

Amber Fund Management Limited

Response to the Auditor General's Report into
the Regeneration Investment Fund for Wales (RIFW)
dated 15 July 2015

for National Assembly for Wales
Public Accounts Committee

1. Executive Summary

- Amber Fund Management Limited ("AMFL" or "Amber") welcomes this inquiry and is pleased to have the opportunity to set out its views on the Regeneration Investment Fund for Wales ("RIFW") and its own involvement in RIFW. Amber has always constructively engaged with the study team of the Auditor General, as acknowledged by the Welsh Audit Office ("WAO"), and will continue to do so.
- From the time that allegations were first raised with respect to the land sale, RIFW and AFML have been extremely active to ensure that RIFW's interests have been properly protected. Both RIFW and Amber have been in extensive and co-operative dialogue with Welsh Government and an enormous amount of work has been undertaken in reviewing the circumstances around the sale.
- The role of Amber in RIFW, as set out in the Fund Management Agreement with RIFW is to advise on the regeneration investment opportunities of RIFW and to manage investments once made. Amber is not responsible for property valuation or advice, nor does it make property related decisions on behalf of RIFW but in the course of its role in managing and supervising LSH, did procure additional legal and valuation advice on the sale in order to fulfil its supervisory role.
- The valuation methodology of the District Valuer and the £30.9 million property portfolio valuation that is referred to in the WAO report was not prepared on a like for like basis to the actual amount achieved for the sale. This is recognised by the WAO who note in their Report that *"we consider it unlikely that RIFW could have disposed of the assets to achieve sale proceeds consistent with the District Valuer's market valuation"*.
- Amber is of the view that the decision made by RIFW to sell the portfolio needs to be seen in the context of the time at which it was taken and the other pressures that RIFW was subject to in terms of its investment pipeline.
- The WAO noted that *"In its role as Fund Manager, Amber applied robust evaluative and financial due diligence procedures to applications from potential projects for investment funding. Despite pressure from the need for RIFW to commit funds to regeneration projects by December 2015 in order to draw down the full amount of its available ERDF funding, our review of a sample of applications found that Amber's decisions in respect of approval or rejection on behalf of the RIFW Board were soundly based."*
- AFML is of the view that while it undertook its supervisory and investment duties diligently, wider lessons can be taken from the way in which RIFW was established and the portfolio disposal process, and is pleased to be able to share these insights in this submission.

2. Introduction

AFML is pleased to submit this paper at the request of the National Assembly for Wales Public Accounts Committee ("PAC") as a response to the Auditor General's Report into the RIFW dated 15 July 2015 (the "Report"). We are committed to collaborating with the committee throughout the process in the shared interest of the success of RIFW.

This submission addresses the inquiry's terms of reference, the background and the context to AFML's involvement in RIFW, as well as dealing with specific points addressed to AFML in the Report. If further information is required, we will do our utmost to assist the Committee's inquiry.

The Report is wide ranging in its scope with the main focus on the process and outcome of the disposal of the portfolio of land assets which had been transferred by Welsh Government to RIFW at the time of its establishment. These assets were provided in lieu of cash so that through a combination of cash and property assets (assumed by Welsh Government to have a total value of £30m) RIFW would be established with total assets of £55m as shown below.

Initial composition of the RIFW Investment Fund	
Funding source	Amount (£ million)
European Commission: ERDF – JESSICA	25.0
Welsh Government: Property asset portfolio	20.6
Welsh Government: Cash	9.4
Total Fund value	55.0

2.1 Structure of RIFW and the role of Amber

The structure of RIFW and its funding with a mix of cash investment from European sources combined with cash and land transferred from Welsh Government was determined by Welsh Government prior to AFML being appointed as fund manager to RIFW.

AFML was appointed by RIFW as its fund manager following a competitive process run by Welsh Government. AFML continues in this role working in close dialogue with Welsh Government and is also (along with Welsh Government) a member of RIFW (which is constituted as a limited liability partnership). AFML is an adviser on investment opportunities not a property adviser. As RIFW's fund manager, AFML's main role is to advise on the regeneration investment opportunities of RIFW and to manage investments once made. RIFW has made one investment to date.

Following the original procurement of advisers for RIFW by Welsh Government, RIFW and AFML jointly employed the property consultancy firm Lambert Smith Hampton (LSH) as RIFW's "investment manager". In this function LSH's main role was to provide advice to RIFW and AFML on property related matters both in respect of new investment and in respect to the "land dowry" with which RIFW was established. LSH owed the same contractual duties to each of RIFW and AFML in this role.

The WAO notes that that *"The legal contracts agreed between RIFW LLP, Amber and LSH resulted in complex arrangements in which there was simultaneously a tripartite relationship between the three as well as a bilateral relationship between Amber (as principal) and LSH (as agent). This complexity created a degree of ambiguity and confusion between the parties, which has been reflected in their differing portrayals to us of their respective responsibilities and relationships to each other"*.

While AFML agrees with this statement, it notes that the contractual frameworks was established by the Welsh Government prior to procurement of AFML and LSH as advisers to RIFW, and that in the course of that Restricted Procedure procurement AFML were told that no changes to the contractual structure or terms would be accepted by Welsh Government for procurement reasons. In practice however AFML, Welsh Government and RIFW have worked very closely at all times and AFML considers that these close working relationships have mitigated any problems that might otherwise have existed.

3. Comments on Value

The WAO's overall conclusion is that:

Due to flaws in the way RIFW was established, in the selection of assets and also in the sale process itself, neither RIFW nor the Welsh Government are able to demonstrate that value for money was achieved from the portfolio sale transaction.

The decision making relating to the sale of the land was a matter reserved under RIFW's constitution for the RIFW board and as such was not a matter delegated to AFML. As noted above RIFW employed a property consultancy firm who gave it advice on property related matters. That firm owed contractual duties to both RIFW and AFML. These duties included to:

- *act in a competent and efficient manner and in the best interests of the Fund Manager and the Partnership so as to give to the Fund Manager and the Partnership the full and complete benefit of the Manager's experience and expertise in relation to the Properties;*
- *exercise the reasonable skill and care to be expected of an experienced investment manager;*
- *have regard to the principles of good estate management and professional codes of conduct and/or guidelines laid down from time to time by the Royal Institution of Chartered Surveyors (or its successor body from time to time);*

From the time that allegations were first raised with respect to the land sale, RIFW and AFML have been extremely active to ensure that RIFW's interests have been properly protected. Both RIFW and AFML have been in extensive and co-operative dialogue with Welsh Government and an enormous amount of work has been undertaken in reviewing the circumstances around the sale.

Notably both RIFW and AFML (in conjunction with Welsh Government) have been anxious to understand whether there is any possibility that RIFW was negligently advised with respect to the land sale and, in the event that it was, to ensure proper legal recompense was available. As a consequence, in order to protect RIFW in this respect, additional legal and valuation advice was procured for RIFW (in accordance with Welsh Government procurement procedures) and shared with Welsh Government.

In particular RIFW commissioned a fully independent ex-post facto valuation of the land portfolio from Colliers International (a large firm of international property consultants with no prior involvement with the portfolio). This valuation was commissioned by RIFW expressly on terms and conditions that would enable it to be utilised by RIFW as expert evidence in any legal proceedings that might be brought in the future. AFML believes that among the range of valuation opinions considered by the WAO relating to the portfolio it is only the Colliers valuation report (commissioned by RIFW) that was prepared with the forensic goal of establishing the issue of whether RIFW had suffered loss through inadequate advice.

As noted in the Report, the conclusion of the independent Colliers valuation was that *the aggregate Market Value of each individual asset which sold as part of the portfolio to SWLDL is £22,225,000*. This value accorded with the actual sales price achieved by RIFW for the land portfolio.

Given this conclusion, RIFW's legal advisers, Blake Morgan, have told RIFW that even if it were the case that RIFW was badly advised (which is denied by LSH) then because no loss to RIFW can be demonstrated then there is no basis for RIFW to take any legal action in respect to the advice given to it about the land sale.

We believe from discussion with the WAO that they too accept that there is no valuation evidence that would establish on the balance of probabilities (the relevant civil standard of proof) that RIFW suffered a loss on the land sale through negligent advice. We believe that it is important this point is made clear.

AFML and RIFW continue to keep this matter under close scrutiny. AFML, RIFW and the Welsh Government have a complete identity of interest in ensuring that RIFW has not suffered loss through being improperly advised. Were it the case that evidence was to emerge that RIFW had suffered loss through bad advice both AFML and RIFW would have no hesitation in enforcing their contractual rights in this respect.

However, this is not the complete picture. The work of the PAC and WAO is partly focussed on whether the actual transaction that took place at the actual time it occurred was on reasonable terms. As noted above, subject to any new evidence that may emerge, subsequent professional advice has not suggested that RIFW has grounds of complaint in this respect. But that work is also focussed on whether better outcomes would have been achieved had an alternative approach to the land portfolio been adopted.

4. Comments on Process

No doubt, because of the points referred to above, the main thrust of the Report and its recommendations go towards the process adopted with respect to the sale. The centrepiece of the Report is the WAO statement that:

Our conclusions are reinforced by, but are not completely dependent upon, the District Valuer's valuation of £30.9 million for the property portfolio sold to SWLD, excluding any future receipts from overage. This valuation, which is higher than other valuations of the portfolio, is predicated on different valuation assumptions and also an alternative approach to disposal that would maximise potential returns for RIFW.

The £30.9m figure has received a lot of publicity but the important point here is that in reaching this conclusion the District Valuer (and WAO) have moved away from a like for like comparison with the transaction that occurred and that this figure is *predicated on different valuation assumptions and also an alternative approach to disposal*. This means that the £30.9m figure used by the District Valuer and referred to in the Report cannot be directly compared with the actual amount achieved on sale.

Indeed the Report recognises this stating:

We acknowledge that RIFW's structure and remit were not designed to facilitate realisation of the maximum potential sale proceeds from its asset portfolio in the short-term....furthermore, RIFW's understanding of the assets' value was based upon a notional 'transfer value' set by the Welsh Government below the asset portfolio's market value and which was already known within the property market. Therefore, we consider it unlikely that RIFW could have disposed of the assets to achieve sale proceeds consistent with the District Valuer's market valuation. [added emphasis]

In effect, the District Valuer and WAO are suggesting that had different processes been adopted in the establishment of RIFW then different and better outcomes might have been achieved. Such views are of course heavily influenced by hindsight. AFML have a number of comments on the processes associated with the land portfolio in the following section. These views are not uncritical. In particular AFML have comments on the processes relating to:

- the establishment of RIFW with a land dowry;

- the decision to sell the portfolio;

4.1 Establishment of RIFW

The Report comments that *the RIFW investment concept was innovative and has many merits, but the need to sell property assets was a distraction from RIFW's core investment purpose*. AFML agrees with this view.

In hindsight (and obviously this decision pre-dated any AFML involvement in RIFW), it would have been much easier if Welsh Government had taken responsibility for selling the portfolio and then transferred the proceeds of sale to RIFW, particularly as the assets proved to be complex and management intensive (see para 3.10 to 3.13 of the Report). This would have allowed RIFW to focus fully on investing to create jobs. As Fund Manager, AFML was selected for its investment expertise.

RIFW was set up to promote investment. Its core mission is evident in its name – the Regeneration Investment Fund for Wales. It was to do this by investing cash into employment generative development. This inevitably focussed attention within RIFW on the need to turn the property assets it had had transferred to it into cash as soon as reasonably practicable in order to focus on its core investment function.

Ultimately AFML concurs with the WAO conclusion: *The need for RIFW to realise sufficient proceeds from property sales to fund its investment operations represented a significant distraction from its core purpose, to invest in regeneration schemes*.

4.2 Decision on the Sale of the Portfolio

The Report states that *RIFW wrongly believed that the whole asset portfolio had to be sold by December 2015* and, arguably, implies that this was a motivation behind seeking an early sale of the portfolio. Moreover the Report states that *Amber and LSH both maintain that ERDF match-funding placed a requirement upon RIFW to sell all of the property assets in order to invest the proceeds in regeneration projects by December 2015*. AFML does not accept the attribution to it of that remark. AFML has never maintained that position and is unaware of any reason that would justify the WAO assuming that it has. AFML does not believe that RIFW was under the impression that the portfolio had to be sold by the end of December 2015 simply for the purposes of ERDF match-funding.

Notwithstanding the foregoing, RIFW was under both a self-imposed pressure and an external pressure to realise the value within the property portfolio. This was not because of any misapprehension of EU legal requirements but because of the extent of the need for regeneration investment in the target areas of Wales. The sale discussion in the middle of 2011 took place against a backdrop of the following:

- A property market where land values were falling. In August 2011 the house price index was showing a 4.5% fall in house prices in Wales on an annualised basis. Indeed LSH were advising RIFW that there was a risk that the land portfolio might be worth less than the value at which it had been transferred to RIFW¹.
- The Welsh economy was contracting during the worst recession in a generation;

1

http://landregistry.data.gov.uk/app/hpi/view?from_m=0&from_y=2011&loc_0=Wales&loc_uri_0=http%3A%2F%2Flandregistry.data.gov.uk%2Fid%2Fregion%2Fwales&m_ap=1&m_chy=1&m_hpi=1&source=preview_form&to_m=11&to_y=2011

- Unemployment rates across all ages were at the highest levels seen across Wales in the period of recession;
- A strong political imperative to stimulate growth - “we are committed to getting people into jobs, and trying to keep people in their jobs” - First Minister Carwyn Jones in August 2011.”

Against this backdrop there was obvious pressure for RIFW to fulfil its core role and contribute to regenerative activity in the Wales economy. RIFW had a strong pipeline of opportunities to invest in regeneration projects. The WAO makes an illustrative comment that:

The quarterly reports prepared by Amber for the Board indicate that by early 2013 the stream of potential projects had strengthened and an increasing number of potential projects had been evaluated. The RIFW progress report to WEFO for the period ending 30 April 2013 documented that there were 62 projects at various stages of development.

There were therefore strong pressures on RIFW to ensure that it had the cash available to meet the expected calls on its resources and enable it to meet the anticipated stream of investment opportunities. The concern at the time was to ensure that the relatively illiquid land assets held by RIFW were turned into cash at a rate sufficient to ensure capital was available for RIFW to deploy into employment generative regeneration investment. In the view of AFML it was in the light of this position that the RIFW board made the decision to sell the property portfolio.

It is also important to appreciate that the sale of the portfolio proceeded on the basis of full external professional advice from RIFW’s investment manager. LSH, who acted as RIFW’s investment manager responsible for advising on property matters, is one of the largest property advisory businesses in the UK. The way this worked was for LSH to submit reports on property matters to AFML who then forwarded these (together with any other reports that AFML prepared relating to non-property matters) as part of a fuller board pack to RIFW.

Where the Report refers to AFML circulating papers to the board these were in fact (so far as they related to the land sale) papers prepared by LSH which were then on-sent by AFML to RIFW. Examination of the actual papers makes this process clear. While AFML is tasked with oversight of LSH, AFML is not qualified to comment on the specific content of LSH’s valuation advice but so far as it knows all LSH’s advice was acted upon by RIFW.

The RIFW board who considered these reports included members and observers who were themselves expert on property matters. In addition to members with such experience from the private sector the board included Welsh Government employees with direct experience of land transfers and had as a participant at all its meetings the individual who had had responsibility for the land portfolio while it was in the ownership of Welsh Government. The decisions made by RIFW relating to the sale were considered debated and supported by both board members and attendees.

AFML is of the view that the decision to sell the portfolio needs to be seen in the context of the time at which it was taken and the other pressures that RIFW was subject to in terms of its investment pipeline.

5. Other Comment

AFML would like to make one specific comment on paras 3.130 to 3.137 of the report which deal with the question of possible “state aid”. This is important as the WAO correctly state that *the Investment Management Agreement also required that both Amber and LSH should use their best endeavours to ensure compliance with EU requirements, including in relation to state aid.*

It is of obvious importance that the giving of unlawful state aid is avoided and AFML notes the recommendation that *the Welsh Government should investigate whether unlawful state aid has been provided.* Since this issue was first raised considerable time and expense has been incurred in obtaining both a legal opinion from a law firm and from a specialist QC which have given reassurance on this point.

While the comment of the WAO that: *...we are unable to place audit reliance upon either the legal opinion obtained by RIFW or the QC opinion...* is noted, AFML is not aware that the WAO has obtained any different legal advice.