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# The Next Footings in the Local Property Market 2019

Thursday 9th May 2019

DoubleTree by Hilton Lincoln

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# Agenda

- **Property Market Update**
  Sam Elkington, Lambert Smith Hampton

- **The Tax Life Cycle of a Commercial Property**
  Chris Connor, Tax Partner, Streets Chartered Accountants

- **Development Agreements - An Overview of ‘What Forms They Can Take’, ‘Who Is Involved’ and ‘The Importance of Clear Detailed Deal Terms’**
  Anthony Ogley, Partner, Fraser Brown Solicitors

# Lincoln & Lincolnshire Property Update –

# May 2019


Sam Elkington BSc (Hons) FRICS
Director


Lambert Smith Hampton

Lambert Smith Hampton

# LINCOLN

- 2 Universities
- Over 16,000 Students and 1,600 Academic Staff
- Providing a £250 million contribution to the local economy
- 4 million Tourists per year
- Retail catchment of over 550,000
- Direct rail connections to London




Lambert Smith Hampton

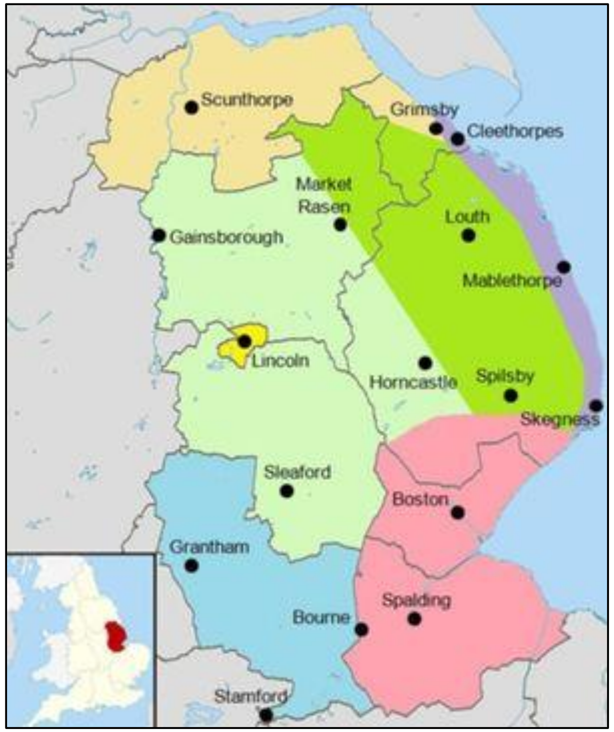
# RETAIL - LINCOLN

- Prime High Street still strong
- Boots relocated
- Cornhill Quarter filling up
- New multi-storey car park
- Out of town centre and roadside

Lambert Smith Hampton

# COUNTY RETAIL CENTRES

- Grantham
- Sleaford
- Boston – Quadrant
- Gainsborough
- Bourne
- Stamford
- Spalding






Lambert Smith Hampton

# OUT OF TOWN RETAIL

- Employment Park opportunities
- Countywide demand


The Quadrant, Boston

Roman Gate, Nettleham Road

- Good investment and development opportunities



Lambert Smith Hampton

# RESIDENTIAL DEVELOPMENT LAND

# HIGHLIGHTS OF 2018

| | |
|---|---|
| 2018 | SALE of in excess of 800 Residential Development Plots completed |
| 2018 | In excess of 750 Residential Development Plots ACQUIRED for Clients |
| 2019 | APRIL – 540 Residential Development Plots SOLD on a Subject to Planning basis. |
| 2019 | MAY – 410 Residential Development Plots put UNDER OFFER this year so far |
| 2019 | MAY – in excess of 425 Residential Development Plots on the market FOR SALE or coming to the market. |

# INDUSTRIAL

Lincoln

- Increased rental levels - £6-£7 psf
- Speculative schemes pre-let
- Teal Park – Jaguar Land Rover

Avro Court, Sadler Road

# INDUSTRIAL

- Sleaford – NKDC acquire 35 acres employment land.
- Stamford – SKDC acquire Cummins Factory
- Gainsborough – 10 acre Serviced land sale

Cummins Factory, Barnack Road, Stamford

# OFFICE

- Limited new build demand
- Uneconomic to speculatively build
- Stock levels becoming lower
- Changing working practices


Alpha Court, Kingsley Road



Lambert Smith Hampton

# The Tax Life Cycle of a Commercial Property

Chris Connor, Tax Partner
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# Decision 1 – Lease or Buy?

- Are funds available to purchase?
- Leases
  - Lots of different scenarios
  - Grant vs Assignment
  - Duration of Lease
  - Inducements by landlord

# Purchase of Commercial Property

1) Buy new commercial premises
2) Self build
3) Buy used commercial premises

# Buy New Commercial Premises

- Fixed asset – Balance sheet
- Subject VAT at standard rate (<3 years old)
- SDLT on VAT inclusive amount

Any tax relief available?

# Capital Allowances

Capital allowances on plant/integral features

- Heating/ventilation/air conditioning
- Electrical systems including lighting
- Water systems
- Data installations
- Lifts/security equipment
- Sanitary ware

- May require specialist CA survey if developer will not provide cost analysis
- Could equate to 35% of cost
- Balance – SBA’s 2% per annum (After 29 October 2018)

# Self Build

| | |
|---|---|
| Buy land | - VAT exempt unless opted |
| | - SDLT |
| Build contract | - VAT – standard rated generally |
| | - SDLT – No |

Any tax relief available? Yes – Capital Allowances

Exactly the same as when buy new commercial premises

| | |
|---|---|
| Advantages | - You control contractor – cost information available |
| | - Your exact specification |
| | - May eliminate element of developer profit |
| | - More tax efficient – save SDLT |

# Buy From Developer

| | |
|---|---|
| Purchase | 1,000,000 |
| VAT | 200,000 |
| | 1,200,000 |

SDLT on £1.2m =

| | |
|---|---|
| 0 – 150,000 @ 0% = | 0 |
| 150,000 – 250,000 @ 2% = | 2000 |
| 250,000 – 1,200,000 @ 5% = | 47,500 |
| | 49,500 |

Total cost = **£1,249,500**

Note: VAT likely recovered under option to tax
£1,049,500

# Self Build

| | |
|---|---|
| Land cost - say | 300,000 |
| VAT | - |
| SDLT | |
| 0 – 150,000 @ 0% = | 0 |
| 150,000 – 250,000 @ 2% = | 2000 |
| 250,000 – 300,000 @ 5% = | 2500 |
| | 4500 |
| | **304,500** |
| | |
| Build | 700,000 |
| VAT | 140,000 |
| SDLT | - |
| | **840,000** |
| Total cost | **£1,144,500** |
| VAT likely recovered under option to tax | |
| | £1,004,500 |
| Saving – SDLT | **45,000** |

# Used Commercial Building

- Fixed asset
- Subject VAT? Maybe yes – standard rated if opted to tax
- SDLT on VAT inclusive amount

Any tax relief available? Maybe

- Capital Allowances

- Property History
- Negotiation Seller
- Formal election as part of purchase process
- Mandatory pooling

# Refurbishments

- Capital vs Revenue (repair)
- If Capital – Capital Allowances
- If Revenue – Deduction in year if in P+L

How do we decide?

- Replacement of entirety – Capital
- Improvement above and beyond modern equivalent – Capital
- Work required to bring into useable state on acquisition – Capital
- Reinstatement to original condition – Repair
- Level of cost irrelevant
- Roofs – common mistake
- Accounting treatment critical

# Land Remediation Relief

- Costs removal of harmful substances from land and buildings
- Trading and UK property companies only
- 150% deduction relevant costs
- Examples – asbestos, sulphate contamination
- Tax credit if loss in the period at 16% of 150% deduction
- Not responsible for contamination

# Disposal of Property

- Sell property
- Capital gain – sale proceeds less purchase

| | |
|---|---|
| Proceeds | X |
| Less: selling costs | (X) |
| Net sale proceeds | **X** |
| Less: acquisition cost | (X) |
| Enhancement costs | (X) |
| Indexation Allowance (if company) | (X) |
| Taxable gain | **X** |

Reliefs may be available

# Reliefs on Disposal

- Individuals/companies
  - Rollover relief
  - Replacement land for use in trade
  - Holdover against – fixed plant/machinery
- Individuals
  - Gift relief
  - Assets used in business of donor/personal co
  - Base cost transfer to recipient
- Entrepreneurs relief
  - Associated disposal rule
  - 10% rate

# Capital Allowances on Disposal

- Seller could retain benefit of allowances
- Seller could negotiate greater proceeds
- Sales particulars
- Negotiation and election to protect from clawback

# Buying a Commercial Property through a SIPP

- Increasingly common for SIPPs to invest in commercial property
- Investment returns on other generally low
- Attractive from a tax perspective
- Particularly where the property is used in the trade

# Tax Advantages

- No CGT payable if property disposed of by the SIPP
- Rent paid by the business will be deductible and tax free in the SIPP
- Potential tax relief on contributions to the SIPP
- As a pension asset the property would usually be safe from creditors

**But:**

- There could be a CGT liability on transfer to the SIPP
- There will be SDLT to pay on the transfer and potentially on any lease back

# Points to Consider

- Values often significant – so is tax relief
- Can be time critical
- Take proactive advice at early stage

# Development Agreements

## An Overview of ‘What Forms They Can Take’, ‘Who Is Involved’ and

## ‘The Importance of Clear Detailed Deal Terms.’

Anthony Ogley, Fraser Brown

Partner, Commercial Property

# Introduction

- Development work and development related work is considered to be one of the most challenging , complex and difficult (but also rewarding) areas of legal work involving real estate, property and construction.

- Development agreement related matters typically involve various parties but all development agreement related matters involve a developer and it is important to understand when progressing a development matter what a developer's requirements, desires and principle concerns are.

- More complex development agreements invariably involve a pension fund or another form of financial institution (colloquially referred to as a 'fund') and a fund tends to look on property purchasing and investment in a different way from the average property investor and therefore it is also important to understand when progressing a development matter what a fund's requirements, desires and principle concerns are.

- There are several different forms of development agreement with each varying in their complexity and which to use being very much dependent on the deal brokered.

- So what forms of development agreement are there?

# Development Agreement – Standalone ('DA')

- What is a DA?
  - typically an agreement used for specific development projects whereby a landowner contracts with a developer to carry out a development on land already owned by the landowner
  - typically a DA deals with funding in one of the below ways:
    - the development will be carried out by the developer with the landowner funding the cost of the development and retaining ownership of the completed development
    - the development will be carried out by the developer with the developer funding the cost of the development and then usually within 'x' number of Working Days after the development is completed the landowner will:
      - either transfer the freehold of the completed development to the developer
      - or grant a usually long lease of the completed development to the developer

# Development Agreement – Standalone (‘DA’)

- Completion
  - typically within ‘x’ number of Working Days of the date when the development is completed (commonly referred to as the date of Practical Completion)

# Development Agreement – Standalone ('DA')

- Purchase Price
  - typically the purchase price paid by a developer for the freehold or the long lease is:
    - either
      - a fixed sum agreed between the parties at the outset and before the DA is exchanged
    - or
      - the market value of the completed development at the time the development is completed calculated in accordance with the provisions in the DA

# Development Agreement for Lease (AFL) (aka Pre-Let Agreement)

- What is an AFL?
  - typically an agreement between a landowner and prospective tenant which sets out the terms on which a tenant commits to take a lease of a property once it has been built in accordance with the provisions of the AFL
  - typically the development will be carried out with the landowner funding the cost of the development – the tenant is unlikely to be involved with the cost of the development
- Completion
  - typically within ‘x’ number of Working Days of the date when the development is completed (commonly referred to as the date of Practical Completion)
- Rent
  - either
    - a fixed starting rent agreed between the parties at the outset and before the AFL is exchanged
  - or
    - a rent calculated in accordance with the provisions in the AFL – typically an amount calculated using a £ per sq ft figure multiplied by an agreed net internal floor are of the whole of or part of the completed development to be leased

# Forward Funding Agreement (FFA)

- What is forward funding?
  - this is where a developer, who owns a development site, enters into an agreement with a fund in which the developer agrees to transfer title to the development site and agrees to procure the construction of the development and the letting / leasing of the completed development
  - under an FFA a developer
    - will find a tenant / tenants for the completed development (typically pursuant to a letting strategy agreed with the fund)
    - will, once the terms of a letting have been agreed with the tenant(s) and have been approved by the fund, arrange the negotiation of AFLs (Pre-Let Agreements) with the tenant(s) and the subsequent exchange of any such AFLs (Pre-Let Agreements)

# Forward Funding Agreement (FFA)

- What is an FFA?
  - typically an FFA will be set up as / structured with two contracts
    - a land contract which will provide for the developer to transfer the legal title to the development site to the fund often, at the outset of the deal and before development commences
    - a development/build contract which will typically contain the provisions dealing with the construction phase(s) of the development project, the drawdown of monies from the funder during the construction phase(s), completion of any lease(s) pursuant to any AFLs (Pre-Let Agreements) and the final calculation of any final sum(s) due from the fund to the developer
  - typically the fund finances the costs of the development
  - generally an FFA is considered to be the most complex form of development agreement and this is because it not only contains the complex construction and development issues contained in most development agreements but an FFA also contains complex financial provisions and terminology (phased payments and drawdowns, developer's profit etc)

# Forward Funding Agreement (FFA)

- Completion
  - typically the land ownership transfer will complete simultaneously with the exchange of the land contract and the exchange of the development/build contract FFA (or very quickly following exchange) and before any construction works commence because this way the fund knows that it is advancing/expending funds to enhance its own land
  - typically any lease(s) will complete ‘x’ Working Days following the date upon which the development has been completed (the date of Practical Completion) pursuant to and in accordance with the provisions in any AFLs (Pre-Let Agreements)

# Forward Funding Agreement (FFA)

- Purchase Price and Developer's Profit under an FFA
  - typically the purchase price will be paid by the fund in instalments in accordance with the provisions in the development/build contract and stages in the construction process (basically re-imbursement of the development costs)
  - in addition to the 'purchase price' as referred to above once the development has been completed and let the developer will receive a profit share payment
    - any such profit payment is typically calculated by
      - either
        - a sum calculated in accordance with the provisions in the FFA (typically being the value of the completed development calculated by way of capitalisation of the total rent roll based upon agreed assumptions (for example yield, treatment of unexpired rent free periods etc) and then deducting from that sum the total development costs (incl any rolled up interest)
      - or
        - by deducting the total development costs (incl any rolled up interest) from a fixed sum agreed between the parties at the outset and before the FFA is exchanged

# Forward Purchase Agreement (FPA)

- What is an FPA?
  - an agreement where a developer agrees to sell a completed development to a fund, and the parties enter into the contract at an early stage, perhaps even before planning has been secured or before the development works have started.  As with an FFA an FPA is typically related to the putting in place of AFLs (Pre-Let Agreements)
  - essentially it is a very similar ‘beast’ to an FFA (previously referred to) BUT unlike in an FFA the fund does not provide the construction finance, the developer will typically fund the construction from its own reserves or by way of short term loan finance which is then typically repaid out of the sale proceeds following completion

# Forward Purchase Agreement (FPA)

- Completion
  - typically the land ownership transfer will complete ‘x’ Working Days following the date upon which the development has been completed (the date of Practical Completion)
    - from a developer’s point of view this timing is preferable because
      - if it is funding the construction works with loan finance this enables it to offer the property to be developed as security for any such loan
      - if it is funding the construction works from its own reserves this enables it to mitigate its risk of using its own reserves to fund the betterment of someone else’s property
  - typically any lease(s) will complete ‘x’ Working Days following the date upon which the development has been completed (the date of Practical Completion) pursuant to and in accordance with the provisions in any AFLs (Pre-Let Agreements)

# Forward Purchase Agreement (FPA)

- Purchase Price under an FPA:
  - typically the purchase price paid by the fund is
    - either
      - a fixed sum agreed between the parties at the outset and before the FPA is exchanged
    - or
      - more typically a sum calculated in accordance with the provisions in the FPA (typically being the value of the completed development calculated by way of capitalisation of the total rent roll based upon agreed assumptions (for example yield, treatment of unexpired rent free periods etc)

# Speculative Funding Agreement ('SFA')

- What is an SFA?
  - it is essentially an FFA but with no AFLs (Pre-Let Agreements) exchanged and in existence at the time the SFA is exchanged
- Risk v Reward
  - the fund in an SFA following an FFA type structure takes on a high risk because it will be funding the construction and development without there being any certainty as to whether there will be any occupational tenant(s) once the development / investment is completed

# Construction Documents and Specifications

- The various types of development agreements referred to not only need to deal with and address the provisions of any specific deal and the obligations of and between the fund, investor purchaser, developer, tenant, lender and landowner and bank but they also all need to specifically deal with the construction aspects of a development

- There will need to be detailed construction documents regulating the separate relationships between the various parties and the building contractor and other professional consultants and these will include documentation such as:
  - a building contract
  - professional appointments
  - collateral warranties/third party rights
  - sub-contractor warranties

# Who is Involved in Development Matters?

This is an illustrative (but not an exhaustive list) of the number and range of the parties / professionals involved in development agreements and development deals

- The Parties – fund / developer / landowner / seller / buyer / landlord / tenant (whichever is/are applicable to the deal)
- Solicitors and Legal Advisors for the Parties
- Accountants and Tax Advisors for the Parties
- Surveyors / Land Agents / Valuers for the Parties
- Building Contractor
- Contract Administrator / Employer’s Agent / Project Manager
- Professional Team / Design Team
- Sub-Contractor

# The Importance of Clear Detailed Deal Terms

- Heads of Terms are used by parties to set out and determine the overall scope of a transaction and to record the points of principle and commercial matters and outline the important deal making terms before pushing too far into the progression of any deal

- Clear detailed Heads of Terms will
  - help identify at an early stage any issues which may prevent a deal moving forward and enable opportunity for further pre final agreement and sign off negotiation
  - help identify issues that will determine how to structure a deal
  - outline the timetable for the deal and outline the obligations of the parties in the deal
  - provide the detail for the legal documentation to be drafted around
  - act as a checklist to aid and speed up the legal documentation drafting process

- Heads of Terms may be prepared by the parties themselves but typically they are brokered between and produced by the parties' land agents / surveyors

- In my opinion and experience, I would urge early involvement of / canvassing of opinion the solicitors / legal advisors for the respective parties in respect of Heads of Terms and their content before the Heads of Terms are finally signed off and agreed

# The Importance of Clear Detailed Deal Terms

- **BEWARE**
  - – it is important to avoid the risk that any agreed development deal Heads of Terms create a binding legal contract
    - the existence of a binding legal contract for the disposition of an interest in land can be argued if both of the following are satisfied
      - – the general legal requirements for the creation of a contract exist namely offer, acceptance, consideration and intention to create legal relations
      - – the contract / document being argued to be a contract
        - is in writing
        - incorporates all the terms that the parties have expressly agreed in one document
        - is signed by or on behalf of each party
  - – to mitigate this risk it is beneficial to ensure that any Heads of Terms
    - are marked 'Subject To Contract'
- AND
    - include a statement that the provisions in the Heads of Terms are not intended to be legally binding on the parties

# Conclusion

- Development work is a challenging, complex and often difficult (but also rewarding) area, which involves a huge number of parties / professionals interacting and working together.

- Development and land law related transactions are in their very nature
  - transactional
  - not litigious / ‘combative’
  - not structured / brokered to have ‘winners’ / ‘losers’ per se
  - structured / brokered to do a deal which is so far as it is possible to do so best for all parties involved.

- Development transactions without ‘completion’ actually being achieved will typically leave the parties involved having expended time and effort and incurred cost and expense but not ‘made anything’ out of the deal.

- Development work and transactions are as much exercises in organisation, logistics and negotiation as they are exercises in professional expertise. All parties and professionals involved should accept and endeavour to work together in a practical, commercial and professional way.

- If the above is achieved all parties and professionals involved can ‘make’ out of the deal!

Any Questions?

If you would like a copy of this presentation, please email info@fraserbrown.com

Thank You

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