

Sales of Scottish New Towns' Commercial and Industrial Properties



This report has been prepared under Section 6 of the National Audit Act, 1983 for presentation to the House of Commons in accordance with Section 9 of the Act.

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National Audit Office
14 March 1997

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Scottish New Towns

Livingston

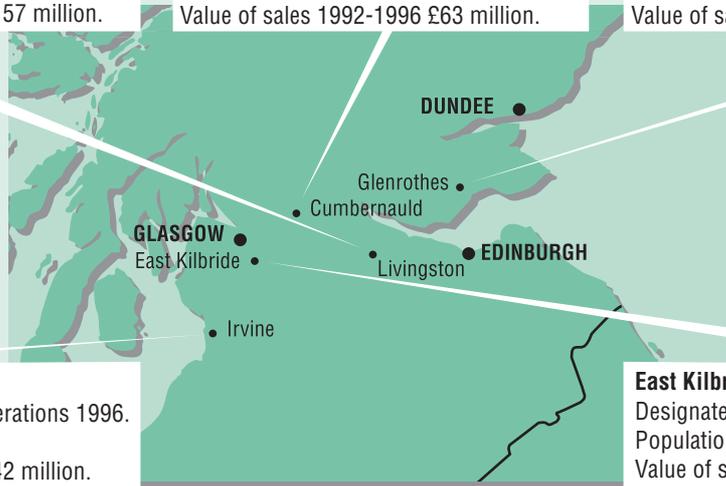
Designated 1962, ceased operations 1996.
Population in 1995 44,000.
Value of sales 1992-1996 £157 million.

Cumbernauld

Designated 1955, ceased operations 1996.
Population in 1995 52,000.
Value of sales 1992-1996 £63 million.

Glenrothes

Designated 1948, ceased operations 1995.
Population in 1995 40,000.
Value of sales 1992-1996 £47 million.



Irvine

Designated 1966 ceased operations 1996.
Population in 1995 56,000.
Value of sales 1992-1996 £42 million.

East Kilbride

Designated 1947 ceased operations 1995.
Population in 1995 72,000.
Value of sales 1992-1996 £111 million.

Scotland's five new towns - East Kilbride, Glenrothes, Cumbernauld, Livingston and Irvine - were established between 1947 and 1966. Originally the main objective in establishing the towns was to attract people and industry to the designated areas, usually away from more heavily populated areas in west central Scotland including Glasgow. Since the 1970s the towns' role has been to reinforce the Scottish economy by providing an environment in which industry could expand and flourish, to widen employment opportunities and sustain job growth, and to create fully developed and balanced communities.

At the start four towns each had a population of less than 3,000. All of the towns have grown substantially since. By 1995 almost 265,000 people lived in the five towns, some five per cent of Scotland's population.

The towns now accommodate a wide range of industries with total employment of some 116,000 people in 1995. In recent years they have attracted about 30 per cent of all jobs in Scotland arising from inwards investment from overseas and other parts of the UK. They have achieved this through investment in improved infrastructure, and the construction of new factory, warehouse and office and commercial premises for rent and for purchase. Some of the towns have also benefited from special planning powers and assisted area status providing access to regional selective assistance.

Most of the towns' investment was financed by borrowing from the National Loans Fund. In recent years the Corporations have applied an increasing share of disposal receipts together with repayment grant from the Scottish Office towards the early redemption of their outstanding debts, and have cleared all their indebtedness to the National Loans Fund.

Summary and conclusions

Introduction and scope of the National Audit Office examination (Part 1)

- 1 In 1989 the Government proposed the winding up of Scotland's five New Town Development Corporations - East Kilbride, Glenrothes, Cumbernauld, Livingston and Irvine. Following consultation, the Government made orders for the wind-up in 1992 and 1993; East Kilbride and Glenrothes Corporations ceased operations on 31 December 1995; and Cumbernauld, Livingston and Irvine Corporations did so on 31 December 1996 (paragraphs 1.1 to 1.5).
- 2 The Scottish Office Development Department and, before October 1995, the Scottish Office Industry Department (the Department) have been responsible for ensuring that the Corporations completed their wind-up on time. In 1992 they issued guidance to all Corporations including a requirement for them to dispose of their entire interest in all property assets. This has required a step change in the scale of disposals of commercial and industrial land and property assets compared to earlier years. At March 1992 these assets had a book value of £406 million. Sales, almost entirely to the private sector, are expected to total almost £420 million between April 1992 and the end of 1996 (paragraphs 1.6 to 1.7).
- 3 The National Audit Office sought confirmation that the Department and the Corporations had implemented these disposals in accordance with current professional practice and previous recommendations of the Committee of Public Accounts (Appendix 3). With assistance from Richard Ellis, property advisers, they examined the disposals programme in all five Corporations, including 37 sales totalling £176 million. This represented 53 per cent of the proceeds of all sales completed up to March 1996 (paragraphs 1.8 to 1.11).

Planning the sales (Part 2)

- 4 *Overall the Department and the Corporations planned the disposals to a high standard, and successfully implemented the programme without delay, though there was some scope for better preparation in one area, industrial building allowances.*
- 5 The Department provided a strong framework of guidance governing Corporations' management of disposals and established an expert advisory group to oversee the sales programme. The Department's sales guidance was consistent with earlier recommendations of the Committee of Public Accounts. Consistent with this guidance, Corporations implemented sale strategies based upon external professional analysis and advice, which was of good quality and soundly based (paragraphs 2.3 to 2.7).

Disposal strategy and guidance

- 6 The National Audit Office identified one area, industrial buildings allowances, where sales preparation might have been better. These allowances which can enable the purchaser of a property to offset liability to corporation or income tax, are likely to have attached to a significant proportion of the industrial properties sold by Corporations. The National Audit Office have estimated that utilisation of these allowances could give tax savings to purchasers of these properties up to a range of £12 million to £16 million though in practice actual tax savings are likely to be reduced by various factors (paragraphs 2.8 to 2.9).
- 7 Previous public sector experience had not established a need to consider industrial buildings allowances. The Department's sales guidance did not therefore deal with the allowances and, consistent with the Department's objective to dispose of the whole interest in property, Corporations proceeded on the basis of previous practice which allowed purchasers access to the allowances. However they adopted different approaches to marketing property where allowances were available. The National Audit Office found no evidence to show that the absence of consistent treatment reduced sale proceeds. However in their view it would have been advisable for all Corporations to have assessed the potential tax allowances available to purchasers prior to each sale and to have drawn attention in all cases to the allowances during marketing. This would have helped to ensure that intending purchasers had all relevant information about the potential tax savings before making bids, and would have contributed to the Corporations' responsibility to satisfy themselves that the terms for any disposal represented the best consideration reasonably obtainable (paragraphs 2.10 to 2.15).

Timing of sales

- 8 The Department's advisory group successfully minimised overlap in the marketing of major disposals by the five Corporations. Market conditions over the wind-up period have been mainly positive, as indicated by the level of market interest in the largest disposals, the prices achieved, and wider market trends (paragraphs 2.16 to 2.19).

Performance against sales and receipts targets

- 9 The Corporations have met or exceeded the key financial targets for the disposal programme, mainly concerning repayment of National Loan Fund debt. As a result Corporations have returned to the Exchequer £306 million of the £420 million total receipts generated between 1992 and December 1996. Corporations have secured the policy objective of total disengagement from the properties and completed the sales programme by the wind-up dates set by the Secretary of State, eliminating all outstanding debt (paragraph 2.20).

Sales implementation and outcome (Part 3)

- 10 *Generally in implementing the programme, and particularly for the larger competitive sales, the Corporations have conducted individual disposals skilfully and in line with previous Committee of Public Accounts recommendations. They can reasonably be expected to have maximised sales proceeds in most cases. However, there were some shortcomings, in particular weaknesses in pre-sale valuations, and in a few cases there were grounds to question whether the Corporations had achieved best price.*
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Method of sale

- 11 Sales of £164 million, (56 per cent by value of major sales completed to March 1996) followed competition and acceptance of the highest available offer (paragraph 3.4).
- 12 Of the remaining major sales in that period, £45 million (15 per cent) could not be sold by competition. This was either because leases provided tenants with pre-emptive rights to purchase (£25 million, 8 per cent) or as a result of the Government's policy to transfer selected key properties to Scottish Enterprise (£20 million, 7 per cent) (paragraph 3.4).
- 13 The remaining major sales worth £85 million (29 per cent) were also by negotiation; in these cases Corporations did not consider open market disposal appropriate. The National Audit Office examined 22 cases where there was no competition: in all cases there were reasonable grounds for not pursuing open market disposal often because the sale involved economic development benefits which competition would have jeopardised (paragraphs 3.3 to 3.5).

Marketing the properties

- 14 Overall marketing of the major package disposals was of a high standard with satisfactory results, and costs were controlled. In a few cases small price reductions resulted from clarification with purchasers of information made available to bidders during marketing (paragraphs 3.6 to 3.9).

Valuations

- 15 The Department required Corporations to record a formal valuation of assets before any disposal and to undertake revaluations where disposals became protracted or the market shifted significantly. Corporations obtained pre-sale valuations from their sales advisers for almost all sales (98 per cent by value) conducted on the open market, but much less often for other, negotiated sales (50 per cent by value). This was because Corporations considered that the District Valuers' previously supplied annual valuations of all their property for different accounts purposes often provided a sufficient alternative, when taken together with the knowledge and experience of their in-house professional staff. In nine of the 37 sales they examined the National Audit Office found benchmarks to be unavailable or weak because they did not anticipate the terms of the sale sufficiently (paragraphs 3.10 to 3.16).

Control over sales

- 16 In most cases Corporations had conducted sales satisfactorily, involving senior officials, Board members and where appropriate the Department's advisory group in key sales decisions. However the Department's disposals guidance did not extend to cases where Corporations were pursuing their long established

economic development role, which required them to strike a balance between encouraging development and maximising sales proceeds. The Corporations gave some concessions in six development sales which, while not unusual in such cases, should have been supported by explicit cost benefit analyses (paragraphs 3.17 to 3.22).

- 17 In December 1995 the Department issued supplementary guidance to Corporations on disposals. This emphasised the need for Corporations to prepare pre-sale valuations for all remaining disposals, including sales linked to Corporations' development activity (paragraph 3.23).

Clawback

- 18 Initially Corporations anticipated that purchasers would strongly resist the Department's requirement to apply clawback, and that this might have a potentially detrimental effect on sales. The Department clarified and expanded their guidance in 1993, and Corporations subsequently applied it successfully (paragraphs 3.24 to 3.27).

Sales prices and outcomes

- 19 For major sales completed between 1992 and 1996 proceeds at £293 million exceeded the aggregate estimated value of the properties, £280 million. In 32 of 37 cases the National Audit Office examined in detail Corporations achieved satisfactory or better prices compared with valuations and other criteria. Where Corporations sold properties below valuation, almost three-quarters of the sales were completed after competition, ie when Corporations would normally accept the highest offer after wide marketing (paragraphs 3.28 to 3.30).
- 20 In the remaining five cases the National Audit Office had doubts about the price achieved compared with pre-sale valuations and other criteria (paragraph 3.30).

Audit

- 21 The Department required internal audit coverage of the sales in each Corporation, but this did not happen in Cumbernauld and Livingston and coverage was insufficient in Irvine. The Department also required the external auditors of the Corporations to test whether disposals were undertaken in accordance with the Department's guidance and that sales prices represented best value for money within the context of that framework. External auditors have reported no significant shortcomings in this area (paragraphs 3.31 to 3.33).

Factors to consider for future disposals of public sector property assets

- 22 *Looking ahead to future public asset sales the National Audit Office highlight four issues which public bodies may wish to take into account (see below). In three areas these reinforce existing recommendations of the Committee of Public Accounts which are accepted by the Government. In a fourth area, concerning industrial buildings allowances, further research and consideration may be necessary to establish best practice for the public sector. This is an area about which the Committee have made no previous recommendations.*

Issues for future public property sales

Pre-sale preparation

- ◆ Effective marketing and sale of property requires presentation of reliable information to prospective purchasers. Such work may need to start six months or more before marketing can commence, if bodies are to be sure that they complete the necessary research and investigation into such matters as lease and tenancy details, the physical fabric of the property and the costs associated with its management.

Valuation and the role of professional advisers

- ◆ Up-to-date and appropriate valuations are essential prior to any sale, as the basis for the asking price and to benchmark offers received.
- ◆ If organisations obtain in-house valuation advice they have the right to expect that it achieves sufficient professional standards and is clearly documented. Where negotiated sales are necessary the availability of independent advice may provide an additional safeguard against possible criticism of the value achieved.

Conduct of sales

- ◆ Written guidance on the conduct of sales should be available which should reflect the need to provide assurance that sales guidance is complied with in practice, for example requiring internal auditors to report upon this aspect at specified intervals. Where there is a need to balance competing objectives, for example economic development and maximising sales proceeds, the guidance should set out the priorities to be followed.

Industrial buildings allowances

- ◆ Where significant taxation allowances exist in connection with properties to be sold, public bodies should consider the strategic implications early on, including the incentives to investment which these allowances represent.
- ◆ In determining their sales strategy public bodies should recognise that the transfer of industrial buildings allowances is likely to impact on the Exchequer through reduced taxation receipts. They should quantify in advance the potential allowances, obtaining professional advice as necessary. Where allowances are significant public bodies should examine the options for disposal including, where practical, options which allow the public sector to retain the relevant interest for the purpose of claiming any allowances. Because of some uncertainties associated with such options public bodies may need to consider new approaches to marketing the property, to enable them to quantify accurately the costs and benefits. This could include inviting purchasers to bid on the basis both of a freehold sale including transfer of the allowances and a long leasehold sale which withheld interest in the allowances and provided for the transfer of the freehold interest when the allowances expired. Public bodies would also need to balance any Exchequer benefits from retaining the relevant interest against any impact on the level and number of bids and on any wider objectives such as the benefits from the property continuing to be used for the qualifying activity for which the allowances were given.
- ◆ In all cases public bodies marketing property should ensure that: they publicise any allowances where the relevant interest might be transferred to purchasers; marketing information refers positively to the potential availability of allowances; they are prepared to provide supporting factual data to allow the extent of the allowances to be estimated accurately; and that their valuers have considered the potential impact of allowances.

Part 1: Introduction

The Scottish New Town Development Corporations

- 1 Scotland's five New Towns - East Kilbride, Glenrothes, Cumbernauld, Livingston and Irvine - were established between 1947 and 1966. Their main objectives have been to assist the dispersal of industry and population from over-crowded urban areas, and to provide locations for and promote new economic development. The Corporations were established with wide powers to acquire land, develop infrastructure and build housing and commercial and industrial premises. The Secretary of State for Scotland appointed the Boards of the Corporations.

Winding-up the Corporations

- 2 The New Towns (Scotland) Act 1968 provided for each Corporation to be wound up once it had substantially achieved its objectives. In July 1989 the Government's White Paper "The Scottish New Towns - The Way Ahead", contained proposals for the progressive winding-up of the Corporations by 1999.
- 3 In February 1992, following consultation, the Secretary of State made the orders to wind-up the operations of East Kilbride and Glenrothes Development Corporations on 31 December 1995. Wind-up has happened and both Corporations were dissolved as legal entities on 5 April 1996.
- 4 During 1993, the Secretary of State reviewed the timetable for completion of the work of the other three Corporations: Cumbernauld, Livingston and Irvine. He concluded it was desirable to bring completion forward to 1996 from 1999. This reflected the ability of Locate in Scotland and the local enterprise network, established in 1991 under Scottish Enterprise, to take over responsibility for economic development within the new towns; and the desire for the local authority type functions to transfer on re-organisation of local government in Scotland, expected from April 1996. In December 1993 the Secretary of State made Orders to wind-up Cumbernauld, Livingston and Irvine by 31 December 1996. All three Corporations ceased operations on this date. A chronology of key events is at Appendix 1.
- 5 Winding-up the Corporations involves a wide range of activities, including the disposal of commercial and industrial land and property, which is the subject of this report.

Disposal of new town commercial and industrial land and property

- 6 The Scottish Office Development Department and, before October 1995, the Scottish Office Industry Department (the Department) have been responsible for ensuring that all Corporations complete development of the towns and cease operations by the dates set by the Secretary of State. In March 1992 the Department issued guidance to the Corporations on the winding-up of their affairs, amongst other matters requiring the Corporations to dispose of their entire interest in land and premises.
- 7 Since 1992 the five Corporations have sold substantial amounts of commercial and industrial property mostly to the private sector. By December 1996 these sales realised almost £420 million in total, representing a step change in the scale of disposals compared to earlier years (Figure 1).

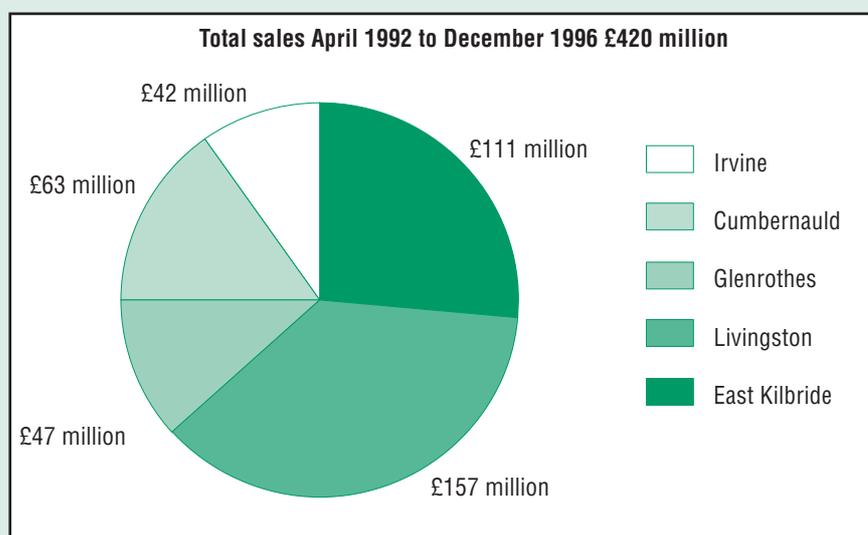
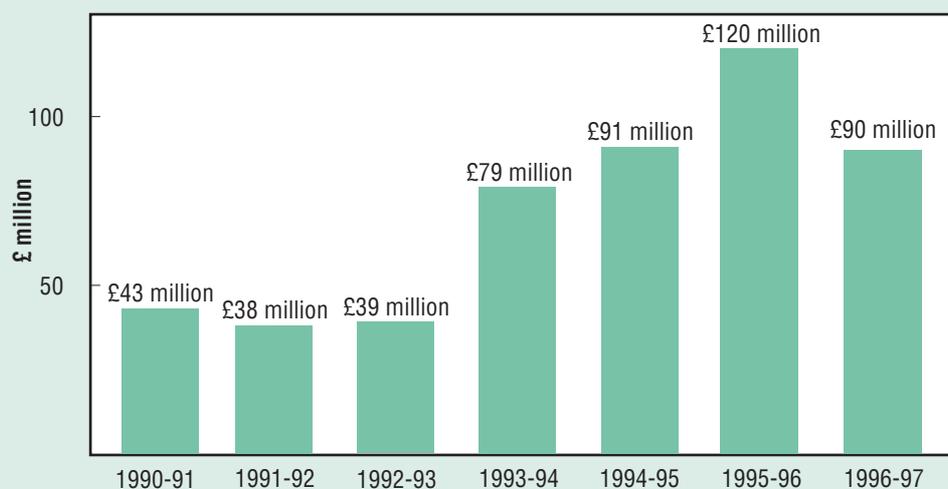
The National Audit Office examination

- 8 The disposal of commercial and industrial land and property assets realising £420 million in less than five years is a substantial task. The National Audit Office therefore decided to focus their examination on these disposals and sought confirmation that the Department and the Corporations had implemented the programme in accordance with current professional practice and recommendations of the Committee of Public Accounts. In particular they examined:
 - a) **Planning the sales:** whether the Department and the Corporations established sound disposal plans, taking into account prevailing market conditions, so as to ensure sales took place in an effective manner (part 2 of this report).
 - b) **Sales performance:** whether Corporations conducted individual property disposals so as to maximise sales proceeds taking account of the objectives of the disposals (part 3 of this report).

Methodology

- 9 The National Audit Office examined 37 individual, mainly high value sales out of a total of 283 major sale transactions. The 37 sales examined provided receipts of some £176 million (53 per cent of the total receipts of sales of commercial and industrial land and property for the period examined from April 1992 to March 1996 - see Figure 2). They supplemented this by analysis of key statistics for the other sales completed in this period. They interviewed the senior staff responsible for the sales programme at each Corporation and their external property advisers, and members of the Department's New Towns Disposals Advisory Group. Richard Ellis property consultants provided advice to the

Figure 1: Receipts from disposals of Scottish New Town commercial and industrial land and property 1990-96



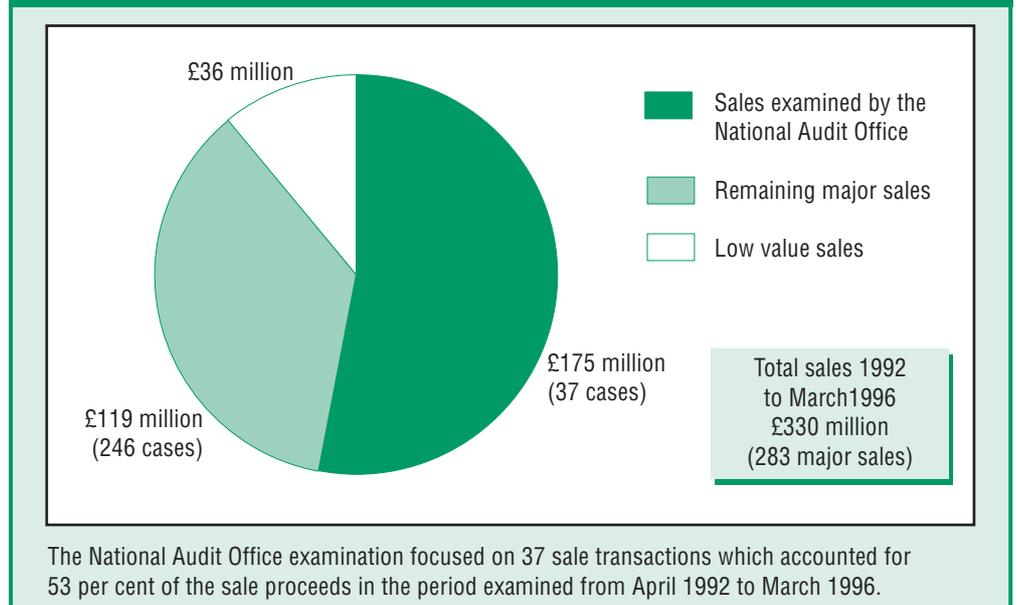
Source: The Department

Between April 1992 and December 1996, the five Corporations sold substantial amounts of commercial and industrial land and property mostly to the private sector. The sales have raised proceeds of some £420 million, and represent a step change in the scale of disposals compared to earlier years.

National Audit Office on the Corporations' disposal and marketing strategies, and on the conduct of individual sales, while Price Waterhouse provided advice on certain tax matters. Details of the study methodology are at Appendix 2.

- 10 Cases 1 to 4, presented at pages 32 to 35 of this report, are four of the 37 cases examined by the National Audit Office. They illustrate important issues arising from their work.

Figure 2: Value of sales examined by the National Audit Office



Previous recommendations of the Committee of Public Accounts

- 11 In 1987 the Committee of Public Accounts examined the Disposal of New Town assets in England and Wales between 1979 and 1986 (Tenth Report, HC 234, 1986-87). Appendix 3 includes a summary of the Committee's recommendations from this and subsequent reports on the disposal of public assets which are relevant to this report.

Part 2: Planning the sales

- 1 This part of the report considers the Department's and the Corporations' strategy for and timing of sales in relation to market conditions etc, and the financial targets for the disposals programme.
- 2 The Committee of Public Accounts has emphasised the importance of a well-considered disposal strategy, and the need to ensure that sales are supported by reliable procedures and controls. They recommend that when planning sales programmes bodies should ensure that their strategy is directed towards clear and specific disposal objectives, and is fully implemented without delay (Appendix 3 Issue 1). The Department's objective for the Corporations' sale of commercial and industrial land and property was to ensure that other than in exceptional circumstances the whole interest in assets was disposed of, for the best prices reasonably obtainable, by the wind-up dates set by Ministers.

Did the Department and the Corporations establish robust sales strategies, taking all relevant factors into account?

The Department provided a strong framework of guidance governing Corporations' management of disposals and Corporations implemented sound sales strategies based on expert professional analysis and advice. In one area, industrial buildings allowances, preparation might have been better.

- 3 In March 1992, shortly after the wind-up orders for the first two new towns had been made, the Department issued comprehensive guidance to all Corporations setting out general principles to govern the conduct, monitoring and control of sales (Figure 3). The Department issued supplementary guidance in 1993, 1994 and 1995. This guidance recognised the Committee of Public Accounts recommendations on the disposal of public assets (Appendix 3).
- 4 Also in early 1992 the Department established an advisory group to oversee the sale of commercial and industrial property assets by Corporations. This group comprised representatives from the Department, including their professional estates adviser, and a private sector property professional, who together provided advice on market conditions, timing and size of disposals and consideration of bids. The group aimed to ensure that the Exchequer obtained maximum receipts from disposals, while recognising the other objectives of wind-up and of completing the development of the towns.
- 5 An important part of the group's work was to examine Corporations' disposal strategies and ensure that appropriate packages of assets were put to the market and that clashes of timing were avoided. They were also required to consider and approve each proposed disposal of assets where the pre-sale valuation was more than £4 million (though the group relaxed this condition for three Corporations from July 1994, reflecting those Corporations' disposals

Figure 3: Summary of the Department's disposals guidance to Corporations

General principles

- ◆ Assets to be sold with the benefit of appropriate planning approval in place, for the best consideration reasonably obtainable, and with a presumption in favour of open competition and appropriate publicity. Department's approval required for any proposed exceptions
- ◆ Disposals to be conducted in a fair and equitable manner, with any private negotiations after marketing fully documented
- ◆ Professional selling agents should normally be appointed to assist with sales
- ◆ Sales to tenants should be conducted against a full knowledge of market value, and having regard to the effect of any sale on the price obtainable for surrounding property
- ◆ A small number of strategic sites and advance factories for inward investment to be earmarked and transferred to Scottish Enterprise
- ◆ Corporations should continue with "normal" development activity in their towns. Nothing in the guidance is intended to effect such transactions, and Corporations are responsible for ensuring that the terms for these disposals represent the best consideration reasonably available
- ◆ Sales other than in exceptional circumstances should involve disposing of the whole interest in an asset and thereby free Corporations from further involvement
- ◆ Conditions of sale to include clawback provisions to secure a share in any increase in value resulting from a change of use following disposal

Monitoring and control

- ◆ Corporations to handle sales on the basis of clear formal procedures, with formal valuation of the assets recorded before any disposal procedure commences
- ◆ The Department's advisory group to be involved in the assessment of bids in all major disposals (over £4 million)
- ◆ Corporations' internal audit to scrutinise disposal procedures and transactions
- ◆ Corporations' to provide quarterly reports on progress with the disposals programme

Source: Scottish New Town Development Corporations Guidance on Wind-up (March 1992)

In 1992 the Department provided comprehensive guidance to govern Corporations' conduct, monitoring and control of disposals.

experience to that date). As a result, the group reviewed and approved 16 sales realising receipts of £145 million, or 44 per cent of total receipts between 1992 and March 1996.

- 6 In accordance with the Department's guidance, in 1992 and 1993 each Corporation appointed external property professionals to assist with sales. Each Corporation selected their advisers on the basis of the lowest bid after competition. In each case the advisers' key responsibilities included advice on the formulation of disposal strategies, and on the valuation and disposal of each major sales package.
- 7 Richard Ellis, consultants to the National Audit Office, evaluated the advice from these five external agents in relation to sale strategies. On this basis the National Audit Office concluded that the advice was of a consistently good standard, and that the advisers had demonstrated a sound knowledge of the issues which might influence sales performance.

Industrial buildings allowances

- 8 The National Audit Office identified one area, industrial building allowances, where sales preparation might have been better. Where qualifying conditions are met purchasers of industrial properties may have access to tax allowances known as industrial buildings allowances. Such allowances may be given as a deduction in computing profit assessable to tax. They may therefore provide potential savings to purchasers, and lower tax receipts, depending on purchasers' individual tax status and the extent to which they are able to and do in fact claim the allowances. Appendix 4 summarises the provisions which govern the availability of allowances.
- 9 Corporations' sales of industrial property completed by March 1996 have generated receipts of £182 million. To quantify precisely the potential industrial buildings allowances position for these properties would have required the detailed examination of the records of each individual property. However, extrapolating from Price Waterhouse's work for them on six high value cases examined, the National Audit Office estimated that utilisation of the potential allowances by purchasers of all industrial properties sold by Corporations since 1992 could give rise to tax savings to purchasers of up to a range of £12 million to £16 million (see Appendix 4). In practice the actual tax savings are likely to be reduced by various factors (as discussed in paragraph 6 of Appendix 4).
- 10 Previous public sector experience had not established a need to consider industrial buildings allowances. The Department's sales guidance did not therefore deal with the allowances and Corporations made their own decisions concerning allowances on a case by case basis, supported for the major disposals by advice from their professional sales agents. Consistent with the Department's objective to dispose of the whole interest in property, Corporations proceeded on the basis of established practice, which allows purchasers access to the allowances.

Corporations' approaches to industrial buildings allowances

- 11 Corporations adopted different approaches to providing information on allowances to prospective purchasers. Irvine and Livingston commissioned accountancy advisers to assemble and make available to bidders detailed, precise and verifiable information about allowances as part of property information made available to help inform their bids. East Kilbride took a similar initiative in one case, though they did not make the information available before the closing date for bids. Cumbernauld and Glenrothes took no such initiative.
- 12 Where Corporations had not prepared information about allowances for marketing purposes, they advised the National Audit Office that they would have responded positively to any prospective purchaser's request for data on allowances. In some cases the purchaser did seek and obtain such data once a provisional sale agreement and price had been reached. There is no evidence that prospective purchasers had been less than satisfied with the information that had been made available to them.

- 13 There is no evidence about how far in practice purchasers place value on the allowances. In seeking best price for a property some sellers believe that it helps to emphasise the availability of allowances during marketing. There is, though, no accepted valuation practice to demonstrate explicit values for allowances within property valuations. The National Audit Office and their property advisers could not identify any independent evidence from other property sales to demonstrate that purchasers are willing to pay a price premium in recognition of the availability of industrial buildings allowances.
- 14 In only one case examined by the National Audit Office, which was at Irvine, was there evidence that either a Corporation or their professional adviser separately considered or quantified the allowances for the purposes of their pre-sale valuation. Generally the Corporations and the Department took the view that there was no requirement for this because their valuations relied on comparisons with disposals on the open market and would therefore implicitly reflect the market's assessment of the worth of industrial building allowances.

Conclusions on industrial buildings allowances

- 15 In most cases (66 per cent by value of industrial property sales to March 1996) Corporations sold properties on the open market after full competition. The remaining disposals were negotiated. In this mature market bidders could reasonably have been expected to take into account all relevant factors including, if appropriate, the availability of industrial buildings allowances in preparing their bids. Nevertheless, while the National Audit Office found no evidence to show that the absence of consistent treatment reduced sale proceeds, they concluded that it would have been advisable for all Corporations to have assessed the potential tax allowances available to purchasers prior to each sale and to have drawn attention in all cases to the allowances during marketing. This would have helped to ensure that intending purchasers had all relevant information about any potential tax benefits before making bids, and would thus have contributed to the Corporations' responsibility to satisfy themselves that the terms for any disposal represented the best consideration reasonably obtainable.

Did the Department and the Corporations give sufficient consideration to the timing of sales, in order to maximise sale proceeds?

The Department's advisory group successfully minimised overlap in the marketing of major disposals by the five Corporations. Market conditions over the wind-up period have been favourable as indicated by the level of market interest in the largest disposals, the prices achieved, and wider market trends.

- 16 Many of the new town properties to be sold were tenanted warehousing and manufacturing units, typically on estates which the Corporations had themselves developed. Drawing these properties together for sale as investment packages in single lots was seen by the Department, the Corporations and their external advisers as a means of providing viable portfolios in the same

geographic areas thus enhancing their marketability. It also reduced Corporations' sales costs, and was the most cost-effective way of disposing of some of the less desirable properties. It was also the most practical means of completing the significant sales programme within the required period, taking into account the 1993 decision to accelerate wind-up of two Corporations (paragraph 1.4).

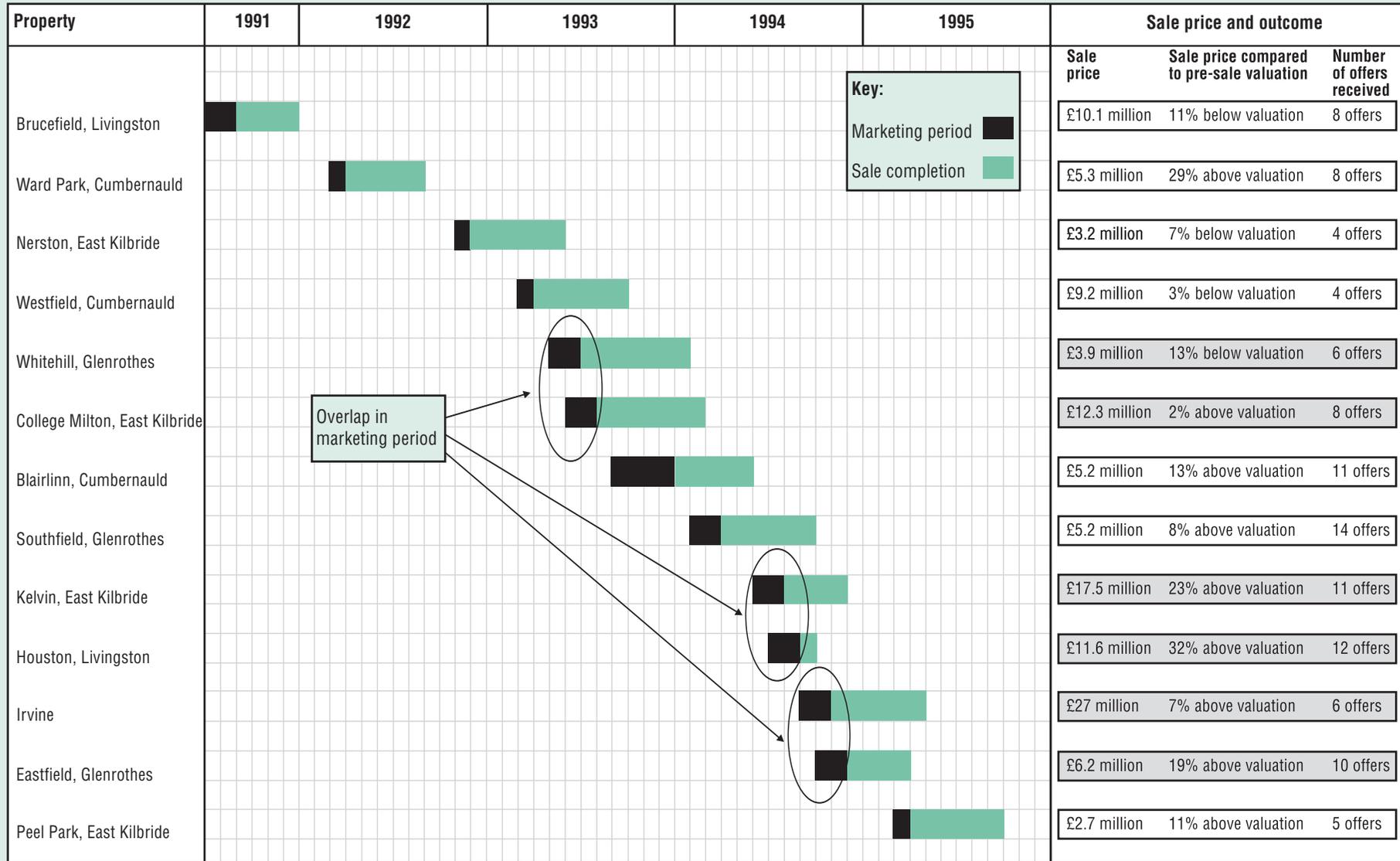
- 17 A key role for the Department's advisory group was therefore to co-ordinate the sales programme to ensure that where possible Corporations did not take these large packages to the market at the same time. Any overlap in the programme might dilute market interest and reduce prices achieved. This was because most of the bidders for new town properties were private property and investment companies which were not likely to apply themselves to more than one complex, high value transaction at a time.

- 18 Up to March 1996 Corporations completed 13 package sales of industrial property each yielding between some £3 million and £27 million receipts, some £120 million in total. Nine sales were marketed in 1993 and 1994 and in six of these cases the marketing period partly coincided with that of another package from a different town. Nevertheless market interest remained satisfactory in all cases and the final price paid exceeded pre-sale valuations in five of the six cases where overlap had occurred (Figure 4). In the sixth case there was no evidence that timing of marketing had adversely affected the sale. Cases 1 and 2 at pages 32 and 33 are examples of these sales.

- 19 Wider property indicators suggest that, in carrying out their disposals, Corporations benefited from favourable market conditions. Between 1991 and 1995 the total returns on investment in the Scottish property market consistently outstripped the UK average. Returns on all types of Scottish property peaked in 1993 and 1994 during which time Corporations marketed 10 major industrial portfolios, and completed sales worth approximately £170 million in total (see Figure 5). The Corporations' position is in contrast to recent experience in England, where between 1990 and 1994 the work of the Commission for New Towns in meeting targets for disposal receipts set by the Department of the Environment had been made difficult by the downturn in the property market there*.

* Commission for the New Towns: Disposal of Land and Property Assets - Report by the Comptroller and Auditor General (HC 308 Session 1994-95).

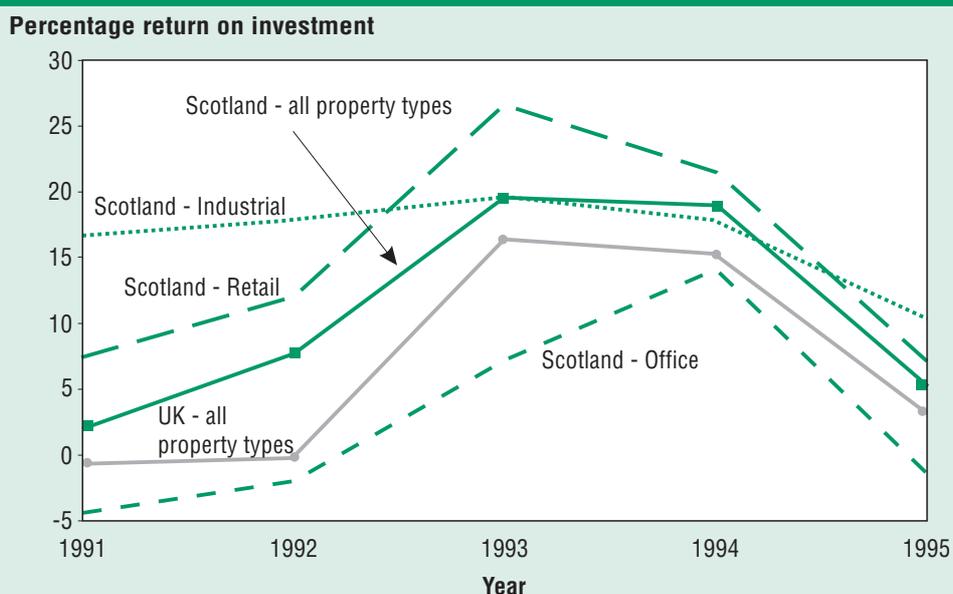
Figure 4: Major package sales of tenanted industrial property



Source: National Audit Office examination

Up to March 1996 Corporations completed 13 major package sales of industrial property, including six cases where the marketing period coincided with that of another package from another town. Market interest remained satisfactory throughout, with between six and 12 bids received in the overlap cases resulting in a final price above the pre-sale valuation in five of those cases.

Figure 5: Scottish investment property trends 1990-1995



Source: Scottish Property Market Report 1995, University of Paisley/Scottish Enterprise

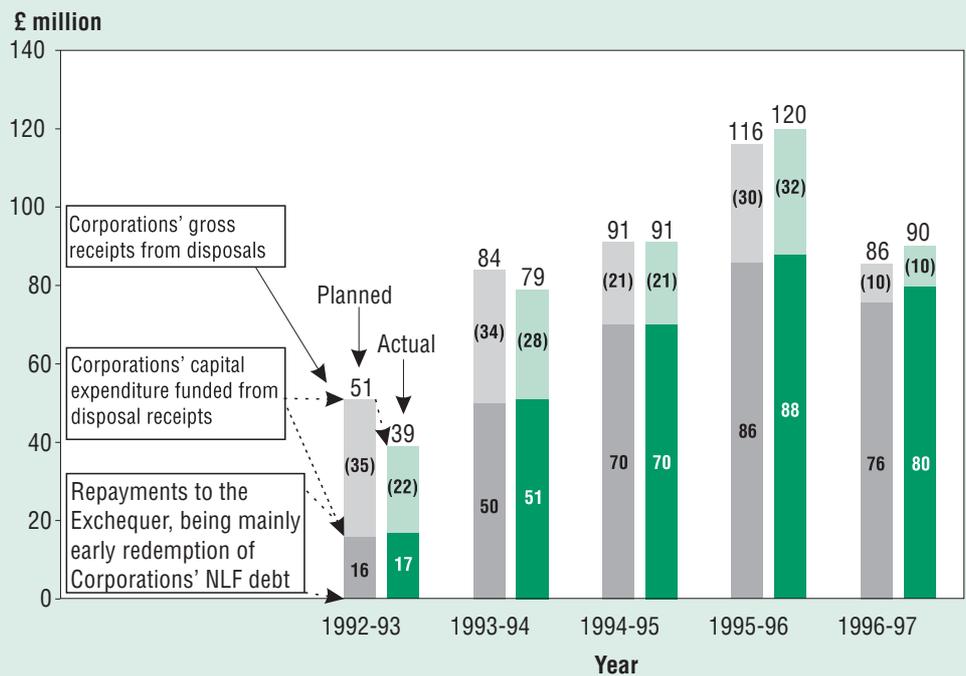
Between 1991 and 1995 the total returns on investment in the Scottish property market consistently outstripped the UK average. Returns on all types of Scottish property peaked in 1993 and 1994 during which time Corporations marketed 10 major industrial portfolios, and completed sales worth approximately £170 million in total.

Did the Corporations achieve sales and receipts targets set by the Department?

The Corporations have met or exceeded the key financial targets for the disposal programme, mainly concerning the premature redemption of part of their outstanding National Loans Fund debt. As a result Corporations have returned to the Exchequer £306 million of the £420 million total receipts generated between 1992 and December 1996. Corporations completed the sale programme by the wind-up dates set by the Secretary of State and have eliminated all outstanding debt.

- 20 Since the commencement of the wind-up and disposals programme in 1992-93 the Department have reviewed and approved annually Corporations' disposals plans. As part of this, Corporations have been required to apply disposals receipts both to finance remaining investment in development in the new towns and to make increasing net repayments to the Exchequer, mainly represented by early redemption of the Corporations' outstanding National Loans Fund debt. The net repayment targets were the key financial targets for the disposal programme set by the Department. Corporations collectively satisfied or bettered these targets of £16 million, £50 million, £70 million, £86 million and £76 million respectively for the five years 1992-93 to 1996-97 (see Figure 6).

Figure 6: Corporations' performance against receipt targets 1992-93 to 1996-97



Source: Scottish Office Development Department

Corporations have together achieved or bettered the key financial targets for disposals, concerning repayments to the Exchequer. Where necessary they have reduced investment plans to achieve their repayment targets.

Part 3: Sales implementation and outcome

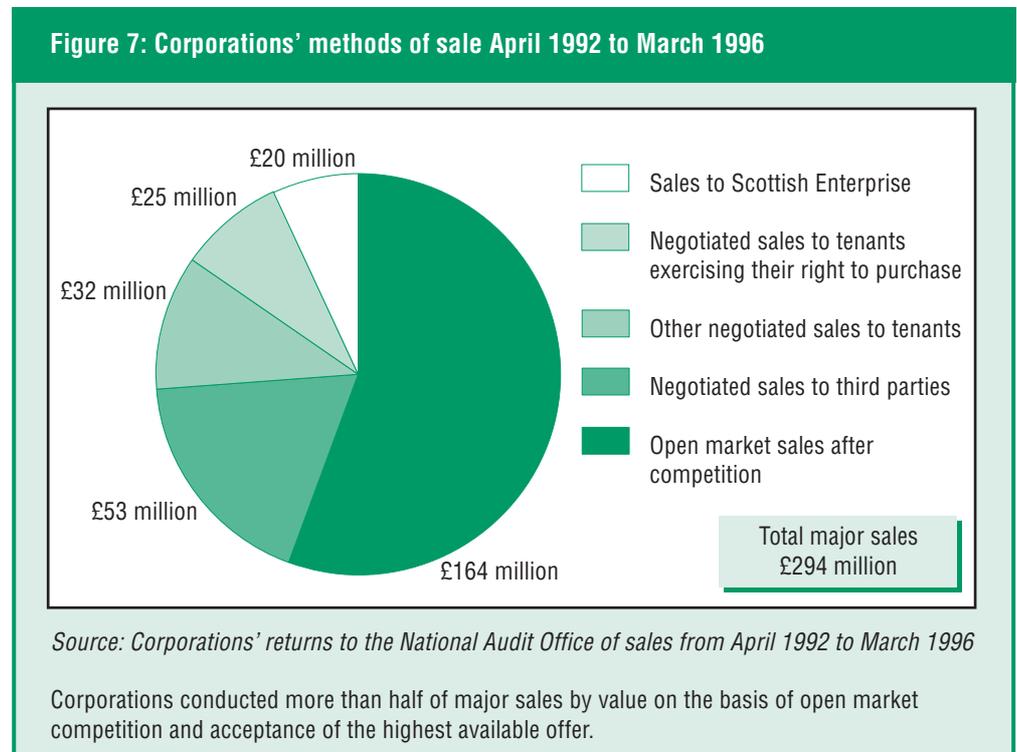
- 1 This part of the report considers how well Corporations have conducted individual property disposals, and whether they have concluded sales at the maximum price taking account of the objectives of the disposals.
- 2 For this analysis the National Audit Office examined in-depth a sample of 37 mainly high value disposals out of the total of 283 major sales. The sales examined in detail realised £176 million, representing 53 per cent by value of the £330 million sales completed in the period examined between 1992 and March 1996. The National Audit Office supplemented this casework with analysis of key statistics for the other 246 major sales completed in the same period (Appendix 2).

Did the Corporations adopt appropriate methods of sale to maximise sale proceeds?

Sales completed after open market competition and acceptance of the highest available offer realised £164 million (56 per cent of receipts from major sales). The Department permitted sale by negotiation where wider policy justified it, subject to achieving a sale price equivalent to estimated open market value. Corporations sold property worth £45 million (15 per cent) by negotiation to tenants exercising their rights to purchase or to Scottish Enterprise. They sold the remaining property worth £85 million (29 per cent) also by negotiation; in these cases they did not consider open market disposal appropriate. In all 22 non-competition sale cases examined by the National Audit Office, there were reasonable grounds for not pursuing open market disposal.

- 3 The Department's guidance to Corporations (paragraph 2.2) reflected previous recommendations by the Committee of Public Accounts (Appendix 3, Issue 3) that assets should be exposed to the market unless there are compelling reasons to the contrary, and that exceptions to competitive tender, including sales to tenants, should be subject to strict controls. It required the Department to approve any proposed exception to full market exposure. And sales by negotiation were permitted in defined circumstances only, for example to tenants whose leases already included a right to purchase and without offering favourable terms (Appendix 3 Issues 3 and 4). Also the guidance provided for Scottish Enterprise to purchase, at the greater of open market value or the building's cost, a small number of sites and properties of strategic importance for future inward investment.
- 4 Between April 1992 and March 1996 Corporations completed £164 million (56 per cent) of major sales after competition. There were a further £45 million (15 per cent) negotiated sales, either to tenants exercising their right to

purchase or to Scottish Enterprise. The remaining £85 million (29 per cent) were other negotiated sales where Corporations did not consider open market disposal to be appropriate (Figure 7).



- 5 The National Audit Office examined 22 cases where Corporations had not exposed the property to the open market. In each case there were reasonable grounds for this, mostly because the sales were made for strategic or economic development reasons and competition would not have been appropriate or practicable (Figure 8).

Did the Corporations adopt appropriate and effective marketing methods?

Overall marketing of the major package disposals was of a high standard with satisfactory results, and costs were controlled. The information made available to bidders appeared sufficient and reliable, though in a few cases small price changes resulted from changes to and disagreement with purchasers about property information.

- 6 Successful marketing and sale of commercial and industrial property, particularly tenanted property to be sold for investment, requires the seller to provide a range of financial and non-financial information to help prospective purchasers formulate their bids. The information may include:

Figure 8: Case findings on methods of sale

		Sales value £ million	Percentage by value
Sale after competition on the open market.	15 cases	123	70
Non-competition sales	22 cases:		
5 cases	Tenants' exercising their right to purchase under the lease.	25	14
2 cases	Negotiated sale because of the prospect of increased proceeds as a result of releasing marriage value.	6	4
6 cases	Transfers to Scottish Enterprise for strategic or other economic development reasons.	8	4
7 cases	Sales to companies seeking to locate within the new town, and therefore furthering the Corporation's wider statutory objectives for development of the town.	8	5
2 cases	<ul style="list-style-type: none"> ♦ one negotiated sale of additional land to secure completion of a tendered sale of a development site; ♦ one tenant sale resolving a long-standing dispute with the tenant over liability for remedial work on the property. 	less than 1	-
		5	3
		<u>176</u>	<u>100</u>

Source: NAO examination of 37 disposals

The National Audit Office examination included 22 cases where Corporations had not exposed the property to the open market. In each case the National Audit Office concluded that there were reasonable grounds for this.

- physical description of and data on the property, encompassing the quality of the fabric and any environmental factors such as contamination;
- lease and tenancy details including the financial standing of tenants; and
- information on management costs etc associated with ownership of the property.

7 While the seller does not need to guarantee the information provided the Property Misdescriptions Act 1991 is a legal benchmark^{*} and there will be an expectation amongst prospective purchasers that the seller has made all

* The Act prohibits the making of false or misleading statements about property matters in the course of estate agency and property development business.

material information available for the purposes of a best and final bid. If the seller fails to highlight favourable information about a property, there is the risk that bidders may bid too low. Conversely, if the seller fails to disclose potentially adverse information there is a risk that the selected bidder will subsequently seek a reduced price by negotiation.

- 8 The National Audit Office examined 10 of the 13 major package sales of Corporations' industrial property. In each of these cases the design and presentation of marketing particulars were of a high standard, there was widespread advertising and other marketing activity and costs were controlled and reasonable. As described in part 2 of this report, there was a good response from prospective purchasers to Corporations' marketing of these cases.
- 9 In most cases the property information supplied to bidders appeared to have been sufficient with the exception of industrial building allowances information, paragraph 2.15 above. Aspects of four cases, though, raised questions about the Corporations' performance:
 - a) In one case there were mistakes and delays in property information Livingston Development Corporation provided to bidders. The mistakes were corrected after marketing was well advanced.
 - b) In three other cases the Corporations concerned (Cumbernauld, East Kilbride and Glenrothes) accepted small reductions from the highest bid linked to revised property information becoming available after offers were received. The resulting price variations were between one and three per cent of the final proceeds in each case, and can be attributed to purchasers' intention to take reasonable steps to protect their own position during final sale negotiations (see Figure 9).

Did the Corporations obtain up-to-date valuations to benchmark the sales?

Corporations obtained pre-sale valuations from their external sales advisers for almost all sales (98 per cent by value) conducted on the open market, but much less often for other, negotiated sales (50 per cent by value). This was because Corporations considered that the District Valuers' annual valuations of all their property for different accounts purposes often provided a sufficient alternative, when taken together with the knowledge and experience of their in-house professional staff. In nine of the 37 sales examined valuation benchmarks were unavailable or were weak because they did not anticipate the terms of the sale sufficiently.

- 10 The Department's guidance required Corporations to record a formal valuation of assets before any disposal and to undertake revaluations where disposals became protracted or the market shifted significantly (Appendix 3 Issue 7).

Figure 9: Quality of marketing particulars

Livingston Development Corporation - sale of Brucefield industrial estate for £10,212,000 November 1991

- ◆ This was the first major package sale of tenanted industrial property by any Corporation. It was completed prior to the start of the wind-up programme and the issue of disposals guidance by the Department, and the quality of the marketing process was not of the same standard the Corporation achieved in later sales. Marketing commenced in early July 1991 and particulars were issued to over 350 parties. However errors in sale particulars including rent review notice periods, service charges and tenancy schedules were identified after most of the marketing period had elapsed, requiring the Corporation to issue revised information three weeks before the closing date for offers. Two bidders expressed concerns on these points, though in the end the information made available was accepted as sufficient and ten bidders submitted offers for the property.

Glenrothes Development Corporation - sale of Whitehill and Viewfield industrial estates for £3,900,000 January 1994

- ◆ Parts of this industrial estate were let on the basis that the landlord met internal repair costs. Because of the overriding need to achieve the planned programme of sales the Corporation did not have sufficient time to research and make available detailed information about such costs prior to marketing the property and accepted that this could lead to bidders attempting to renegotiate their offers. Following receipt of offers the Corporation selected a preferred bidder, who requested additional information on repair costs before finalising terms. The Corporation made this information available, after four months research, and on this basis the purchaser reduced his offer from £4,035,000 to £3,900,000.

East Kilbride Development Corporation - sale of College Milton industrial estate for £12,300,000 February 1994

- ◆ Marketing material included reference to the Corporation's estimates of non-recoverable estates management expenditure. The estimate was lower than actual Corporation expenditure on the expectation that potential purchasers could achieve savings in this area. Following receipt of offers, the preferred and highest bidder attempted to negotiate his offer of £12.625 million down because he came to the view that non-recoverable expenditure levels would be significantly greater than the Corporation had suggested. The Corporation were unable to satisfy this bidder that their estimate was reasonable and formed the view that the bidder wished to withdraw from the transaction. They commented to the National Audit Office that the disputed estimate was at the same level applying for all other package sales and was accepted by all other bidders without query. Accordingly the Corporation terminated negotiations and completed sale of the property with the original second highest bidder.

Cumbernauld Development Corporation - sale of Ward Park and Blairlinn industrial estates for £5,250,000 May 1994

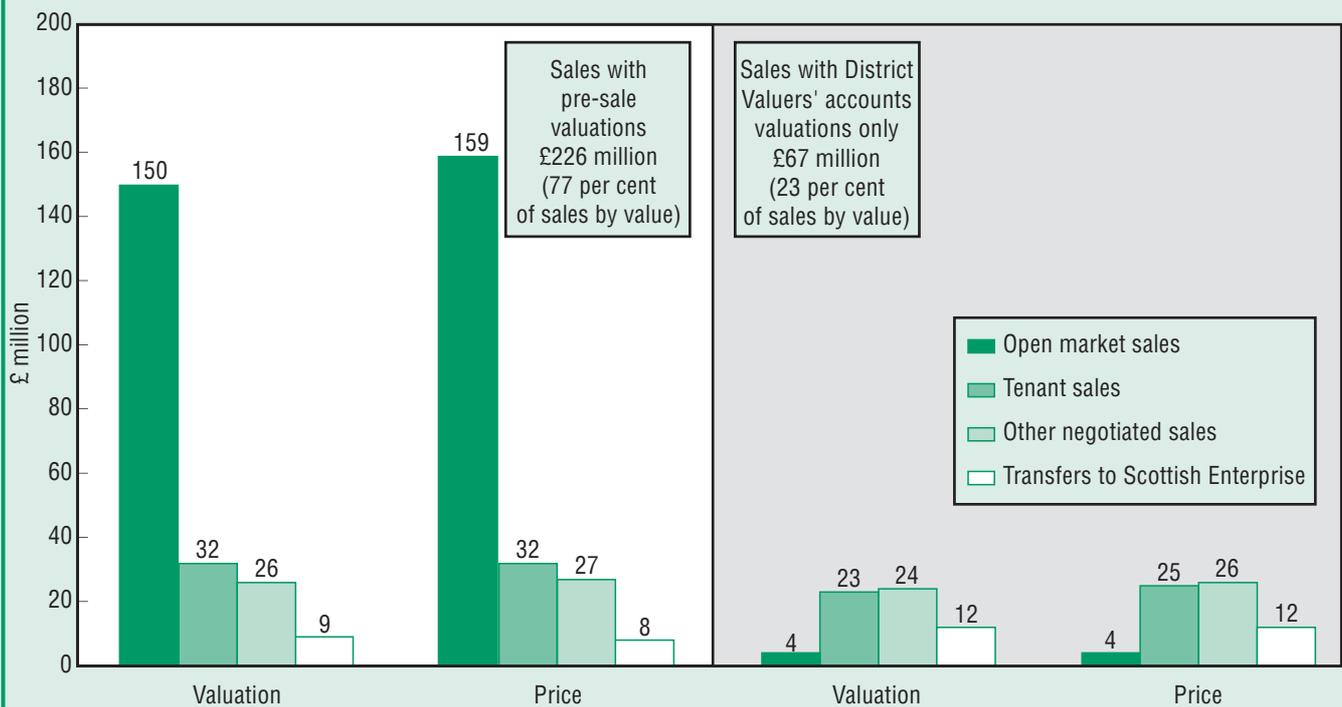
- ◆ The marketing brochure did not include reference to a stepped rental agreement in respect of a unit within this large industrial estate. As a result, following receipt of offers and selection of a preferred bidder, the purchaser negotiated a £50,000 price reduction on his offer of £5,300,000 to take account of the rental agreement.

Source: National Audit Office examination of 37 disposals

In most cases examined by the National Audit Office information supplied to bidders appeared sufficient and reliable. In one case though the standard of marketing information was poor (Brucefield, Livingston) while in three other cases Corporations accepted small price reductions from the highest bid linked to revised property information becoming available.

- 11 The National Audit Office's analysis of sales data for all major sales demonstrated that Corporations obtained formal pre-sale valuations from their advisers in 77 per cent of cases by value. Such valuations were obtained for 98 per cent of sales conducted on the open market but only 54 per cent of other mainly negotiated sales, including sales to tenants (Figure 10). This was because Corporations considered that the District Valuers' annual valuation of all their property for accounts purposes often provided a sufficient alternative, when taken together with the knowledge and experience of their in-house

Figure 10: Incidence of pre-sale valuations



Source: Corporations' returns to the National Audit Office of sales from April 1992 to March 1996

Corporations obtained formal pre-sale valuations in 77 per cent of sales by value. In most other cases, including about half of all negotiated sales to tenants and third parties, there was no pre-sale valuation and Corporations relied on the latest available accounts valuations from the District Valuers and the knowledge and experience of professional staff.

professional staff. In a few cases sales may have been concluded in line with fixed prices set in options to purchase within lease conditions, and in such circumstances a pre-sale valuation would not be required.

- 12 The National Audit Office's analysis of 37 cases found that the Corporations' sales advisers had provided pre-sale valuations for 17 sales which generated receipts of £116 million.
- 13 In the other 20 cases, which generated sales receipts of £60 million, there were no formal pre-sale valuations by the sales advisers. In 11 of these, Corporations had benchmarked in other ways, eg against the District Valuers' annual valuations of the property for accounts purposes. In the remaining nine cases, ie one in four of the cases examined, there were doubts about the quality of the valuation information available.
- 14 In four of these nine cases the Corporation had completed the sales on different terms to those known to the District Valuers when valuations were made for the annual accounts. In three cases the Corporations obtained no valuation prior to agreeing sale terms, or had not updated the valuation to take account of changes since the valuation was prepared. In one case the Corporation negotiated a sale to a tenant based on an option price set a year earlier; the

basis of this price was not recorded and the purchaser subsequently sold on the property at a higher price. And in the final case relevant papers were not available (Figure 11).

Figure 11: Case findings on pre-sale valuations

Number of cases	Valuation evidence	Sales value £ million	Percentage sale value
17	Satisfactory pre-sale valuations provided by sales advisers	116	67
6	Satisfactory benchmarking of sale against District Valuers' accounts valuations	6	3
2	No formal pre-sale valuations but sales advisers provide broad indication of value and/or asking price	18	10
3	No formal pre-sale valuations but regard paid to comparative sales prices (housing land sales)	2	1
4	No formal pre-sale valuations. Sale completed on different terms to those known to the District Valuers for the accounts valuations	15	8
5	Other, eg no valuation, valuation not updated, valuation papers not traced	19	11
		<u>176</u>	<u>100</u>

Source: National Audit Office examination of 37 disposals

The National Audit Office examination included nine cases where they questioned the quality of valuation evidence available to assess prices achieved.

- 15 For the sale of public assets to tenants particularly the Committee of Public Accounts have recommended bodies should obtain open market valuations and employ agents to negotiate with tenants (Appendix 3 Issue 3). This reflects the need for professional judgement about how much can be secured in negotiation, and the idea that agents can adopt a commercially independent attitude in negotiating with tenants. The Government responded by indicating that individual bodies will have responsibility for deciding whether agents should be employed, and the Government have emphasised the need for a tough negotiating stance.
- 16 Major sales made by Corporations to tenants generated receipts of £57 million (19 per cent of major sales proceeds). In 44 per cent of these cases by value the Corporations' own professional property staff negotiated the sales directly without preparing a pre-sale valuation, though with the benefit of the latest available accounts valuations from the District Valuers and their own professional knowledge of the market (see Figure 10).

Did the Corporations apply sufficient control over sales?

In most cases Corporations conducted sales satisfactorily, involving senior officials and Board members in key sales decisions. The Department's disposals guidance did not seek to alter existing practice for cases where Corporations were pursuing their long established economic development role, which required them to strike a balance between encouraging development and maximising sales proceeds.

- 17 The Department's guidance required Corporations to establish clear formal procedures for disposals. These included delegated limits and separation of duties between key Corporation staff, and the involvement of professional selling agents.
- 18 The National Audit Office found that Corporations did not meet this requirement fully. Irvine and Cumbernauld had no written sales instructions other than the Department's guidance. East Kilbride and Livingston, had established their own checklist for the management of disposals though Livingston's was incomplete. Glenrothes had established written financial delegations governing who could conduct sale negotiations and rules for recording sales valuations, but had no other written procedures.
- 19 Nevertheless, in most cases examined Corporations had conducted the sales in a reasonable way. Their chief officials were consulted before key sale decisions, and Board members were often consulted and were always kept informed. Difficulties with sales such as late or withdrawn bids were rare, arising in only four cases, and Corporations handled three of these satisfactorily (Figure 12).
- 20 The Government's policy was to allow Corporations to continue to undertake or plan development activity. The Department's guidance on disposals (paragraph 2.2 and Figure 3) stated that Corporations should continue with "normal" development activity in their towns during the wind-up period and that nothing in the guidance was intended to affect such transactions. Corporations were responsible for satisfying themselves that the terms for disposals linked to development activity represented the best terms that could reasonably be obtained.
- 21 The National Audit Office examined 12 disposal cases linked to Corporations' development activity. Usually these cases required sale by negotiation, since introducing competition might have defeated the objective to secure or maintain investment by the company purchasing the property. Linked to this, Corporations generally did not consider it appropriate to engage independent selling agents in such cases. In five such cases there were doubts about the quality of valuation benchmarks available, as described in paragraph 3.13.

Figure 12: Handling of sales - problems encountered

Cumbernauld Development Corporation - sale of Westfield/Lenziemill Industrial Estate for £9.25 million September 1993

- ◆ Following conditional acceptance of the highest offer, at £10.8 million, the successful bidder for this estate proposed a reduction in the purchase price to £9.41 million. The revised offer was lower than the bid originally received from the under bidder, with a net present value of £9.82 million, but this bid was conditional on lettings and satisfactory survey reports and was much less secure. Two months after refusing their previous offer the Corporation asked the original under bidder to submit a revised bid within three days. The company did so, but on conditional terms which were unacceptable to the Corporation and the Corporation's agents recommended the Corporation proceed with the preferred bidder's revised offer at £9.41 million. The sale proceeded on this basis, though subsequently the Corporation accepted a further reduction to £9.25 million as a result of building defects discovered during final investigations by the purchaser.
- ◆ The National Audit Office recognises the Corporation's right to refuse conditional or insufficiently precise bids. In this case the safest course of action after the preferred bidder had reduced their offer by £1.4 million would have been to invite all interested parties to rebid.

East Kilbride Development Corporation - sale of College Milton Industrial Estate for £12.3 million February 1994

- ◆ Eight offers were received for this estate. After offers were received the highest and preferred bidder sought a significant reduction in the purchase price. This was unacceptable to the Corporation who terminated negotiations with the preferred bidder and concluded the sale with the second highest bidder, reaching agreement at a price in excess of the pre-sale valuation.

Glenrothes Development Corporation - sale of Eastfield Industrial Estate for £6.2 million April 1995

- ◆ The Corporation received ten offers for its last major package of industrial assets by the closing date of 8 December 1994. On 11 December, one of the interested parties submitted a revised bid, stating that there had been an error in the calculation of their original offer. In accordance with Scottish Office guidelines on late bids, which took into account the experience from the earlier sale in Cumbernauld (see above), all parties were advised that such a bid had occurred and invited to re-submit their offers by a revised closing date. All but two did so and the price eventually agreed was some £170,000 higher than the best offer under the original tender.

Irvine Development Corporation - sale of Irvine industrial property for £27 million, May 1995

- ◆ Following acceptance of the highest offer, at £27.18 million, the successful bidder for the Irvine portfolio sought to reduce the purchase price to £24.32 million, or alternatively to defer payment of the original offer price by one year. This was unacceptable to the Corporation and, after consulting the Department, they set a deadline for this company to stand by their bid.
- ◆ When they did not do so the Corporation invited the previous underbidders to submit new offers. The Corporation accepted the highest bid resulting of £28 million, although this was subsequently reduced by £1 million to take account of changes in tenancy information and other problems disclosed during final investigations by this purchaser.

Source: National Audit Office examination of 37 disposals

Difficulties with sales such as late or withdrawn bids were rare, arising in four cases examined by the National Audit Office. Experience from one early case in Cumbernauld helped achieve a satisfactory outcome when difficulties arose in some later sales.

- 22 The Corporations gave some form of concession in six cases. This is not an unusual feature of development cases, and the concessions were justified by broadly quantified but clear development benefits, eg retention of jobs, though in no case was there explicit analysis of costs and benefits (see Figure 13).

Figure 13: Findings on development cases**Livingston Development Corporation - sale of factory at Hunter Road for £2,071,000 April 1993**

Entry to the property was given in May 1992 but the purchase price was not received until April 1993. As a result the purchaser enjoyed rent free occupation of the property for 11 months, estimated by the National Audit Office to be worth £180,000. The Corporation commented to the National Audit Office that the delay in payment was reasonable because the property required roof repairs. Also had the company been leasing the property then a one year rent free period would have been reasonable.

This concession was recognised to be part of a package promoting inward investment, with the creation of 30 new jobs.

Livingston Development Corporation - sale of factory at Fleming Road for £950,000 December 1992

Immediately prior to sale the Corporation accepted the previous tenant's renunciation of a 25 year lease, in exchange for one year's penalty payment of £75,000. The National Audit Office estimated this amounted to a concession of at least £75,000, since the Corporation advised the National Audit Office that they might normally have expected to require payment of at least two years rent to permit surrender. The Corporation advised the National Audit Office that the concession was provided to encourage continued investment in the town by a major communications sister company who subsequently increased employment there from a few hundred to 1,400, and because the outgoing tenant left building improvements valued at more than £100,000. Also, within one year from the surrender of the lease, the Corporation found another occupier for the vacated property now employing some 390 people.

Livingston Development Corporation - sale of premises at Grange Road for £1,030,000 January 1993

The purchasers were allowed to occupy the premises under licence and rent free between January 1992 and January 1993. This was because the Corporation encountered severe legal difficulties in securing a clear title to convey to the purchaser; and the purchaser required title in order to obtain funding for their investment in the site. Previous transactions involving the title to this property had not revealed any problem with the title. The National Audit Office estimated the costs of this concession in deferred payment/lost rent terms was some £85,000. The Corporation advised the National Audit Office that the purchaser had created 250 jobs and, had they been leasing the property, a one year rent free period would have been reasonable.

Livingston Development Corporation - sale of premises at Kirkton South for £2,225,000 March 1995

The Corporation permitted the previous tenant of these premises to surrender their lease on payment for dilapidations some £120,000 below their estimated full cost. The Corporation advised the National Audit Office that they granted this concession to help secure the company's expansion in Livingston. Also the new occupier and purchaser of these premises was to make alterations to the building which removed the need to carry out some of the dilapidation work otherwise necessary.

Cumbernauld Development Corporation - sale of factory premises at Grayhill Road for £2 million March 1995

The Corporation accepted surrender of a 25 year lease from the tenants, an inward investor, to allow them to move to smaller premises in the town and secure viability. The site was valued at £3,670,000 with the company as tenants, though it was sold to Scottish Enterprise for £2 million as void - an apparent loss of some £1.67 million.

The Corporation considered that if they had not permitted the surrender of the lease and transfer there was a significant risk that the company would cease their activities in Scotland. The company now employ 170 staff in the town compared with 125 in 1994.

Cumbernauld Development Corporation - sale of factory at Drum Mains Park for £1,500,000 February 1995

The tenant, an inward investor, notified the Corporation in June 1993 that they intended to close the plant. Following discussion the Corporation agreed to extend a rent free period of occupation from July 1993 to February 1995 at which point the property was to be sold to Scottish Enterprise. The National Audit Office estimated this concession was worth £194,000 to the company. The company have continued operations in Cumbernauld and employment at the factory has subsequently increased from 40 to 80 jobs.

Source: National Audit Office examination of 37 disposal cases

In the six cases where Corporations gave some form of concession this was justified by broadly quantified but clear development benefits, eg retention of jobs. Neither Corporation concerned made explicit analysis of the costs and benefits involved.

- 23 The National Audit Office concluded that while it was reasonable not to require competition for development cases, this did not reduce the need for a pre-sale valuation which was an important way of benchmarking the sales. The Department accepted this and in December 1995 they clarified their earlier guidance. For remaining sales linked to ongoing development, Corporations are required to obtain formal pre-sale valuations. And in any case where a Corporation proposed to reach agreement on a sale price at less than the pre-sale valuation they had to record the full value for money justification.

Did the Corporations apply clawback where appropriate?

Initially Corporations anticipated that purchasers would strongly resist the Department's requirement to apply clawback and that this might have a potentially detrimental effect on sales. In 1993 the Department clarified and expanded their guidance, which Corporations subsequently applied successfully.

- 24 The Committee of Public Accounts has recommended the use of clawback in all cases where real doubts exist about the basis for valuation and the possibility of wind-fall profits to the purchaser. The Committee has noted that clawback should not be so frequently used as to interfere with the orderly and timely disposal of assets and it should be considered on its merits in each case (Appendix 3 Issue 9).
- 25 The Department's guidance required Corporations to include clawback provisions only to secure a share of any increased value arising from a change in the planning status of the property following disposal - the most likely reason for significant increase in value. Exceptionally, subject to the Department's approval in major cases, Corporations could dispense with a clawback clause where their marketing agents took the view that such provision was inappropriate or would have a significant adverse affect on the sale price.
- 26 In practice, Corporations and their agents encountered some difficulties in applying the guidance, with some bidders for industrial property with limited scope for change of use expressing concern regarding the application of clawback and they raised the matter with the Department in 1992. In one case, the sale of the Westfield/Lenziemill industrial package in August 1993, Cumbernauld Development Corporation accepted that they would not apply clawback because the preferred bidder was not prepared to complete the sale on any other basis.
- 27 Following further experience and detailed consideration the Department provided clarification of their guidance and advice on its application in August 1993. The National Audit Office examined one case where clawback secured an additional payment of £2.45 million (51 per cent of the uplift in value). In a second case clawback did not apply when a buyer sold on a property without any change in its planning status to another party for £0.4 million more than the purchase price (Case 4 at page 35).

Did the Corporations achieve the best price and avoid concluding sales at any price?

For major sales completed between April 1992 and March 1996 proceeds at £293 million, exceeded the aggregate estimated value of the properties, £280 million. In 32 of 37 cases the National Audit Office examined Corporations achieved satisfactory or better prices compared with valuations and other criteria. And in cases where Corporations sold properties below valuation, almost three-quarters of the sales were completed after open market competition, ie where Corporations would normally accept the highest available offer after wide marketing. In the remaining five cases the National Audit Office had doubts about the price achieved.

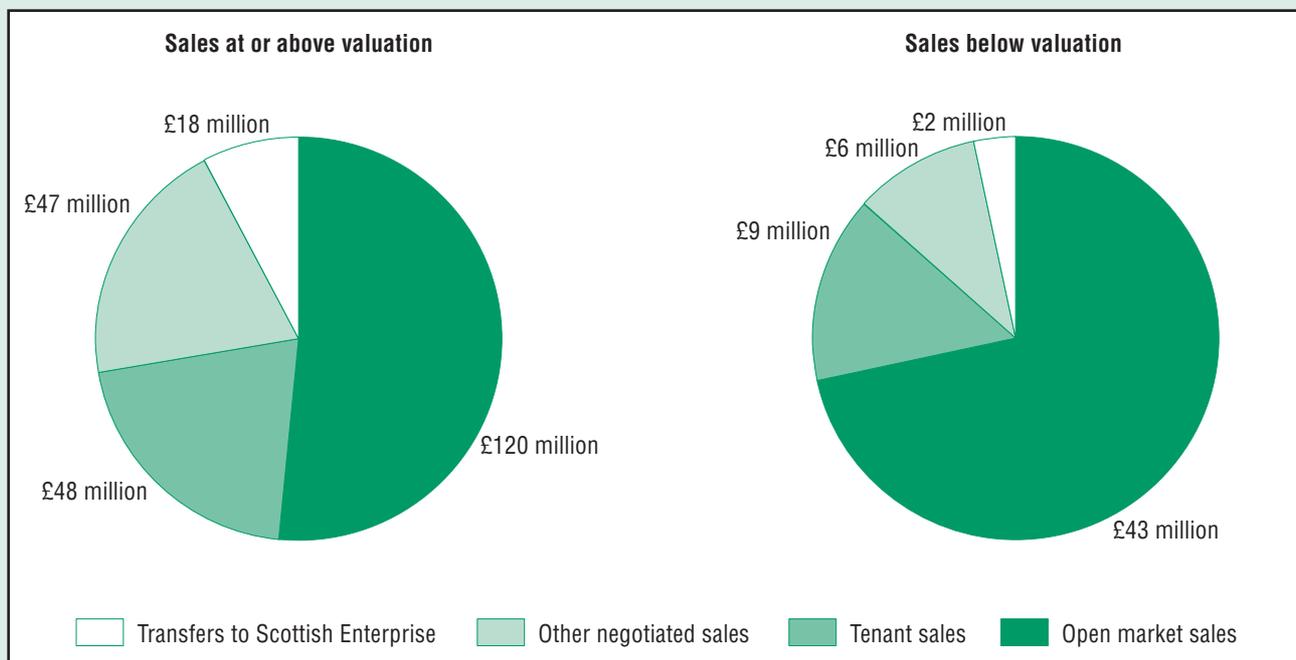
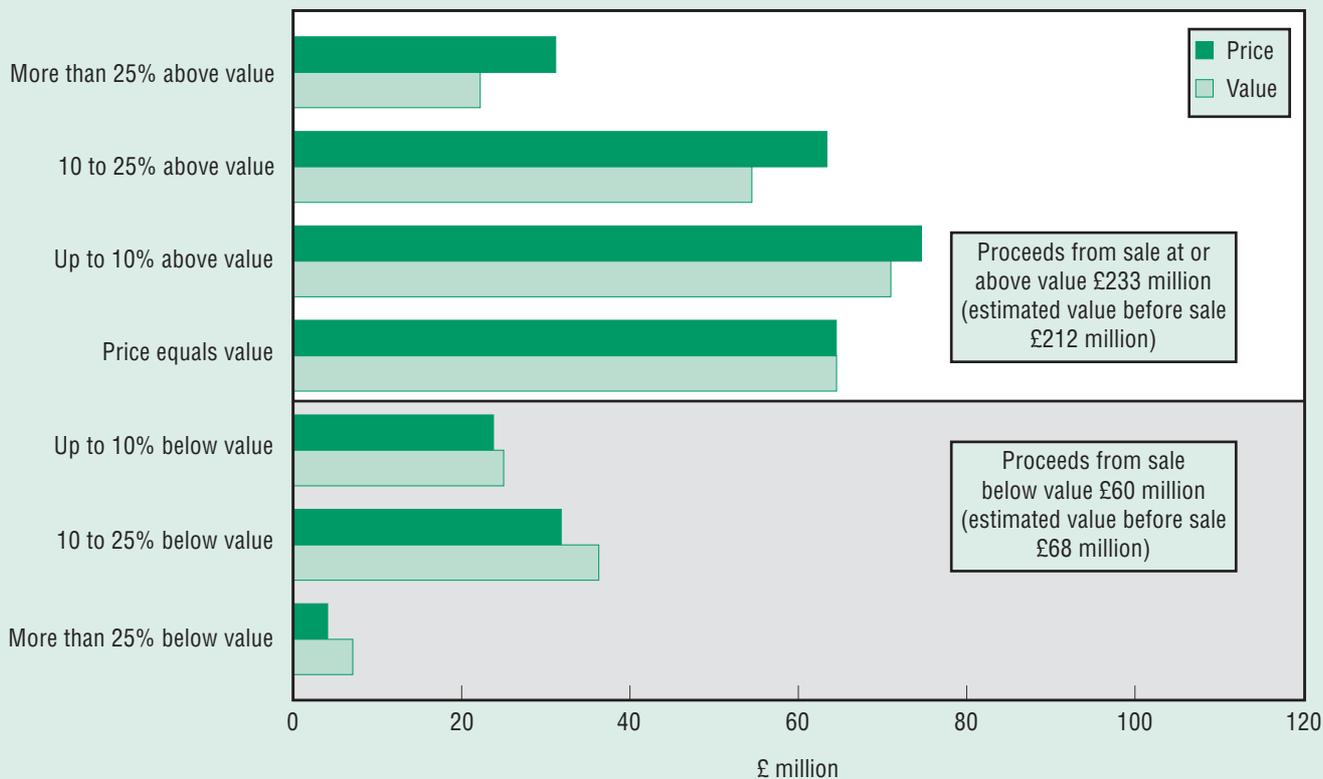
- 28 For major sales proceeds at £293 million exceeded the aggregate estimated value of the properties, £280 million. For most of these sales - 80 per cent by value - proceeds equalled or exceeded the estimated value at the time of sale (Figure 14).
- 29 Although Corporations completed 49 sales for prices below estimated values, in many cases the variance was small. And almost three-quarters of sales at prices below value were completed after competition, ie in circumstances where Corporations would normally accept the highest available offer after wide marketing (see Figure 14).
- 30 For 32 of the 37 sales they examined, against the criteria identified at Figure 15 on page 31, the National Audit Office concluded that the price achieved by Corporations was satisfactory or better (two examples are Cases 1 and 2 on page 32-33). In the remaining cases the circumstances of the sale raised questions about the price achieved (see, for example, Cases 3 and 4 at pages 34-35).

Were sales subject to review by internal or external audit?

The Department's sales guidance required examination of sales by the Corporations' internal and external auditors. There was no internal audit of sales in Cumbernauld and Livingston and only limited coverage in Irvine. The external auditors of the five Corporations have reported no significant shortcomings.

- 31 The Department's guidance included the requirement for Corporations' internal audit to scrutinise disposal procedures and transactions.
- 32 Only Glenrothes and East Kilbride had arranged for their internal auditors to scrutinise sale transactions, with generally satisfactory results. In Cumbernauld internal audit had not examined disposals at all. In Irvine some exception checks were made by internal audit for the major package disposal of all of the Corporation's industrial property, and a systems audit was planned for the end of 1995-96. This was carried out and there were no adverse findings. For

Figure 14: Analysis of sale price against valuation - all major sales April 1992-March 1996



Source: Corporations' returns to the National Audit Office of sales from April 1992 to March 1996

Note: excludes £1 million sales for which valuation data is unavailable

For major sales proceeds from disposals (£293 million) exceeded the aggregated estimated value of the properties (£280 million). Although around one-fifth of sales were completed at prices below the previous estimated value of the property, three quarters of these followed competition, where Corporations would normally accept the highest available offer after wide marketing.

Figure 15: Criteria for assessing price

◆ Number and quality of bids etc

Generally full exposure to the market and acceptance of the highest offer will achieve the best price. Few bids and/or bids from organisations without a strong track record could indicate problems exposing the property to the market and therefore with the price achieved.

◆ Sale price compared to valuation

Where property is sold at a price below valuation there may be a poor deal, a deliberate concession by the vendor or an error in the valuation.

◆ Management of the sale process

Factors such as an ill-considered sale strategy or poor performance in marketing may result in a badly timed sale or loss of confidence in the product amongst prospective purchasers, with commensurate impact on the price achieved. For negotiated sales, weak preparation may also increase the risk of a poor deal.

◆ Professional knowledge and experience from Richard Ellis

The National Audit Office's property advisers were able to assess sale results in individual cases against their professional knowledge and experience.

◆ Resale evidence

Property changing hands after disposal by Corporations may indicate that the original disposal achieved a weak price.

The National Audit Office considered a range of factors in assessing whether Corporations could reasonably be expected to have achieved best price in individual disposal cases.

Livingston internal audit had examined disposal receipts but only for the purposes of verifying the correct accounting treatment on behalf of the Corporation's external auditor.

- 33 The Department, on behalf of the Secretary of State, is responsible for appointing the Corporations' external auditors who are major firms of chartered accountants. The Department's terms of reference state that these auditors' work should include tests designed to check that asset disposals have been undertaken in accordance with the Department's guidance and that sales prices represent best value for money within the context of that framework. External auditors of all five Corporations have reported no significant shortcomings in this area.

Case 1

Livingston Development Corporation - sale of Houston Industrial Estate for £11,585,000 September 1994



Houston Industrial Estate Livingston, from the south west.

This case illustrates the benefits of an open market sale in positive market conditions, with sale at almost £3 million above the asking price, and the importance of thorough pre-sale preparations which enabled rapid completion of the sale. Though the Corporation did not have available information on industrial buildings allowances at the outset they provided this in time for bidders to allow for this in their offers.

Valuation

1. The Corporation did not obtain a formal pre-sale valuation though their selling agents recommended an asking price of £8.75 million in June 1994.

Sale method

2. Sold on the open market by closed tender. Marketing began in June 1994 and the Corporation received 12 informal bids by the closing date of 29 July in the range £8 million to £11.5 million. The Corporation invited the four highest bidders to submit formal offers by a second closing date of 26 August. Prior to the second closing date the Corporation provided these bidders with supplementary data on the properties, including information on industrial building allowances commissioned from accountants. The three highest bidders increased their bids by between some £0.1 million and £0.6 million at this second stage, while the fourth reduced their bid by some £1.4 million.

Sale price and completion

3. The Corporation accepted the highest offer of £11,625,000. Pre-sale preparations included relevant property enquiries and an environmental audit of the site. As a result, the Corporation were able to complete the sale formalities in little over a month, although they accepted a small price reduction of £40,000 to take account of necessary dilapidation works required by the purchaser.

Case 2

Irvine Development Corporation - sale of Irvine industrial property for £27 million, May 1995



South Newmoor Industrial Estate Irvine.

Part of the largest package of industrial property sold by a New Town Development Corporation.

This was by far the largest single sale completed by any Corporation. The Corporation marketed the property effectively, overcame completion difficulties which arose and were able to secure a price almost £2 million above the pre-sale valuation.

1. In December 1993 the Corporation, with the agreement of the Department's Advisory Group, decided to market all their industrial property as a single package following the Secretary of State's decision to being forward wind-up to December 1996.

Valuation

2. The Corporation's advisers indicated a pre-sale valuation for the industrial portfolio of £25,300,000 on 8 August 1994.

Sale method

3. Sold on the open market by closed tender. Following informal approaches to prospective purchasers marketing commenced in May 1994 with presentations to interested parties and wide distribution of sales brochures. Updated sales particulars were issued prior to the closing date for informal offers to take account of the latest tenancy and income alterations.

4. Prospective purchasers were also advised at that time that information on industrial buildings allowances was available on request. No requests were received prior to the submission of informal tenders. Notwithstanding after the receipt of informal bids but prior to inviting formal tenders the Corporation made available to all prospective bidders information on industrial building allowances prepared by their accountancy advisers and accepted by the Inland Revenue.

Sale price and completion

5. On the closing date of 27 October 1994 the Corporation received six informal tenders in the range of £25,000,000 to £27,180,000. When inviting formal tenders the Corporation excluded the lowest tender as it was below the pre-sale valuation. Of the five invited to tender formally only four did so by the closing date of 11 November 1994 and the tenders ranged from £25,700,000 to £27,180,000.

6. The Corporation wished to accept the highest offer of £27,180,000. The Corporation's thorough pre-sale preparation ensured that legal completion procedures proceeded smoothly until January 1995, when the intended purchaser sought to reduce or defer payment of the agreed offer price.

7. After consulting the Department the Corporation set a deadline for this company to stand by their bid. When they did not do so the Corporation invited the previous under-bidders to submit new offers. The Corporation accepted the highest bid resulting, £28 million, though during detailed negotiations they agreed a reduction of £1 million in this price to take account of the results of this purchaser's environmental audit and an audit of the leases.

Case 3

Livingston Development Corporation - tenant sale of three factories at Firth Road for £9,415,000 December 1994



Firth Road Livingston, with the three factories sold indicated.

This case illustrates the balance to be struck between encouraging development of new employment in the town and maximising sale proceeds where an option to purchase prevents a competitive sale. It is also an example of the Corporation not obtaining an accurate quantification of the potential worth of industrial building allowances prior to sale negotiations with the tenant.

1. The tenant, the UK subsidiary of a major overseas manufacturer, had occupied the property for seven years. The lease gave the tenant an option to purchase the factories at the higher of their full open market value or total cost of construction.

Sale method and valuation

2. The Corporation negotiated sale with the tenant and their agents following the tenant's decision to exercise the purchase option. The Corporation did not commission sales or valuation advice from agents. The total cost of construction was some £9 million while the District Valuer's (Lothian) accounts valuation at March 1994, valued the properties at £10 million taking account of the tenant option clause.

3. The District Valuer was not asked for an additional formal valuation but in August 1994, during negotiations between the Corporation and the tenant, the District Valuer upon request advised the Corporation that for a portfolio type valuation for sale purposes of the three factories together with the ongoing purchase of a fourth factory that discounting his valuation by five per cent (ie to £9.5 million) to reflect quantum would not be unreasonable. The Corporation did not seek the District Valuer's advice on the sale price subsequently agreed with the tenant, £9.315 million plus £100,000 for deferred payment of the purchase price.

4. Industrial building allowances were known to be of interest to the tenant purchaser. After the main terms of the sale had been agreed in December 1994 the purchaser sought and received from the Corporation information to enable the allowances to be quantified. The District Valuer's March 1994 accounts valuation report did not make explicit reference to allowances because he was of the opinion that open market comparisons would implicitly reflect the market's assessment of Industrial Building Allowances. Subsequently, Price Waterhouse, advising the National Audit Office, estimated that industrial building allowances of some £7.6 million with a net potential tax saving of £1.2 million, could have been available to a purchaser of this property able to take advantage of such tax allowances.

Sale completion

5. Settlement of the purchase price was deferred until April 1995, three months after the legal transfer of the property in December 1994, with £100,000 included in the purchase price in recognition of this. This was some £75,000 below the cost to the Corporation of deferring payment, based on prevailing interest rates.

6. The Corporation commented to the National Audit Office that the occupier of these factories, a major overseas investor, had created over 600 jobs in Livingston and in negotiating this sale it was felt that a fine balance had been achieved between maintaining a good working relationship with the company and optimising sales proceeds.

Case 4

**Cumbernauld Development Corporation - tenant sale of factory at 1 Drum Mains Park for £1,500,000
October 1994**



1 Drum Mains Park Cumbernauld, bought by the tenant for £1.5 million and resold under a sale and leaseback agreement for £1.9 million in March 1995

The Corporation sold this property to the tenant in 1994 at a price set by an option to purchase granted when the tenant first occupied the property in 1993. It is an example of a case where policy precluded the Corporation from clawing back any of the £0.4 million price increase achieved on its resale by the purchaser five months later because there has been no change in the planning status of the property.

1. In August 1993 the Corporation granted a 25 year lease to a new tenant company. Initial rental was £184,000 a year but, as a concession to encourage the company, no rent was payable until June 1995. The lease also provided the company with an option to purchase the property at £1,575,000 at April 1995.

Valuation

2. The District Valuer's (Motherwell) accounts valuations of the property were £1,220,000 (March 1993) and £1,375,000 (March 1994). The Corporation fixed the price in the lease in August 1993 at £1,575,000 reflecting their professional judgement of the open market value of the property in April 1995, though there was no record of this assessment. There was no requirement for the Corporation to seek an external valuation in setting the option price.

Sale method and completion

3. In 1994 the Corporation accepted the company's proposals to bring forward exercise of the purchase option. Recognising the earlier receipt of the purchase price, the Corporation agreed terms leading to the sale of the property to the tenant for £1.5 million in October 1994. This price was estimated to exceed any realisable open market value at the date of sale.

4. The National Audit Office established that in March 1995 the company resold and leased back the factory from a finance company, at a sale price of £1.9 million. Under the terms of the lease back, in the period to March 2000 the date of the first rent review, the company will pay almost exactly the same rent as they would have otherwise paid to the Corporation from June 1995.

5. Price Waterhouse, advising the National Audit Office, established that industrial building allowances of £1.2 million were available for this property, with a net potential tax saving of £0.2 million. The Corporation had not considered this factor in fixing the sale price of the property. In July 1996 the Corporation established from the property agents concerned that the availability of allowances did not form any element of their valuation on behalf of the second purchaser, and on this basis did not appear to have influenced the higher price paid for the property in March 1995.

Appendix 1

Disposal of assets by Scottish new towns: Chronology of key events

1988 May	Secretary of State initiates review of the five Scottish New Town Development Corporations, to consider whether Corporations have completed their development task, and the forward programme for wind-up. In October 1988 the Government Green Paper “The Scottish New Towns - Maintaining the Momentum” was issued.																		
1989 July	Following consultation, the government’s White Paper “The Scottish New Towns - The Way Ahead” announces proposals for winding-up the Corporations. These envisage the making of wind up orders three and four years before each Corporation ceases operations with completion by 1999:																		
	<table border="0" style="margin-left: auto; margin-right: auto;"> <thead> <tr> <th style="text-align: left;"></th> <th style="text-align: center;">Orders to be made</th> <th style="text-align: center;">Corporation cease operations</th> </tr> </thead> <tbody> <tr> <td style="text-align: left;">East Kilbride</td> <td style="text-align: center;">1991</td> <td style="text-align: center;">1995</td> </tr> <tr> <td style="text-align: left;">Glenrothes</td> <td style="text-align: center;">1991</td> <td style="text-align: center;">1995</td> </tr> <tr> <td style="text-align: left;">Cumbernauld</td> <td style="text-align: center;">1993</td> <td style="text-align: center;">1996</td> </tr> <tr> <td style="text-align: left;">Livingston</td> <td style="text-align: center;">1995</td> <td style="text-align: center;">1998</td> </tr> <tr> <td style="text-align: left;">Irvine</td> <td style="text-align: center;">1996</td> <td style="text-align: center;">1999</td> </tr> </tbody> </table>		Orders to be made	Corporation cease operations	East Kilbride	1991	1995	Glenrothes	1991	1995	Cumbernauld	1993	1996	Livingston	1995	1998	Irvine	1996	1999
	Orders to be made	Corporation cease operations																	
East Kilbride	1991	1995																	
Glenrothes	1991	1995																	
Cumbernauld	1993	1996																	
Livingston	1995	1998																	
Irvine	1996	1999																	
1992 February	Orders made for East Kilbride and Glenrothes Development Corporations. Wind-up to commence on 1 March 1992 and to be completed by 31 December 1995.																		
March	The Department issue guidance to all Corporations on wind up, including the disposal of remunerative assets (see Appendix 2). The Department also establish an advisory group to oversee the sale of commercial and industrial property by Corporations.																		
July to November	East Kilbride, Cumbernauld and Glenrothes Corporations appoint professional property advisers to assist with asset disposals.																		
1993 January	Irvine Corporation appoint professional property advisers to assist with asset disposals.																		
year to 31 March	Corporations complete sales of commercial and industrial land and property of £39 million.																		
August	Livingston Corporation appoint professional property advisers to assist with asset disposals, although different property advisers had been appointed to deal with the sale of Brucefield in 1991.																		

1993 December	Following consultation, Secretary of State announces that the wind up timetable for Livingston and Irvine Corporations is to be accelerated. Orders made to commence the wind-up of these Corporations and Cumbernauld on 1 January 1994 and be completed on 31 December 1996.
1994 year to 31 March	Corporations complete sales of commercial and industrial land and property of £79 million.
1995 year to 31 March	Corporations complete sales of commercial and industrial land and property of £91 million.
31 December	East Kilbride and Glenrothes Development Corporations cease operations.
1996 year to 31 March	Corporations complete sales of commercial and industrial land and property of £120 million
5 April	Dissolution of East Kilbride and Glenrothes Development Corporations.
To 31 December	Cumbernauld, Livingston and Irvine Corporations complete sales of commercial and industrial land and property of £90 million and cease operations on 31 December.

Appendix 2

Study methodology

- 1 The study was carried out by a joint team from the National Audit Office and Richard Ellis property consultants. Richard Ellis were appointed in consultation with the Department's professional estates adviser following competitive tender.

Structured interviews

- 2 During October 1995, the study team interviewed senior managers at each Corporation and their external property advisers. The team also interviewed members of the Department's disposals advisory group. The interviews helped to identify the strengths and weaknesses of the Corporations and the Department in the preparation, planning and execution of asset disposals. The main areas addressed were:
 - a) the development of the Department's guidance and strategy on disposals;
 - b) Corporations' sale strategies, other pre-sale preparations and the role of professional advisers; in particular, action by Corporations geared to improving marketability and the prices achieved for properties;
 - c) marketing of disposal packages;
 - d) valuation practices;
 - e) sale methods and outcomes achieved in individual cases.

Case examination

- 3 The study team examined in depth a sample of 37 mainly high value disposals out of the total of 283 major sales from April 1992 to March 1996.
- 4 The sales examined in detail realised £176 million. The sample selected was not statistically representative but matched broadly the pattern of disposals by each Corporation in terms of the method of sale and the type of property sold, and there was an emphasis on higher value and negotiated sales. Ten of the 13 completed major package sales were reviewed, and the sample represented 53 per cent of the total value of disposals made to 31 March 1996 (Figure 16).
- 5 In each case the team reviewed the Corporation's management of the disposal against current professional practice and reviewed whether the price and outcome achieved appeared satisfactory. The cases examined are listed in Figure 17.

Statistics for major sales

- 6 In addition, the team analysed key statistics provided by the Corporations and the Department for the other 246 major sales completed up to March 1996. This confirmed that the sample examined in depth was a reasonable basis for assessing Corporations' performance, and provided the basis for wider analysis on issues such as methods of sale and sale valuations.

Industrial buildings allowances (IBAs)

- 7 In January 1996, in the light of their preliminary examination of the Corporations' treatment of IBAs the National Audit Office commissioned Richard Ellis to carry out further analysis of this aspect of seven high value industrial property disposals. The seven cases are identified in Figure 17. Richard Ellis, with the National Audit Office's approval, commissioned Price Waterhouse to provide specialise accountancy advice on the potential amount of allowances available to prospective purchasers. The results of this work are described in Figure 18 in Appendix 4.

Figure 16: Sales of New Town commercial, industrial land and property assets examined by the National Audit Office

a) Major sales examined by the National Audit Office

	Sales examined by the National Audit Office			All major sales		
	Number of cases	Value (£ million)	% of sample (by value)	Number of cases	Value (£ million)	% of population (by value)
Open market	15	123	70	68	164	56
Tenant	9	37	21	77	57	19
Scottish Enterprise	6	8	4	19	20	7
Negotiated	7	8	5	119	53	18
All sales completed between 1992 and 1996	<u>37</u>	<u>176</u>	<u>100</u>	<u>283</u>	<u>294⁽¹⁾</u>	<u>100</u>

b) Reconciliation of major sales to total sales programme

	£ million
Major sales completed between 1992 and 1996 (part a) above)	294 ⁽¹⁾
Sales below £50,000	36
Total sales to March 1996	<u>330</u>
Value of sales April - December 1996	<u>90</u>
Total value of sales programme	<u>420</u>

Note 1: At the National Audit Office's request Corporations and the Department provided key statistics including receipts and valuation data for all major sales completed between April 1992 and March 1996. Major sales were defined as those generating proceeds of more than £50,000, though some Corporations also provided additional data for smaller transactions. This data formed the basis of the sample population.

The National Audit Office examined sales with a value of £176 million, 53 per cent of the value of all major sales completed between 1992 and March 1996.

Figure 17: Property disposal transactions examined by the National Audit Office

	Sale date	Sale price £000	Method of sale
Livingston			
Brucefield Industrial Estate	December 1991	10,212*	Open market
Houston Industrial Estate	September 1994	11,585	Open market
Firth Road	December 1994	9,415*	Tenant option sale
Filling Station, Town Centre	July 1993	500	Negotiated sale to third party
1 Hunter Road	October 1993	2,071	Negotiated sale to third party
1 Fleming Road	February 1993	950	Transfer to Scottish Enterprise
1 Kirkton South	March 1995	2,225	Negotiated sale to third party
1 Grange Road	September 1994	80	Negotiated sale to third party
25 Grange Road	January 1993	1,030	Negotiated sale to third party
Eliburn NW3	March 1995	530	Scottish Enterprise
Fairways	September 1986	1,236	Open market
Cumbernauld			
Westfield/Lenziemill Industrial Estate	September 1993	9,250*	Open market
Grayshill Road	March 1995	2,000	Transfer to Scottish Enterprise
1 Drum Mains Park	October 1994	1,500*	Tenant option sale
3 Drum Mains Park	February 1995	1,500	Transfer to Scottish Enterprise
Wardpark/Blairlinn Industrial Estate	May 1994	5,250	Open market
Glenrothes			
Whitehill/Viewfield Industrial Estate	January 1994	3,900	Open market
Southfield Industrial Estate	August 1994	5,150*	Open market
Flemington Road	September 1993	3,250	Tenant option sale
V9 Viewfield	September 1994	1,750	Tenant option sale
Foxtan Drive	March 1994	560	Transfer to Scottish Enterprise
Kingdom Shopping Centre	September 1995	6,200	Negotiated sale to tenant
Eastfield Industrial Estate	April 1995	6,227	Open market
East Kilbride			
Kingsgate Retail Park	April 1993	12,026	Open market
College Milton Industrial Estate	February 1994	12,300	Open market
Kelvin Industrial Estate	November 1994	17,535*	Open market
Abercrombie House	March 1993	5,250	Negotiated sale to tenant
Site 32, Stewartfield	November 1993	1,020	Open market
Olympia Centre	March 1995	8,900	Tenant option sale
Manson Place	November 1993	535	Transfer to Scottish Enterprise
Arrol Place	September 1993	1,373	Negotiated sale to tenant
Redwood Avenue	August 1994	915	Open market
Irvine			
Industrial Portfolio	May 1995	27,000*	Open market
Chalmers Place	March 1995	1,927	Transfer to Scottish Enterprise
Lawthorn Farm	April 1993	310	Open market
Lawthorn 6A	February 1995	465	Open market
Kelvin Avenue	August 1992	125	Negotiated sale to tenant

Source: National Audit Office

Note: * = Cases selected for further examination re industrial building allowances

The study team examined in depth a sample of 37 disposal transactions completed between April 1992 and mid-1995, representing 53 per cent of the total population by value. In addition, Richard Ellis and Price Waterhouse reviewed the treatment of industrial building allowances in the marketing and valuation of seven high value industrial property disposals.

Appendix 3

Summary of PAC recommendations on disposal of assets and the Department's disposal guidance

Issue	PAC recommendation	Department's disposal guidance
1. Strategy and preparation for sale	<p>The success of the disposals programme will depend heavily on the quality of professional judgements but it is important that these are exercised within the framework of a well considered strategy, supported by reliable information and sound procedures and controls. We endorse the principles for a comprehensive forward disposals strategy directed towards clear and specific disposal objectives, and fully implemented without delay.</p> <p>(10th Report 1986-87, para 22(ii), HC 234)</p>	<p>Development Corporations must prepare a strategy for the disposal of assets ... (with) regard to the requirements to generate specific levels of annual income from disposals in order to make any payments to the Secretary of State that may be required prior to dissolution.</p> <p>(1992 guidance para 4.1)</p> <p>Corporations must put the appropriate planning approval into place prior to disposal.</p> <p>(1992 guidance para 4.7.1)</p> <p>Corporations should commission a structural and environmental survey which would be made available to the bidders... (and) used to inform the amount of expenditure on maintenance and repairs of premises in order that an accurate estimate of these costs can be given to purchasers.</p> <p>(Department's letters to Corporations, December 1993 and July 1994)</p>
2. Method of Sale	<p>Assets should be exposed to the market unless there are compelling reasons to the contrary. All exceptions to competitive tender, including sales to tenants, should be subject to strict controls.</p> <p>(10th Report 1986-87, para 12, HC 234)</p>	<p>Assets must be sold for the best consideration reasonably obtainable. Disposal should involve full exposure to the market, unless there are specific reasons why a more restrictive approach is likely to achieve a better price ... The Department's approval is required to any proposed departure from full exposure to the market.</p> <p>(1992 guidance para 4.7.2)</p>
3. Sales to Tenants	<p>We recommend* ... agents are employed to negotiate with tenants ... and aim to achieve 50 per cent share of marriage values.</p> <p>(10th Report 1986-87, para 15, HC 234)</p> <p><i>* Note: the Government response was that the use of agents in such circumstances would be left to the discretion of the body concerned.</i></p>	<p>In considering sales to existing tenants Corporations must have regard to the effect of the sale on the price obtainable for the estate as a whole ... where it is appropriate to sell to the sitting tenant negotiations towards achieving the best consideration reasonably obtainable should be conducted against a full knowledge of market value ... unless there have been recent open market sales of similar properties an open market valuation should be obtained.</p> <p>(1992 guidance paras 4.11 and 4.12)</p>

continued ...

Issue	PAC recommendation	Department's disposal guidance
4. Marketing	<p>Departments should ensure that marketing strategies are validated before a sale is undertaken.</p> <p>(9th Report 1990-91, para 3(iv), HC 119)</p>	<p>Where it is appropriate to sell a property to the sitting tenant ... Corporations should aim for at least a 50 per cent share when conducting marriage value negotiations ... but should also take account of the possibility that a higher percentage may sometimes be achievable.</p> <p>(1992 guidance para 4.13)</p>
5. Sale Conduct	<p>... all offers received prior to a binding legal agreement being entered into should be thoroughly investigated and the bidders given the fullest opportunity to establish their financial credentials.</p> <p>(12th Report 1990-91, paras 3(i) 3(ii), HC 374)</p>	<p>Development Corporations should normally use agents to handle disposals on the open market ...</p> <p>Agents may also be in a good position to advise on the best approach in marketing particular assets, on the methods likely to achieve best prices and on the conduct of any subsequent negotiations.</p> <p>(1992 guidance para 4.7.4)</p> <p>Disposals must be conducted and seen to be conducted in a fair and equitable manner ... Any private negotiations after open marketing should always be fully documented and subject to careful review in order to minimise the risk of impropriety and to ensure that the consideration obtained is and fully justifiable.</p> <p>(SOID guidelines, para 4.7.3)</p> <p>... a late, or revised, bid must be considered carefully. The duty to the taxpayer of receiving the best possible price needs to be balanced against the risk of original bidders withdrawing their offers because of the delay and the risk of accusation of impropriety in the marketing process. Any such bids must be discussed with the Scottish Office ... before the sale is finalised. Late or revised bids can only be considered where missives have not been concluded ...</p> <p>(Department's letter to Corporations, December 1994)</p>
6. Valuations	<p>We underline the importance that sales are backed up by up-date valuations, particularly in marriage value transactions and in cases where delays occur in the course of negotiations.</p> <p>(10th Report 1986-87, para 17, HC 234)</p>	<p>A formal valuation of the assets, together with any available comparables, should be recorded before the disposal procedure commences. Where disposals become protracted or the market shifts significantly, a revaluation should be undertaken.</p> <p>(1992 guidance para 4.21.1)</p>
7. Costs of Sale	<p>Departments must give careful consideration in advance of sale campaigns to fix budgets and target marketing expenditure towards identified sales objectives.</p> <p>(34th Report 1987-88, para 3(ix), HC 211)</p>	<p>Corporations appointed agents after open competition.</p> <p>(1992 guidance para 4.7.4).</p>

continued ...

Issue	PAC recommendation	Department's disposal guidance
8. Monitoring	<p>Where responsibilities have been properly delegated the degree of detailed monitoring by the sponsoring department is a matter of judgement ... it will be increasingly important to keep such judgements under review in ways that do not undermine initiative or encourage "second guessing" of decisions taken by responsible management.</p> <p>(12th Report 1990-91, para 3(v), HC 374)</p>	<p>The Department and its advisers are to take a central role in the oversight and management of the disposal process across the five Corporations ... setting up an advisory group whose membership will be drawn from the Scottish Office and the Department's external consultants ...</p> <p>The group's main tasks include:</p> <ul style="list-style-type: none"> • advising on Corporations' asset disposal strategies; • monitoring the timing of sales, to avoid adversely affecting the property market; • to participate in the consideration of bids received in respect of assets or packages of assets valued at £4 million or more. <p>(1992 guidance paras 4.3 and 4.4)</p> <p>It is important that scrutiny of disposals procedures and transactions should form part of the remit of development corporations' Internal Audit. The terms of reference of the external auditors appointed by the Secretary of State will be clarified ... The object should be to ensure that any weaknesses in the procedures operated by the development corporation are identified and corrected.</p> <p>(1992 guidance para 4.22)</p>
9. Clawback	<p>Where land is considered to have development potential, serious consideration should be given to all the options for protecting the taxpayers' interest, including a separate sale or the use of clawback provisions.</p> <p>(13th Report 1989-90, para 3(v), HC 352)</p> <p>We encourage bodies to consider the clawback provisions over, say, five years in all cases where there are real doubts over the basis for valuation and the possibility of windfall profits to the purchaser.</p> <p>Clawback should not be so frequently used as to interfere with orderly and timely disposal.</p> <p>(10th Report 1986-87, para 20, HC 234)</p> <p>The case for selling property subject to clawback conditions should be considered on its merits in each case.</p> <p>(22nd Report 1993-94, para 3(v) HC 210)</p>	<p>Clawback provisions should be included ordinarily in the conditions of sale. If the Corporations' agents consider that inclusion of such a clause is inappropriate or will have a significant adverse affect on the sale price, the Corporation may seek the Department's agreement to dispensing with it... It is recommended that the normal period (for clawback) should be ten years ...</p> <p>(1992 guidance para 4.20 and Department's letter of August 1993).</p> <p>... it is not intended that (clawback) should be triggered simply because when the buyer sells on the subjects to another party a better price is achieved, ie without any change in planning status.</p> <p>(Department's letter to Corporations, August 1993)</p>

Appendix 4

Industrial buildings allowances

Availability of industrial buildings allowances

- 1 Under current taxation legislation^{*}, a capital allowance, known as industrial buildings allowance may be available to the holder of the “relevant interest” in an industrial building. The relevant interest is the interest (freehold or leasehold) in the building to which the person who incurred the original qualifying expenditure on the construction of the building was entitled when that expenditure was incurred. To qualify, the building must be in use for the purposes of a trade consisting of, broadly, manufacturing and other industrial activities. The allowance is available on the construction cost of the building, and is given as a deduction when computing taxable profits. For years up to 1986-87 and for 1992-93 an initial allowance was available on new industrial buildings at rates which varied up to 75 per cent of the construction cost. The balance of the construction cost over any initial allowance is given as an annual writing down allowance of four per cent of the construction cost (two per cent for premises constructed before November 1962).
- 2 If the relevant interest in a building is sold, subsequent allowances, calculated on the basis of the residue of expenditure, may be available to the purchaser (depending on their tax status, and capacity to utilise the allowances) over the period from the sale to the 25th anniversary of the first use of the building (50th anniversary for premises constructed before November 1962). On such a sale there may need to be a balancing adjustment to the allowances enjoyed by the seller before determining the residue of allowances available to the purchaser. The total of allowances available to successive holders of the relevant interest cannot exceed the original cost of the building.
- 3 The effect of these rules may be demonstrated by a simple example. Assume that a Development Corporation had in 1985 constructed a factory qualifying for allowances costing £500,000, and had sold these premises in 1995 for £600,000. The Corporation would have been entitled to an initial allowance at 50 per cent and writing down allowances at four per cent a year during its period of ownership, that is £450,000 in total. Upon sale, any allowances actually claimed are clawed back from the Corporation, which is called a “balancing charge”, and the purchaser is then entitled to allowances on the full construction cost of £500,000 over the remainder of the period up to the 25th anniversary of the first use of the building, that is 15 years. Because the allowances are given over 15 years the effective rate of relief for the purchaser increases to 6.7 per cent a year in this case.

* Principally, the Capital Allowances Act 1990

- 4 Provided that the premises continue to be used for a qualifying purpose the availability of any allowances to the purchaser depends on the way the sale is structured, in particular whether the relevant interest for the purpose of claiming any allowances is transferred or not. For example, rather than an outright sale of the entire interest in an industrial building, the owner could opt to sell the interest in a long say 999 year leasehold in the property. This would not of itself transfer the relevant interest for industrial buildings allowances purposes to the lessee, and the lessor would therefore be able to continue to enjoy the annual writing down allowance.

The potential tax consequences of industrial buildings allowances associated with sales of new town property.

- 5 In the period April 1992 to March 1996 Corporations have some £182 million of industrial premises. The National Audit Office did not quantify precisely the potential industrial buildings allowances position for Corporations' sales of industrial properties since 1992, which would require the detailed examination of each individual property. However, for six cases examined Price Waterhouse, advising the National Audit Office, quantified the potential net present value of the tax saving for the purchaser, assuming that the properties remained in use for qualifying purposes and the purchaser could make full use of the allowances.
- 6 The National Audit Office extrapolated from these results that utilisation of the allowances by purchasers of all properties sold by Corporations since 1992 could give a figure of, broadly, up to some £12 million to £16 million in total (see Figure 18). In doing so, the National Audit Office recognised that the six cases were not a statistically representative sample of all sales, and that allowances actually claimed are likely to be reduced by various factors including the tax status of the purchaser the extent to which the purchaser's taxable income is sufficient to enable use of the allowances, and the purchasers ceasing to meet any of the qualifying conditions for the use of the building.

Figure 18: Estimating the potential tax consequences of industrial building allowances associated with sales of new town property

Richard Ellis, with the National Audit Office's approval, commissioned Price Waterhouse to provide specialist accountancy advice on the potential amount of industrial building allowances available to prospective purchasers.

As part of this Price Waterhouse reviewed detailed allowance information provided by the Corporations on seven of the 37 cases examined by the National Audit Office. These were all sales of industrial property and generated receipts of £80 million, 44 per cent of all receipts from sales of industrial land and premises to date. In each case the Corporation transferred the relevant interest in the property to the purchaser and for their estimate Price Waterhouse assumed that any purchaser would be able to offset the allowances against corporation tax liabilities calculated at 33 per cent of profit. They discounted the resulting sum by 10 per cent a year from the year in which the benefit arose to arrive at the potential tax saving taking account of deferment.

On this basis, in the six cases examined where there was sufficient data to make an estimate, Price Waterhouse estimated the potential tax saving available at £7.4 million. In addition there were plant and machinery allowances attaching to fixtures and fittings in these properties which Price Waterhouse estimated to offer potential tax saving of £1.7 million.

In the period April 1992 to March 1996 Corporations sold £182 million of industrial properties. The Price Waterhouse results showed that where allowances could be estimated the potential tax saving represented between six and 15 per cent of gross sales proceeds, 10 per cent on average. However the Inland Revenue advised the National Audit Office that in practice they would expect many purchasers to have insufficient tax capacity to make full use of the allowances, and that for this reason the calculation of tax effect should be reduced by 20 per cent. The National Audit Office, taking all these factors into account, estimated that the potential tax saving from allowances associated with all industrial properties sold by Corporations might be of the order of up to £12 million to £16 million.

With advice from Price Waterhouse, the National Audit Office estimated that utilisation of industrial buildings allowances by purchasers of all properties sold by Corporations since 1992 could give a tax saving of up to, broadly, some £12 million to £16 million.