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## REVIEW OF CPO INDEMNITY PARTNER FOR MANSTON AIRPORT

To: **Extraordinary Cabinet – 29<sup>th</sup> October 2015**

Main Portfolio Area: **Leader of the Council**

By: **Director of Corporate Governance**

Classification: **Unrestricted**

Ward: **All**

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**Summary:** **To update Cabinet on the review of the appointment of a CPO indemnity partner for Manston Airport.**

### **For Decision**

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#### **1.0 Introduction and Background**

1.1 At the beginning of this report, it is worth setting out the main objective in seeking an indemnity partner. In the report to Council of the 11<sup>th</sup> December 2014, it said:

*'The objective of seeking an indemnity partner is to ensure that – if the Council determines to pursue a CPO – a viable airport comes into sustainable long-term operation as quickly as is reasonably possible without any residual cost to the Council.'*

1.2 On the 11<sup>th</sup> December 2014 Cabinet received a report on the soft-market testing exercise for an indemnity partner for a Manston Airport CPO. The report said that the Council had made every effort to work constructively with (RiverOak) including making several deadline extensions for submitting the information requested from the potential indemnity partner. The report and minute are attached as Annex 1 and Annex 2, respectively.

1.3 The Cabinet considered the following as relevant considerations, which remain relevant today:

- (a) The objective of seeking an indemnity partner (set out at 1.1 above).
- (b) The new owners intend to bring forward regeneration policies for the site.
- (c) The new ownership of the site and any proposals put forward would make it much more challenging to demonstrate an overwhelming case for compulsory purchase. It is important that the Council establishes on objective grounds, the financial status of any partner. The assessment must have due regard to the potential scale of the project and the need to demonstrate that resources are available to complete it.
- (d) Any indemnity partner needs to demonstrate the resources to acquire by private treaty well before the stage of seeking a CPO.
- (e) The experience in other local authorities emphasises the need to ensure a prospective indemnity partner has the resources in place to acquire the site and complete the development. Once the land transfers to the indemnity partner any redress for delay or non-completion could prove difficult to pursue. The main purpose of the CPO is for the authority to achieve a viable development, so the

status of the indemnity partner to deliver the development in its entirety is highly relevant.

1.4 On the 14th July 2015, Cabinet agreed:

1. The recommendation from Council on the 21st May 2015 to review its position in relation to the Manston Airport site, taking account of all the surrounding circumstances relating to an indemnity partner for a possible Compulsory Purchase Order;
2. To authorise that specialist legal and finance advice be obtained to determine whether RiverOak are a suitable indemnity partner in relation to a CPO for Manston Airport and to provide advice on the indemnity agreement and CPO process generally.

## **2.0 RiverOak**

- 2.1 On their website, RiverOak Investment Corp describe themselves as 'having a reputation for identifying under-utilised assets & creating new value from them on behalf of our client investors'. A new company RiverOak Aviation Associates has been set up to deliver this project (referred to as RiverOak).
- 2.2 The proposal from RiverOak is that they will fund the legal CPO process but will not themselves be funding the purchase of the land or the development of the airport. These legal CPO costs are not insignificant and it is intended that £2m will be placed in what is known as an escrow account, reserved specifically for these costs.
- 2.3 The funding for the land purchase and development of the airport will instead come from private investors that RiverOak will try to attract to invest in the project. From the documentation so far provided to the Council by RiverOak it appears that those investors will not be investing until after the confirmation of the CPO by the Secretary of State which would be after any inquiry conducted by a planning inspector.
- 2.4 Prior to and during the progress of the CPO the Council should seek to purchase the land by negotiation which can be done in parallel with the CPO process. The Council has no resources itself to buy the land prior to the securing of funding by RiverOak. The Council has seen no evidence that RiverOak have the resources now available to buy the land prior to the confirmation of the CPO.
- 2.5 Counsel has advised that the possibility of a party wanting to sell their land voluntarily to the Council even if the CPO is abandoned would need to be covered in the indemnity agreement to protect the Council. RiverOak have provided no evidence during the negotiations of their ability to cover this eventuality.

## **3.0 Timeline**

### **June 2015**

- 3.1 Following a meeting in May 2015 RiverOak wrote to the Council setting out their position in relation to the CPO and their proposed role as an indemnity partner. RiverOak included their intention to deposit £250,000 in their solicitor's bank account to fund the CPO process. RiverOak also described how that money would be topped up as the scheme progressed.

## July 2015

- 3.2 At a meeting with Council representatives on the 3rd July 2015, RiverOak gave a presentation on their proposals for the airport which included the use of the site to recycle 'end of life' aircraft with some cargo and future passenger activity.

Proposals were also made by RiverOak about financing the scheme and the ability of RiverOak to prove that they could resource the CPO, the land purchase and the development of the airport. Those proposals included:

- (a) An 'escrow' account held by RiverOak's lawyers with funding of up to £2m to fund the CPO process. This was welcomed since it addressed the concern raised in the December report about funding the CPO in stages. Once the escrow account was put in funds, then the whole CPO legal process (but not the land acquisition nor airport development) would be funded.
- (b) RiverOak also proposed to provide a 'letter of credit' from a major European financial institution to cover the costs of land purchase and development of the airport. This meant in the event that RiverOak's third-party investors were unable to make payment on the land purchase, the bank would cover the outstanding amount. This was also welcomed since it addressed the concerns in the December report about the lack of certainty over funding for the land acquisition.
- 3.3 The Cabinet met in July (1.4 above) to agree to review the Council's position in relation to Manston Airport. The Council then instructed Sharpe Pritchard Solicitors who have considerable expertise in CPOs to act for it in negotiations with RiverOak's solicitors. In addition, the Council has also taken advice from a barrister at Landmark Chambers in London who specialises in compulsory purchase. For the sake of brevity, in the rest of the report, references to 'RiverOak' or the 'Council' include RiverOak's solicitors and the Council's solicitors.
- 3.4 Having reviewed the draft indemnity agreement provided by RiverOak, the Council asked them for an up to date business plan for their proposals. The business plan was required to give the Council an understanding of how RiverOak's current proposals met the public interest test which the Council needed to consider before entering into the indemnity agreement.
- 3.5 RiverOak subsequently informed the Council that they would not now be providing their proposed legally binding letter of credit from a bank. So the funding in relation to the costs of the land acquisition reverted back to its December 2014 position. That is, that there is no provision for funding any shortfall from RiverOak or its investors in respect of the monies required to acquire the site. Instead, RiverOak offered to provide a non-binding letter of assurance from a major financial institution.
- 3.6 In response to the request for an up to date business plan, RiverOak referred the Council back to the financial projections previously provided and declined to provide a business plan indicating that this would be provided once the CPO process was underway. This meant that the Council was being asked to enter into an indemnity agreement for the reopening of the airport with no up to date information on the business plan supporting the scheme.

## August 2015

- 3.7 RiverOak informed the Council that their next stage in the process was to develop the business plan in detail.

- 3.8 In substitution for the letter of credit, a letter of support was provided by RiverOak. It was a 'subject to contract' letter from a large American financial services company which 'supported' the efforts of RiverOak regarding the opening and development of Manston Airport following a successful CPO. However, the letter says that it is not a 'binding legal commitment' to the project and that 'any investment is subject to confirmation of the CPO for acquisition of the airport site, as well as, usual and customary funding terms and internal approvals'.
- 3.9 Whilst the letter was from a company with a business history of ownership and management of airports, the letter is not legally binding and there is no indication that any investment will be made before the CPO is confirmed and, therefore, for the purpose of providing assurance that finances will be available for acquisition of the land before the CPO is confirmed, it is of little value.
- 3.10 The Council therefore requested RiverOak to provide the financial guarantees (if any) which they would be providing to secure the council's interests in delivering a viable airport operation as quickly as is reasonably possible without any residual cost to the Council. A deadline of the 14<sup>th</sup> August was given for RiverOak to provide this information.
- 3.11 The Council's legal advice on this point is clear. Whilst funding does not have to be secured at the outset of the CPO process, the Council does have to satisfy itself that there is a real prospect that the scheme will proceed and this means that the Council needs to consider scheme viability and/or funding before making the CPO. At this stage the Council did not have confidence in the finances (which were based solely on the letter of support from the American company) and no written evidence of RiverOak's current proposals for the airport.
- 3.12 The Council then received confirmation from Riveroak that they had placed £1,325,000 with their lawyers which it is intended to be put into the escrow account should the indemnity agreement be entered into. It is worth repeating that this was a positive step forward from the December position where the CPO legal process was to be completed in steps as funds allowed.
- 3.13 On the deadline of the 14th August 2015, RiverOak provided two redacted letters from potential investors (with the details of those investors removed). As with the letter from the company referred to above, the letters expressed strong interest in participating in RiverOak's acquisition of the airport through a CPO. One letter of support was conditional on the CPO process being concluded in a manner satisfactory to RiverOak and its partners. The other potential investor said they were in a position to invest up to £20m subject to satisfactory final documentation. Their final investment decision was conditional 'upon standard commercial due diligence, valuation of the asset and confirmation of the CPO by the secretary of State'.
- 3.14 Since the letters had the details of the authors removed, the Council has been unable to carry out any investigation into the authors of these letters. Counsel has advised that if we knew who the letters were from and could check their bona fides, the redacted letters could have greater weight.
- 3.15 Counsel has advised that the three letters from potential investors by themselves are not sufficient for the council to be satisfied as to the resourcing of the CPO and the likelihood of the scheme going ahead. The letters are of some evidential value but do not by themselves show that all the necessary resources are likely to be available to complete the scheme.

- 3.16 Counsel has pointed out that the letters do not require either the American company or the two investors to fund the CPO if RiverOak were unable to do so. A bond or escrow account or other form of guarantee if sufficient to cover the land acquisition costs and to enable delivery of the project would provide reassurance to the Council. However, the Council would still have to be satisfied that £20m was an accurate figure for land acquisition and start-up costs.
- 3.17 RiverOak referred to a bond in the original draft of their draft indemnity agreement. The Council requested details of this bond with a deadline of the 18<sup>th</sup> August 2015; the response from RiverOak was that discussion of the bond was somewhat premature.
- 3.18 Counsel advised that the requirement for a bond relates to the financial strength of the indemnity partner and the extent to which they can satisfy the Council that they can resource the CPO. Where there is a concern over the resources of an indemnity partner then a bond or other security would be a sensible way to proceed. It is not necessary for the bond or surety provider to be a party to the indemnity agreement but the Council would have to be satisfied as to the enforceability of the bond or surety before any indemnity agreement was finalised.

### **September 2015**

- 3.19 Representatives from RiverOak and the Council and their respective solicitors met to discuss outstanding issues. The agenda included what has changed since the December Cabinet report; evidence of financial resources for underwriting the CPO costs, land acquisition and scheme costs; the business plan and viability of the scheme; the public interest test; contractual commitment to proceed with the scheme if the land is acquired.
- 3.20 Prior to the meeting, RiverOak were informed that the Council would need all necessary information to be able to draw up a report to Cabinet which evidences that all the necessary resources/funding will be available when required to fund the CPO process, the land acquisition and the implementation and on-going airport operation, of the airport scheme as proposed by RiverOak.
- 3.21 The action points from the meeting were:
- a) Explanatory note covering compliance with the tests outlined in Circular 06/2004 to be drafted by RO and issued to TDC as soon as possible and in any event before 30 September 2015.
  - b) CPO Indemnity Agreement to be reviewed by TDC's legal advisors and comments issued to RO as soon as possible and in any event before 30 September 2015.
- 3.22 Compliance with the tests in Circular 06/2004 was described in the minutes of the meeting as:
- 'TDC being able to satisfy itself and show at a public inquiry that the tests in CPO Circular could be met before the Council agreed to use its CPO powers. In order to do so, TDC requested an overall picture of how the financial resources will be put together from start to finish and how the public interest test under the Circular would be satisfied. For the purposes of accurate, clear and confident reporting within TDC and in order to fully address all points raised by TDC in respect of funding and public interest issues, a request was made of RO to demonstrate how the proposed scheme would match the requirements of the Circular both in terms of resources and the public interest test in promoting the CPO.'

- 3.23 The time limit for the actions after the September meeting (3.21 above) was amended at RiverOak's request to the 22nd September (and then the 23rd September) when it was agreed that our respective documents would be exchanged. The Council provided its documents on the 23rd with RiverOak providing theirs on the 24th September.
- 3.24 In accordance with the action point from the meeting, the Council reviewed the CPO indemnity agreement and proposed amendments to Riveroak. It was proposed to amend the bond so that it secured that funding was in place to acquire the land prior to the confirmation of the CPO by the Secretary of State. RiverOak's position was that a bond would only be available after the confirmation of the CPO.
- 3.25 Another proposed amendment was a requirement for RiverOak to request the Council to acquire the land within a set period after the confirmation of the CPO. This is because in the absence of any other agreement requiring Riveroak to proceed expeditiously with the reopening of the Airport, the Council had to impose an obligation on Riveroak to not delay the revival of operations at the Airport. The Council could not permit the Airport land sitting under the shadow of an unexercised CPO with nothing happening on the ground.
- 3.26 These two provisions were intended to secure the Council's interests in ensuring that the airport comes into sustainable long-term operation as quickly as is reasonably possible without any residual cost to the Council.
- 3.27 RiverOak did not agree with the amendment to the timing of the provision of the bond and subsequently publicly announced on the 11th October 2015 'We want to be perfectly clear, as we have in the past, we will not provide a bond. It is neither economically nor commercially viable to do so and is absolutely not required by the governing law'.
- 3.28 RiverOak have argued that providing funding for the project, for which the CPO is required, post consent is the usual order of events in an infrastructure project, and is not something that is unique to RiverOak. In support of this contention, they cite Hinkley Point C, Crossrail, HS1, HS2, all of which they say were/are to be funded post consent. The difference with any Manston Airport CPO is that the projects referred to by RiverOak were/are backed by Central Government whereas the Council has no resources to back the Manston CPO, which is why it requires a bond or other surety in place to cover the period from when the CPO is made.
- 3.29 With respect to the need to acquire the land within a set period after confirmation of the CPO, RiverOak said that they would need time after confirmation of the CPO to secure and document the funding for the project. Given that the CPO process might take up to two years before the CPO is confirmed by the Secretary of State, RiverOak could then take up to 3 years to obtain the funding, this could see the airport lying dormant for potentially five years if there is no obligation on RiverOak to secure its funding within a set period of the confirmation.
- 3.30 RiverOak provided an explanatory note as agreed in the action point from the September meeting. However, at that time it did not provide the picture of the overall financial framework as agreed and nor did it explain how RiverOak's proposals met the public interest test of Circular 06/2004.

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- 3.31 At the end of October, over three weeks after the deadline for providing this information had expired, RiverOak provided a revised version of their explanatory note (3.28 above). The document sought to address the public interest test and, as part of this, the other tests that needed to be satisfied; the planning test, the wellbeing test, the financial test and the necessity test. The paper however lacks detailed evidence which it is suggested will be provided in the future and suggests that Council officers are better placed than RiverOak to comment on whether the planning and well-being tests are met. In the absence of an up to date business plan it is difficult to assess that all the tests will be met. The information that has been provided to seek to satisfy the finance test is covered in this report already and the necessity test is based upon the decision of the present owners not to reopen the airport and that therefore the CPO is required to bring back airport use. However, this assertion by RiverOak as to why the CPO is required has to be balanced against the intentions of the current landowners and whether there is any likelihood that the current landowners' proposed use of the site would also satisfy the public interest test.

### **4.0 The Indemnity Agreement and CPO Powers**

- 4.1 RiverOak have sought to separate the decision on whether to enter into an indemnity agreement from the decision whether the Council should use its CPO powers in relation to Manston airport. Counsel's advice is that there is no particular justification for seeking to take a decision to enter into an indemnity agreement separate from the consideration of whether to make a CPO in support of a particular scheme.
- 4.2 RiverOak has not provided sufficient evidence to show the Council that the funding available to deliver the scheme is currently available or likely to be available to deliver the scheme. Information has been provided that sets out RiverOak's funding intentions but it depends on the CPO being confirmed, and there is little clarity as to the funding in place. In relation to the public interest balancing exercise, that requires a balanced view to be taken as between the intentions of the Council in making the CPO to deliver the underlying scheme, and the interests and intentions of the current landowners. The Council considers it sensible to consider the question of entering an indemnity agreement with RiverOak (and its principal terms) alongside the principle of making a CPO, which requires the Council to be satisfied that there is a real prospect of the underlying scheme going ahead.
- 4.3 RiverOak have had many opportunities to provide this evidence and the Council has itself requested this evidence. In the meeting with RiverOak in July their presentation was provided on flip charts which were taken away after the meeting. In August the request for an up to date business plan was refused. In September despite it being agreed that the finances and public interest argument would match the requirements of Circular 06/2004 the expected level of evidence and explanation was not provided.
- 4.4. In relation to finances generally, the figures for the scheme have not been justified to the Council and the Council has not been given an opportunity to satisfy itself that those figures are reasonable. The mechanism through which that investment would occur has not to date been explained or what role RiverOak would have in delivering the project.
- 4.5 In relation to specifics of the funding. An offered letter of credit was subsequently withdrawn. A bond to cover any shortfall in funding was also offered and then withdrawn.

## **5.0 Changes since the December 2014 Cabinet Decision**

- 5.1 The main material change since the December 2014 Cabinet decision is the provision of an escrow account which will guarantee the funding of the CPO process. This is welcomed and means that the CPO process can be run at no cost to the authority as a whole process rather than the step-approach as originally proposed.
- 5.2 However the purpose of the Council using its CPO powers is not to run a CPO process, but to ensure that a viable airport comes into sustainable long-term operation as quickly as is reasonably possible without any residual cost to the Council. In order to do that, both the land acquisition and airport development, will need to be funded.
- 5.3 The only evidence to support other funding are two non-binding, conditional and redacted letters of support and a similar letter of support from an American company. There is uncertainty about how any shortfall in funding will be met and indeed the offer of a bond at any stage of the CPO process now appears to have been withdrawn by RiverOak (as per paragraph 3.27 above).
- 5.4 Counsel has advised that it is reasonable for the Council at the stage of deciding the principle of the CPO to seek evidence that it is likely that the key resource and financial tests are fulfilled. If not, it would be very difficult to move forward unless the Council has a high degree of confidence that these matters would be addressed shortly.
- 5.5 RiverOak's track record of failing to provide necessary information throughout the process dents this required confidence. This also begs the question as to why the Council should progress, before receiving the necessary assurances. There seems little purpose in entering into an indemnity agreement separate from taking a decision on the principle of the CPO which requires consideration of the likelihood of the scheme progressing as part of the necessary public interest test.

## **6.0 Conclusion**

- 6.1 The objective of seeking an indemnity partner is to ensure that – if the Council determines to pursue a CPO – a viable airport comes into sustainable long-term operation as quickly as is reasonably possible without any residual cost to the Council.
- 6.2 The relevant considerations raised in the December 2014 Cabinet report (at paragraph 1.3 above) remain relevant today. In addition the review of this decision since July 2015 has highlighted the following issues:
  - 6.2.1 There remains the lack of evidence that financial resources are in place or proposed to be in place to acquire the land prior to the confirmation of the CPO despite the fact that the Council is obliged to attempt to purchase the land by negotiation in parallel with the CPO process.
  - 6.2.2 Whilst letters of support for the project have been provided by potential investors, any commitment to the project has been caveated and, in the absence of any binding commitment, there is limited evidence of the financial resources proposed to be in place to acquire the land and develop the airport scheme after the confirmation of the CPO and the evidence is not sufficient for the council to be satisfied as to the resourcing of the CPO and the likelihood of the scheme going ahead.
  - 6.2.3 RiverOak's public announcement indicates that no bond or surety will be offered to fund any shortfall for the proposed funding either before or after the confirmation of the CPO. A bond is required both before and after confirmation.
  - 6.2.4 There is insufficient evidence currently available for the Cabinet to be satisfied that a proposed CPO is likely to be successful which would justify its entering into an



indemnity agreement. There is good reason to consider the principle of the CPO alongside the decision to enter an indemnity agreement.

- 6.3 Given the above, your legal advisors and officers are not satisfied at this moment in time that the information or assurances provided to date by RiverOak justify the Council deciding to make a CPO or as part of that process to support the appointment of RiverOak as the Council's indemnity partner in advance of deciding whether to make a CPO.

## **7.0 Corporate Implications**

### **7.1 Financial and VAT**

- 7.1.1 There are no resources currently available to fund costs in relation to a CPO described in this report. The financial context is of limited financial capacity of the Council, together with the prospect of continued severe financial constraint. Any proposals that involve exposing the Council to unspecified and/or unknown costs would substantially increase financial risks and potentially undermine the Medium Term Financial Strategy. It is therefore the Council's objective to secure that all costs related to the CPO are borne by the indemnity partner.

### **7.2 Legal**

- 7.2.1 The legal advice is set out in the report.

### **7.3 Corporate**

- 7.3.1 There are no direct corporate implications at this stage.

### **7.4 Equalities**

- 7.4.1 There are no direct equality implications.

## **8.0 Recommendations**

- 8.1 Having reviewed its position, details of which are contained in this report, that no further action be taken at the present time on a CPO of Manston Airport, on the basis that RiverOak do not fulfil the requirements of the Council for an indemnity partner;

- 8.2 Cabinet note that this is the second time that RiverOak have not fulfilled the requirements of the Council for an indemnity partner.

## **9.0 Decision Making Process**

- 9.1 This is a non-key decision and subject to call in.

- 9.2 This is a Cabinet decision.

Contact Officer:	Tim Howes, Director of Corporate Governance & Monitoring Officer
Reporting to:	Madeline Homer, Chief Executive

### **Annex List**

Annex 1	Cabinet Report 11 December 2014
Annex 2	Cabinet Minutes 11th December 2014

## Background Papers

Title	Details of where to access copy
None	N/A

## Corporate Consultation Undertaken

Finance	Tim Willis, Director of Corporate Resources
Legal	Tim Howes, Director of Corporate Governance
Communications	Hannah Thorpe, Interim Head of Communications