

Development Sub-Committee



21 March 2022

Title	Approach to transferring assets from Council to Knowle Green Estates – briefing note
Purpose of the report	To note the change to our accounting methodology
Report Author	Paul Taylor Chief Accountant
Ward(s) Affected	All Wards
Exempt	No
Corporate Priority	Community Affordable Housing Recovery Environment Service Delivery
Recommendations	Committee is asked to note the report
Reason for Recommendation	To notify the Committee about the changes in our accounting methodology.

1. Key issues

- 1.1 Following a question raised in a previous Development Subcommittee meeting, officers have reviewed their methodology for valuing property, prior to transferring to KGE.
- 1.2 In the past, when Spelthorne Borough Council (SBC) had built an asset, which was later transferred to Knowle Green Estates Ltd (KGE) it was transferred at market value, based upon an Independent Valuer's report.
- 1.3 Using this methodology, if the project makes a capital loss (i.e., scheme expenditure is higher than market value), this loss will have to be written off to the Council's General Fund, as irrecoverable and this could significantly reduce the level of reserves available to the Council to support its regeneration programme and delivery of frontline services.
- 1.4 To mitigate the risk associated with the market value being lower than cost, officers have consulted externally, with auditors, tax advisors legal professionals, particularly around issues of state aid, and after discussions between our finance and legal teams, officers are now comfortable that moving forward we can transfer assets from SBC to KGE on a cost transfer basis.
- 1.5 This will result in a no capital loss or gain situation, i.e., neutral at point of transfer for SBC, and will avoid reserves accounting issues around such

capital losses, as well as, making it easier for people to understand the viability “equation” for the capital costs of construction.

- 1.6 The current methodology, works perfectly well, when the Independent Valuers report provides a valuation that is more than the costs incurred to build the property.

2. Options analysis and proposal

- 2.1 Keep as is and the Council run the risk incurring capital losses of several hundred thousand, per property.
- 2.2 Officers are looking to reduce the risk of exposure to these capital losses and therefore have rejected this methodology.

3. Financial implications

- 3.1 This approach protects SBC’s reserves and reduces the risk of a capital loss that cannot only be offset against the Council’s reserves, the majority of which has been earmarked by Council for other projects. In those situations where there would otherwise have been a capital loss.
- 3.2 Under the new methodology it will mean that the assets are being transferred at cost and will generate neither a capital loss nor profit in SBC.
- 3.3 The new accounting treatment will significantly increase the financial resilience of the Council and reduce the risk of incurring a capital loss in Spelthorne Borough Council and thereby protect our useable reserves.
- 3.4 The impact on KGE, will be slight, as it will involve a small movement up or down in the actual capital value of the transfer cost, which will be spread over a fifty-year period. The revenue impact will be approximately 2% of the capital value, therefore, negligible for interest movement, which again will be spread over fifty years.
- 3.5 Going forward, there will still be a requirement for KGE to have its property portfolio regularly valued and officers expect to see a return to the upward trend in property value that we have seen historically over the last 200 years.
- 3.6 Upon consolidation of the Group Accounts, there is no impact on either SBC or KGE.

4. Other considerations

- 4.1 In the unlikely event that additional costs are subsequently incurred by SBC on the contract, for example, Property Completion (PC) takes place, and the contract has not been finalised due to a dispute. Officers will estimate the project outcome to allow the Legal Team to prepare the transfer document to allow KGE to occupy and manage the property, with the transfer price being based on the projections.
- 4.2 Once the contract is resolved, it would be practical for either side, (SBC or KGE) to reimburse the other, as a gesture, so we avoid the capital loss being incurred in SBC, for the reason mentioned earlier.
- 4.3 Having discussed the matter with our legal team, we have been advised that this is not a change of Council policy, just a change of accounting methodology of the transfer of SBC assets to KGE.
- 4.4 These proposals are being presented to the KGE Board at their meeting on 16 March.

5. Equality and Diversity

5.1 None.

6. Sustainability/Climate Change Implications

6.1 No impact.

7. Timetable for implementation

7.1 To be implemented immediately.

Background papers: There are none.

Appendices: There are none.