conditions (Scotland) Act 2003

Scottish Ministers have prescribed a list of rural housing bodies<sup>61</sup> who can benefit from the right to enforce RHBs.

- 13.2.17 As with Healthcare Burdens, it is possible for RHBs to be created other than by the benefitting rural housing body entitled to enforce it, provided that the consent<sup>62</sup> of that body to the creation of the burden in its favour is obtained. This means that RHBs can be created on sites owned by the JV rather than a rural housing body.
- 13.2.18 The effect of creation of an RHB is that prior to each disposal of a burdened house, the nominated rural housing body would have the opportunity to buy the property prior to it being sold on the open market<sup>63</sup> in exchange for a consideration calculated with reference to criteria set out in the RHB constitutive deed. On exercising its pre-emption, the rural housing body could then sell the house to a third party who meets the key worker criteria.
- 13.2.19 RHBs would be a relatively expensive mechanism for the preservation of housing for key workers as the rural housing body would need to hold funds to exercise the pre-emption right (including purchase price, Land and Buildings Transaction Tax<sup>64</sup> and legal costs) – however this could be managed by way of a back to back disposal to a third party purchaser chosen by the rural housing body (this would be subject to the timescales involved in the operation of the pre-emption), facilitated by the rural housing body maintaining a waiting list of prospective purchasers who meet the allocation criteria.
- 13.2.20 Unlike with most pre-emption rights, where the property is offered back only on the first occasion on which it is sold, RHBs are not extinguished for future disposals, so can secure the availability of the housing on a long-term basis.
- 13.2.21 **Pre-emption burdens:** For scenarios where there is benefitted property available (for example, where the JV was developing part of a larger, mixed tenure development site where a portion would be retained for social rent) a more straightforward **pre-emption burden** would be available. Similar to the RHB pre-emption, a pre-emption burden would require the first purchaser of each home to make an offer to the JV entitling

<sup>61</sup> Title Conditions (Scotland) Act 2003 (Rural Housing Bodies) Order 2004/477. The list includes Argyll Community Housing Association. The list also includes some registered social landlords.

<sup>62</sup> Consent to be narrated within the constitutive deed.

<sup>63</sup> This is unlike pre-emption real burdens discussed at paragraph 13.2.20 below, which expire if not exercised at the first opportunity arising.

<sup>64</sup> Land and Buildings Transaction Tax is payable by the purchaser of property although, there may be mitigations available, for example Charities Relief where the RHB meets Revenue Scotland's charity criteria.

it to buy back the home. This could be at a pre-determined fixed price (which could also be subject to increases for inflation). There would be no requirement for a rural housing body to be involved. However, a pre-emption burden would only be capable of exercise once – if the JV as the party with the right to receive the offer to purchase declined to exercise it (or otherwise waived the option) then the pre-emption right would be lost forever<sup>65</sup>. If however the pre-emption was exercised, the party exercising it would be able to impose a fresh pre-emption burden on the title to the home on its subsequent disposal. The pre-emption burden would also only be available to the JV for as long as the JV holds the ownership of the benefitted property.

- 13.2.22 **s.75 Agreements**<sup>66</sup> also offer a mechanism by which the use of land could be restricted to key worker accommodation and occupation of each house as a principal residence. In terms of s75(1) "A person may in respect of land in the district of a planning authority (a) by agreement with that authority, or (b) unilaterally, enter into an obligation restricting or regulating the development or use of land".
- 13.2.23 S.75 obligations restricting the use of land to housing for key workers could either be imposed by the JV directly, or by the planning authority.
- 13.2.24 In the former scenario, the JV would put forward a planning application which would specify that all or part of the development will deliver housing for identified key workers (or another special category of occupier class). Any grant of consent would be supported by a planning obligation/s.75 agreement which would restrict the use of the specified units to key worker accommodation and as owners' principal residences, and those restrictions would be tied to the land and therefore bind successor owners.
- 13.2.25 Often the s. 75 agreement will require the affordable housing to be provided as accommodation for social rent and transferred to a local authority or RSL as that tenure. However, there is not a requirement for the drafting to specify a specific tenure, and it is not unusual for the s. 75 agreement to simply require "an affordable housing scheme" to be submitted as part of the first application for approval of matters specified in conditions with the specific affordable tenures being identified at this stage, which would be when the key-worker criterion would be incorporated. In

<sup>65</sup> This is different to RHB pre-emption rights, which continue to apply notwithstanding the right may not be exercised by the rural housing body entitled to enforce.

<sup>66</sup> Being Section 75 of the consolidated Town and Country Planning (Scotland) Act 1997 as amended in 2006 and came into force in February 2011

the latter scenario, the planning authority would impose a planning obligation on the JV to deliver the housing as part of the larger development for which planning permission is sought. Where the local planning authority has identified housing targeted at key workers (or another special category of occupier class) as affordable housing in terms of its affordable housing policy, the housing will be deliverable in terms of the 25% minimum affordable unit requirement applying to any new residential developments in terms of NPF4 (a higher or lower percentage can be justified at local level).

- 13.2.26 In each case, the planning obligation would prescribe a percentage discount to be applied to the price payable on sale and secure the long-term availability of the housing at this discounted price for key workers by prescribing criteria which apply to permitted (or qualifying) purchasers entitled to benefit from the discount. Each prospective purchaser (including second and subsequent purchasers) would be referred by the seller (whether the first seller or subsequent owners) to the Council for consideration against the criteria. Sales to prospective purchasers who are assessed as meeting the criteria will be referred to the then seller to proceed with the sale. In the event that there are no purchasers in the market who meet the criteria, the s.75 Agreement can provide for alternative permitted disposal (e.g., to a Council or an RSL), and finally can permit sale on the open market (usually subject to an overage payment to mitigate any windfall received by the seller against the restricted price paid)<sup>67</sup>.
- 13.2.27 Although s. 75 Agreements are open to variation after the grant of the associated planning permission, variations to the provisions dealing with the delivery of housing are not generally challenged. Where the planning application is made on the basis that the development will be for a specific type of housing, the principle of the development is founded on the mix of housing to be delivered so there will be very limited grounds for challenge on the basis of the restriction of the use of the land for a specific type of housing. Where a planning obligation is imposed by the planning authority requiring the delivery of affordable housing (and assuming that the Council's planning policy incorporates key worker housing within its affordable housing policy) as a percentage of the overall development, the percentage will be supported by national/local policy and will usually have

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<sup>67</sup> Note that where the planning authority has identified housing targeted at key workers (or another special category of occupier class) as affordable housing, in terms of NPF4 Policy 16(F) a planning application for a proposed development of new homes on land not allocated for housing in the Local Development Plan will be supported provided the proposal is for less than 50 units.

been factored into the developer's cost analysis and therefore will generally not be subject to challenge.

- 13.2.28 If the Council wanted to convert housing which was delivered in terms of the s.75 agreement from affordable housing to market housing, the s.75 agreement will usually incorporate a clause which allows an affordable house to be sold as market housing if there is no demand from the identified group of priority purchasers, and the Council does not want to purchase itself. The developer will be obliged to pay a commuted sum in lieu of providing the house for affordable housing and sell it at market value. This would also apply to subsequent proprietors. If a landowner wanted to remove the obligation, they would apply to the Council to vary it either by agreement or under a s75A application. Where the house has been transferred to the Council, technically the Council could not vary the s. 75 agreement as it could not enter into an agreement with itself, they would simply stop enforcing the s. 75 agreement. However, where the Council has acquired the house from a developer at affordable housing value, it would likely need to pay to the developer an uplift on the price reflecting the difference between the affordable and market values.
- 13.2.29 **Contractually**, the occupation of housing by people meeting key-worker criteria and who also satisfy the requirement to occupy the housing as their principal residence could be secured at the point of disposal, by way of a personal contract between the JV and purchaser, backed by a standard security<sup>68</sup>. This is the mechanism used to secure obligations in help to buy/new supply shared equity schemes.
- 13.2.30 Effectively, the JV would retain an equity interest in the property sold which would notionally reflect the difference between the open market value (i.e. without any occupancy restriction) and the value taking account of the restriction. In exchange of the JV's equity, the purchaser would undertake to perform particular obligations, which could include obligations restricting the onward sale of the house— generally by way of an option to buy back the property prior to open market disposal either for the seller or their nominee, being the obligations secured by the standard security mentioned above.

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<sup>68</sup> The Land Reform (Scotland) Act 1974 provides that the owner of secured property can receive a discharge of the standard security at year 20 provided that the balance of their loan, plus any interest and fees due, is paid. This is known as 'the 20 year security rule'. To mitigate this risk Scottish Ministers put in place legislation which removes this right in certain circumstances for certain named schemes (these include the New Supply Shared Equity Scheme, Help to Adapt and Help to Buy (Scotland)).

- 13.2.31 The registration of a standard security in favour of the JV would act as a "red flag" to any third-party purchaser considering purchasing the property that there are continuing obligations affecting the property to be considered. The security also prevents the property being sold without the consent of the JV who would need to sign a discharge of the standard security prior to completion of any disposal.
- 13.2.32 Usually, shared equity arrangements permit the purchaser to "tranche up" their equity interest, often up to 100% at which point the obligations due to the equity holder (including the standard security would be discharged). This can be avoided by use of the "golden share" mechanism whereby there would be a limit on the extent to which the purchaser can tranche up – usually up to 80% of open market value.
- 13.2.33 Another contractual mechanism would be the use of **personal pre-emption rights** ("PPERs"). PPERs are similar to pre-emption burdens and the pre-emption rights which form part of an RHB in that they will offer the original seller of homes the option to buy-back housing prior to disposal on the open market. The differences are that PPERs are contractual in nature between the original seller and purchaser and therefore the right to enforce PPERs could not be transferred to a third party. Unlike pre-emption burdens, PPERs do not require a benefitted property to be enforceable and therefore offer a helpful alternative where the housing site is not adjacent to other land owned by the party seeking to enforce the pre-emption. Unlike with RHBs, there is no limit on the type of party who can enforce the pre-emption, i.e., there is no requirement for a rural housing body to be involved. The obligation to offer the PPER to the party entitled to receive it could be secured by a standard security, however the security itself will only be enforceable for a period of 20 years<sup>69</sup>, creating a practical timescale for the enforceability of the PPER.
- 13.2.34 Title conditions and s.75 agreements could both be very effective mechanisms for securing the availability of housing for purchasers who meet specific criteria in the long term. These mechanisms also, in theory, offer a means of enforcing conditions during occupation, although it would generally be relatively resource intensive to monitor the changing circumstances of occupiers during the period of occupation. It is generally

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<sup>69</sup> As noted above, in terms of the Land Reform (Scotland) Act 1974, at year 20 year the homeowner would be entitled to receive a discharge of the standard security provided that they have performed the secured obligations, being in this case to offer the pre-emption. If the pre-emption wasn't exercised at this point, the standard security would be discharged.

accepted practice that it is only on change of occupier that criteria are applied<sup>70</sup>.

- 13.3 **What protocols would need to be put in place to ensure that the Programme adopts a prioritised approach to site selection to ensure a wellbeing-led approach?**
- 13.3.1 The Programme would need to establish clear site outcomes which would deliver the wellbeing-led outcomes it seeks to achieve. Criteria establishing the delivery of each outcome would need to be developed and adopted by the programme, together with a scoring mechanism and go/no-go scoring thresholds. Each potential site would then need to be assessed against those criteria to establish the extent to which development would deliver the outcomes sought, a score awarded and based on that score, a decision to proceed or not taken. In general, it would be preferable to develop those sites with the most pronounced impact on wellbeing (of the area, or persons within it) first.
- 13.4 **Does the new stock created by the JV, and subsequently sold, need to meet the quality standards of development that would be required by a Council if it was developing new homes for social rent?**
- 13.4.1 If the JV is to make houses available for social rent, the JV will need to be a registered social landlord.
- 13.4.2 Section 31 of the 2010 Act requires registered social landlords to aim to meet the standards and outcomes contained within the Scottish Social Housing Charter ("SSHC") in the performance of housing activities, including the Scottish Housing Quality Standard ("SHQS"). They are subject to the oversight of the SHR in relation to their attainment of those standards and outcomes. We consider that the SHR would generally expect new build homes for social rent to attain the SHQS at the point at which they were being made available to tenants. While we do not anticipate that failure to meet the SHQS would result in immediate intervention (there are many properties that do not currently meet the standard), we would anticipate that the SHR would expect, at least, for there to be plan for the SHQS to be met.
- 13.4.3 For affordable or open market value houses, there would be no obligation to align construction standards with the SHQS. That said, as a risk

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<sup>70</sup> Scenarios could conceivably arise whereby a house is owned by 2 individuals, one of whom met the criteria at the point of purchase and that person dies and a third party who does not meet the criteria succeeds to the ownership interest, or otherwise ceases to be in occupation leaving an occupier who does not meet the criteria. In these scenarios, the party entitled to enforce would want the option to recover possession by way of enforcement action, although may not do so for policy reasons.

mitigation matter, to enable the properties to be readily sold to a social landlord or operated as social housing by the Council, in the event that open market sale turned out not to be possible, the JV may wish to consider whether to align with that standard from the outset rather than to look to redesign at a later date.

**13.5 Is the justification for Community Wealth Building a sufficiently strong rationale (on its own and/or aligned with other rationale) for use of the wellbeing power and use of a CBRS approach?**

- 13.5.1 A Council has power to do anything which it considers is likely to promote or improve the well-being of its area and persons within that area. There must be a clear link between what is done under the section 20 power and the resultant impact on wellbeing.
- 13.5.2 We note from the case study that the community wealth building ("CWB") approach would build market capacity in the small and medium enterprise ("SME") contractor base and delivers "recognised construction skills/qualifications for local people". We would have some hesitation about placing excessive weight on the CWB approach in relation to the section 20 power if the likely benefits are restricted to those referred to in the case study. We say this because: (i) it is not immediately clear that building market capacity in the SME contractor base provides a benefit to the wellbeing of an area, or people within that area, and, even if it does provide such a benefit, the link between the exercise of the section 20 power and the result is not necessarily clear or direct. Even taking the SME aspect together with the anticipated development of skills and qualifications for local people (in respect of which we are satisfied that a link could exist between exercise of the section 20 power and benefit to the wellbeing of people within the area), we would have concerns as to proportionality. We consider the Council would need persuasive evidence of significant benefit to be satisfied, in terms of its best value obligations in particular, that it was appropriate to commit the significant resource needed to implement the project proposal.
- 13.5.3 That said, the CWB approach is not irrelevant. We consider pursuit of CWB outcomes can play a supporting role in the case for use of the section 20 power, supporting what we consider to be the more obvious and compelling principal purpose underlying the use of the power in this case study – that of providing sufficient housing of varying tenure to meet the demands of the local area. We consider this purpose more clearly draws a link between the Council's exercise of its section 20 power and benefit to the wellbeing of area and people within it.



13.6 **Given the intended cross-subsidy approach, does the JV, and its profit -sharing agreement, need to include any specific criteria in order to meet the test for the use of the wellbeing power?**

- 13.6.1 As the section 20 power is being used to promote wellbeing by ensuring a sufficient housing mix, this is consistent with the scope of the power. It is important to structure this as being about the need for market rate housing and a housing mix – it would not, for example, be competent for the Council to use the section 20 power to develop market rate housing *purely* in order to cross-subsidise MMR and social housing (per *Brent*), but we note that the Council has identified insufficient open market value housing stock, and the development of mixed-tenure communities could also be independently justified and would not preclude the cross-subsidy.
- 13.6.2 Put another way, if the Council's objective is to ensure an appropriate mix of tenures in a given area, then it may use section 20 to develop properties with a range of tenures for that purpose. If the arrangements for the financial management of that development scheme happen to involve cross-subsidy between one tenure type and another, that would not adversely affect the Council's ability to rely on the section 20 power to achieve the housing mix sought. The more distinct (whether geographically or in terms of management etc) the market rate housing development is from the MMR and social housing being cross-subsidised is located, the more difficult it is likely to be to justify the market rate housing by reference to such a desire for a housing mix.
- 13.6.3 That leads on to a separate question of whether the JV enjoys any profits at all or surpluses from one tenure type are diverted in their entirety to support another tenure type. We note that the JV will have a profit- sharing mechanism at both programme and individual site level. This is likely to mitigate against a risk that a JV partner would find the profits at programme level insufficient if cross-subsidy is required.

13.7 **Does the intended disposal of the rented stock at the end of the Programme conflict with subsidy controls if the Council has funded a gap in the capital cost of one, or more, specific sites?**

- 13.7.1 Whether or not a subsidy arises in respect of any particular disposal vis-à-vis the acquirer will depend on whether the acquirer receives an advantage and not on whether the Council has incurred a loss (for example by gap funding the capital cost of a site). We assume that the disposals will take place at market rate. If the acquirer pays the price for a site or sites that it would expect to pay if the site(s) were owned by a private owner, then no subsidy will arise.

- 13.7.2 However, a subsidy may arise *in respect of the JV and/or JV partner* if the Council provides gap funding. This will arise at the time of the provision of that funding rather than at the time of disposal. If the Council contributes gap funding, then this, like any other investment from the Council, will need to be justified on a "market economy operator" basis if a subsidy is not to arise. That will require the Council to receive the sort of returns on that investment that a private sector investor would expect to achieve, for example to receive an appropriate amount of equity in the JV in exchange for its investment. Generally, this will be met provided that the Council and a JV partner invest on *pari passu* terms. However, where gap funding is required, this will require either (i) additional equity in return or (ii) repayment on commercial terms, or a subsidy will arise.
- 13.7.3 We would note, though, that there is not necessarily a problem if a subsidy does arise. Under the Subsidy Control Act 2022 it is now easier to design a lawful subsidy provided that certain conditions are met and certain considerations are taken into account. That may be a particularly useful route to explore where the Council considers that gap funding is required for individual projects.
- 13.7.4 For the avoidance of doubt, no subsidy can arise in the context of a disposal of residential property to an owner-occupier irrespective of the level of any discount or financial support offered. Subsidy control rules arise only in relation to financial assistance to entities which are active on a market (they may therefore arise in respect of a disposal to a person who is purchasing a property for the purposes of renting it out to a third-party tenant).
- 13.8 **What market failure rationale(s) for public sector intervention can be applied to the project across the various elements – tenure, market sector, location etc?**
- 13.8.1 The Best Value Guidance issued by the Scottish Government under section 2(1)(a) of the 2003 Act, to which Councils must have regard when exercising the section 20 power (and any other power) requires them to work in partnership with "a wide range of national, regional and local agencies and interests across the public, third and private sectors". A Council should be able to demonstrate "how its partnership arrangements lead to the achievement of best value". The requirement in the Guidance for a Council to make best use of its financial and other resources, and to work with partners to maximise the use of their respective resources, should be read in this context.

- 13.8.2 We consider the implication of section 1 of the 2003 Act, read alongside the Best Value Guidance, to be that the Council should carefully consider, in circumstances in which it is engaging in an activity which may displace the private sector (particularly local businesses), whether doing so is reasonable, proportionate, and consistent with its best value obligations. That will involve the Council satisfying itself: (i) what the relevant market(s) in which it seeks to intervene are, and (ii) the reasons for a lack of private activity in those markets.
- 13.8.3 In this case, we note from the case study that there is private sector interest in building market value housing in more accessible locations, but insufficient delivery of affordable / mid-market / and remote rural housing stock. We also note that there is insufficient delivery of open market value housing for rent across the whole area.
- 13.8.4 It will be essential for the Council to understand, where the market is not providing housing of certain types and tenure, why this is the case. If for example, obtaining planning permission was the source of the difficulty, then that would not represent, in our view, an obvious example of market failure. On the other hand and by way of example, if the reason for the lack of interest in developing affordable / mid-market / and remote rural housing stock is that a commercially unattractive level of profit stands to be made at the point of sale, the Council could, in our view, conclude that there was a market failure (assuming the Council was satisfied, on the basis of evidence, that there was demand for housing of this type). As discussed elsewhere in this note we consider analysis carried out by a specialist in respect of the local market would likely be necessary in order for the Council to arrive at this conclusion. If the Council is imposing, for example, a 'gold standard' in relation to new build through the planning system, it should seek to understand whether private sector delivery would be viable if a lesser, (but nonetheless lawful) standard was required.<sup>71</sup> Otherwise, the question may arise as to whether the market is not failing to deliver housing of the type the Council considers is required, but rather homes that meet the Council's standards, which will carry different considerations as to the Council's justification for intervention.
- 13.8.5 Perhaps the more difficult issue, is the apparent intention is for the JV to engage in development in the accessible locations in which private sector developers are interested. In this respect, we consider the Council will

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<sup>71</sup> This is only an example of the kind of feedback that may be received and, if so, taken account of by the Council (alongside all other relevant factors).

need to tread carefully. We assess the risk of private sector challenge is (in comparison to other case studies) higher because the Council (via the JV) would be engaging in activity which had the potential to displace the private sector.

**13.9 What are the requirements for local stakeholder engagement to demonstrate support for the Programme and for individual site proposals from local stakeholders (people, businesses, other organisations)?**

13.9.1 Given: (i) the proposed ten-year period lifetime of the project proposal, (ii) the intention that the project proposal should extend across multiple islands and (iii) the fact that sites are yet to be identified for use in connection with the project proposal, we recommend a staged approach to consultation in this instance. That would involve: (i) consulting first on general scheme ("stage 1 consultation") and (ii) further consultation when project proposals in respect of particular sites are at a more concrete stage ("stage 2 consultation").

13.9.2 The consultation process should be completed prior to the Council taking a decision to commence the project proposal (e.g., prior to deciding that it will seek a JV partner). That does not mean preparatory work cannot be undertaken, but any such work should not treat as a foregone conclusion that the project proposal will be implemented, at all, or in the fashion currently anticipated. Similarly, the stage 2 consultation process should be carried out before any commitments are made to development on particular sites.

13.9.3 The following general principles apply at each stage, although it may be that results from the stage 1 consultation mean the extent of further consultation at stage 2 is reduced:

13.9.3.1 At a minimum we consider that the Council should be consulting with private sector housebuilders and community planning partners. We also consider consultation should be carried out with communities on all identified islands – that may involve working with community councils or other local groups, as well as convening engagement events (e.g., 'town hall' meetings).

13.9.3.2 The Council should produce a consultation document which sets out the proposals in a reasonable degree of detail, and the rationale for them. It should also set out what (if any) alternatives have been considered and discounted. The consultation document (as well any events or other mediums) should seek to obtain information which will help the Council to

assess the extent of unmet demand for housing of the various tenures proposed in the area. It would be desirable for the consultation process to align with the obtaining of specialist consultant support. That may involve the specialist consultant engaging with housebuilders to understand their lack of interest in development, and the reasons for this, in line with what we say about best value, above at 13.8.

- 13.9.3.3 Responses should be collated and conscientiously considered by the Council. The Council should be open minded to adjusting the proposals in light of consultation responses (including, if appropriate, by making significant changes to the proposals). While it will always be a matter of fact and degree, if a Council adjusts its proposals significantly in light of consultation responses, it will wish to consider whether a further round of consultation is needed.
- 13.9.3.4 Any consultation exercise takes time and requires resource. It can though deliver significant benefit. As well as providing an evidence base, consultation can also demonstrate public support for project proposals. We consider that Councils are entitled to have regard to demonstrated local support when considering whether, and how, to use their section 20 power.
- 13.9.3.5 The Council needs to have regard to the Public Sector Equality Duty, the Fairer Scotland Duty, and other overarching obligations. We recommend that the Council carries out impact assessments in respect of these overarching obligations prior to consultation and invites representations on the assessed impacts as part of the consultation. Impact assessments should be updated as required in light of consultation responses.
- 13.9.3.6 We think a Fairer Scotland Impact Assessment, in particular, has the potential to be a source of assistance to a Council in the context of this case study, if it can demonstrate that adopting the proposal would contribute to reducing inequalities of outcome caused by socio-economic disadvantage.
- 13.9.4 In addition, the Council should consider, in respect of the general scheme, whether an island communities impact assessment ("ICIA") is required in terms of the Islands (Scotland) Act 2018. If it concludes that an ICIA is required, we recommend that the stage 1 consultation seeks information required to inform the ICIA.

- 13.10 **Does the proposed route to procure the JV partner, and the JVs subsequent procurement of its consultant/ contractor team, meet procurement rules? Are there any additional requirements associated with the use of the wellbeing power that need to be considered?**

13.10.1 The case study only advises that the JV partner and its own contractors will be procured on an open-market, procurement compliant basis. Assuming that both the JV partner and contractors are procured following appropriate competitive procedures under the Public Contracts (Scotland) Regulations, the fact that the Council is proposing to use powers under section 20 of the 2003 Act does not imply additional procurement considerations.

**13.11 What challenge – who/ what/ why – might occur from housebuilders that are active in the more accessible parts of the Council's area?**

13.11.1 We identified the risk of challenge from private sector housebuilders in section 13.8.5 above. The likely basis for any challenge would be that the JV was interfering in the market in respect of accessible locations in which private sector developers were interested.

13.11.2 Legally, we suspect any challenge is likely to be advanced against the Council, rather than the JV itself. We say this because, based upon the case study (and upon the fact that the JV partner is to be procured) it appears the Council is to retain control over the project proposal as a whole, rather than leaving this to the JV itself.

13.11.3 Possible grounds of challenge include:

13.11.3.1 That the Council had failed to pay sufficient regard to the Best Value Guidance issued by the Scottish Government under section 2(1)(a) of the 2003 Act, insofar as it concluded that it was entitled to commission the JV to develop properties in the accessible areas.

13.11.3.2 That the Council had erred in law to the extent it had concluded that section 20 of the 2003 Act permitted it to commission the JV to develop properties in the accessible areas.

13.11.3.3 That the Council had acted unreasonably in concluding that it was entitled to commission the JV to develop properties in the accessible areas.

13.11.4 These grounds of challenge may be advanced alongside other more general challenges relating to, for example, the consultation carried out by the Council, or the ICIA or other impact assessments produced in connection with the project proposal. Specific challenges might also be brought by a challenger in relation to procurement or subsidy – each of these would concern both the Council and the JV.

13.11.5 A challenge may also come from other quarters. In particular, actions that could be viewed as local authority trading, without approval from the Scottish Ministers as required under the 1970 Act, may invite a challenge from the Scottish Government, in particular if it was concerned about Councils competing with private housing developers. This is unlikely to take the form of a legal action against the Council, at least in the first instance, but that cannot be ruled out.

**13.12 What is the view of the robustness of a condition contained within a section 75 Agreement that purports to restrict occupancy of residential accommodation to “primary occupancy” where primary occupancy is not something that is referred to in the Council's affordable housing policy and is not referred to elsewhere in housing policy contained within the Local Development Plan or in Supplementary Planning Guidance (SPG)?**

13.12.1 SPG is guidance developed by planning authorities that offers more detailed guidance and expands upon existing policies and proposals contained in the LDP. SPG is a material consideration when planning applications are being determined and when Section 75 Agreements are being drawn up.

13.12.2 We consider that in the circumstances described, there would be no clear planning justification for the inclusion of such a condition in a section 75 agreement and that the condition could not reasonably be insisted upon by the Council.

13.12.3 We are also of the view that it would not be appropriate to refer to occupancy restrictions of this nature within a Council's affordable housing policy as there is no correlation between the nature of the occupancy and the affordability of residential accommodation. We understand that the Council is of the same view. However, provided a reasonable case can be made out for the need for such a policy it may be appropriate to include it in other housing policy that is contained within an LDP or within SPG. We would expect any such case to be underpinned by the Council's Local Housing Strategy and HNDA.

13.12.4 We understand that the Council's LDP2, which has been subject to examination but has yet to be adopted, does not include any such policy. However, there is nothing to preclude the Council from developing SPG at this time subject to appropriate consultation.

- 13.12.5 In relation to housing supply NPF4 recognises that "*There is a clear need for affordable housing provision across the region to improve choice and access to homes, to support local economies, and in some areas to help offset the impact of second home ownership and short term lets on the market. Local solutions may include key worker housing, temporary homes for workers in remote areas, and self-provided homes including self-build and custom-build*" (the region in this case being the North West Coast and Islands - which includes the Council's area).
- 13.12.6 NPF4 also states that "*Demand for development, including in pressured areas, will require a planned response to minimise the impact of second homes on local communities and ensure new homes are affordable and meet local needs*"
- 13.12.7 The emphasis within NPF4 is very much on local solutions to address local issues which ought to be of assistance to the Council should it consider the introduction of SPG as discussed above. This is, of course, subject to the case being made out that such SPG is appropriate. The availability of SPG that supports the restriction of occupancy in the manner suggested by the Council will strengthen its position in relation to the negotiation of future section 75 Agreements and will help ensure that planning obligations are robust (subject, of course, to any planning obligations properly reflecting the terms of the SPG).

## 14 ADDITIONAL QUESTIONS FROM LOCAL AUTHORITY REGARDING SPECIFIC PROPOSAL

### 14.1 Best value analysis

- 14.1.1 The Best Value Guidance issued by the Scottish Government under section 2(1)(a) of the 2003 Act, to which Councils must have regard when exercising the section 20 power (and any other power) requires them to work in partnership with "a wide range of national, regional and local agencies and interests across the public, third and private sectors". A Council should be able to demonstrate "how its partnership arrangements lead to the achievement of best value". The requirement in the Guidance for a Council to make best use of its financial and other resources, and to



work with partners to maximise the use of their respective resources, should be read in this context.

- 14.1.2 We consider the implication of section 1 of the 2003 Act, read alongside the Best Value Guidance, to be that the Council should carefully consider, in circumstances in which it is engaging in an activity which may displace the private sector (particularly local businesses), whether doing so is reasonable, proportionate and consistent with its best value obligations. In order to do that it will be necessary for the Council to establish what the relevant market(s) in which it seeks to intervene are, and the reasons for a lack of private activity in those markets. That repeated attempts to dispose of the property at [X Street] have been unsuccessful would tend to suggest that the private sector is not interested its redevelopment. However, that does not mean the market is failing. For example, if there would not be demand from within the population to live at [X Street] even after redevelopment, this may be an example of the market operating appropriately. As discussed, elsewhere in this note, we consider analysis carried out by a specialist in respect of the local market would be necessary in order for the Council to properly address this point. That specialist analysis should be incorporated into the Council's best value consideration.
- 14.1.3 We are asked how often this analysis would need to be refreshed. Unless circumstances change, or the project takes a particularly long time, we would not expect this specialist analysis to be refreshed during the lifetime of the project.
- 14.1.4 There are no bright line rules in terms of best value and a differential between investment and financial return. Best value  $\neq$  most money.
- 14.1.5 Before seeking to exercise the section 20 power, the Council should obtain a reliable body of evidence, and analysis, which outlines benefits arising from the works. We would expect that the specialist providing market analysis could assist in also building this evidence base. If the evidence suggests that the works at [X Street] would be likely to e.g., stimulate private sector investment in surrounding properties, or create employment opportunities, we consider these are matters the Council could properly consider in its best value analysis.
- 14.1.6 We understand a very significant loss is likely to be incurred to the Council by implementing the project proposal. A question arises whether, if that is so, the Council can, consistent with its best value obligations, lawfully use

the section 20 power. While we do not exclude a lawful application of the section 20 power in such circumstances, we consider the Council would wish to be satisfied of likely substantial, direct benefit(s) to the area or people within it before exercising the power, and to record carefully why it considered use of the section 20 power was appropriate, notwithstanding the likelihood of a very significant loss being incurred.

- 14.1.7 A factor that may be relevant to whether exercise of the section 20 power is appropriate is the Council's discharge of its statutory duties. If it is not currently fulfilling its statutory duties (in particular in the area of housing – e.g., homelessness obligations), or is doing so inadequately, we consider it would be more difficult for the Council to be satisfied that it was appropriate to exercise its section 20 powers in the manner contemplated, in the knowledge of the likelihood of a very significant loss.
- 14.1.8 That said, we expect a court would be reasonably deferential to the Council as to what was (or was not) proportionate, so long as the Council could demonstrate it had carefully considered the competing considerations.
- 14.1.9 Where a Council is able to show that implementation of the project proposal would not only benefit the wellbeing of the local area and/or persons within it but also that the project proposal was in line with national, regional or local policy commitments, it will be better placed to counter any argument that the likely financial loss means that the section 20 power cannot be lawfully used.
- 14.1.10 The Council should record carefully why it considers use of the section 20 power is appropriate (assuming it considers use of the power is appropriate).

## 14.2 Consulting with neighbouring landowners

- 14.2.1 We do not have all the details of the specific site, and why agreements with adjacent landowners are thought to be necessary – this may arise from the build model selected.
- 14.2.2 However, while early discussions with adjacent landowners may be valuable in order to gauge their appetite to work with the Council, we do not recommend that Council enters into any binding, unqualified commitment with landowners prior to running a consultation process.

14.2.3 In practical terms, doing so may leave the Council bound to do or not do something (including make payment) even if the works at [X Street] do not proceed in light of consultation responses. In legal terms, entering binding agreements prior to consultation risks giving the appearance that the Council has pre-judged the conclusion of the consultation. That exposes the Council to legal risk.

### 14.3 Subsidy

14.3.1 Whether or not a subsidy arises in respect of any particular disposal vis-à-vis the acquirer will depend on whether the acquirer receives an advantage and not on whether the Council has incurred a loss in developing the site. We assume that any disposal to an enterprise will take place at market rate. If the acquirer pays the price for a property or group of properties that it would pay if those were owned by a private owner, then no subsidy will arise notwithstanding that the Council has spent more money than it has recouped. However, we would also note that if the Council anticipates incurring a loss, this should be fed into its best value assessment from an early stage.

14.3.2 There is no requirement to sell to private individuals. The Council's best value duty would additionally weigh against prioritising private individuals as buyers over enterprises – that would require to be justified by reference to other objectives.