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**SCOTTISH FUTURES TRUST LIMITED**

**LEGAL OPINION – CONCLUSION / NEXT STEPS**

Council Built Homes for Market Rent and Sale

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1 **INTRODUCTION**

1.1 The paragraphs in section 2 below are an extract from Burness Paull LLP’s legal opinion to Scottish Futures Trust Limited (“SFT”) on the legal basis and structure to support Council built homes for market rent and sale in Scotland. It has been set out as a separate document to give SFT, and the local authorities with which SFT engages, a flavour of the key issues explored in the legal opinion and recommendations as to the next steps to be taken to further establish a proof of concept that enables more homes to be delivered across Scotland with a broader mix of type and tenure that will meet local need.

1.2 It is not, however, a substitute for the full legal opinion, which explores these matters in some considerable detail and highlights that the legal position is not absolute: there are a number of dependencies and related risks which go to the facts and circumstances in which a given local authority operates – most critically, the needs of their communities and the evidence base for intervention.

1.3 This extract and the underlying legal opinion have been prepared solely for the benefit of SFT and may not be relied upon by any party other than SFT without our express written agreement. For the avoidance of any doubt, we understand that this extract and the opinion will be shared with third parties (including local authorities) for their consideration, but that such third parties will seek independent legal advice on the matters detailed.

2 **CONCLUSION / NEXT STEPS**

2.1 *Suitability of the Power to Advance Wellbeing*

2.1.1 We have considered a wide range of statutory powers and assessed their scope in the context of empowering local authorities to build homes for market rent and sale. There is, for the avoidance of any doubt, **no specific statutory provision** that allows local authorities to build out new housing for sale on the open market. While certain well established statutory powers afforded to local authorities (such as those set out in the Local Government (Scotland) Act 1973) offer a basis in law for certain activities that would form a necessary part of any development project (such as the power to acquire and dispose of land (with certain conditions)), there would be (we surmise) an uncomfortable gap in respect of other – ancillary, but necessary – activities in the context of these projects, such as (by way of illustration) the marketing of properties or factoring/property management. We see an attraction in seeking to rely on a more holistic, overarching, power that would support the **underlying objective**, thereby enabling multifaceted, supplementary activities to be captured, to the extent that they further that underlying objective.

- 2.1.2 With this in mind, we consider the wide-ranging **power to advance wellbeing**, as set out at section 20 of the Local Government in Scotland Act 2003, which gives local authorities in Scotland the statutory power to do **anything which they consider likely to promote or improve the wellbeing of its local authority area and/or persons within that area**, to have considerable merit.
- 2.1.3 Indeed, the Scottish Government expressly intended the wellbeing power to encourage innovation and partnership working, subject to sensible safeguards. Accordingly (and subject to those safeguards) it seems to us that a very clear and well evidenced business case in favour of the use of the power to advance wellbeing would offer a clearer and more transparent route to undertaking projects with an element of novelty, than seeking to proceed on the basis of piecemeal local authority powers for different elements of the project.
- 2.1.4 The power to advance wellbeing is, however, a permissive power: it only confers power where it does not conflict with other legal restrictions. There are, accordingly, a number of relevant limitations on the power and key safeguards to be considered and actioned by local authorities in their use of the power. First, however, we set out a number of preliminary matters to be discussed with Scottish Government, with a view to establishing a proof of concept.

## 2.2 *Preliminary matters - engagement, led by SFT, with Scottish Government*

- 2.2.1 **We have, in the context of our review of the limitations on the power to advance wellbeing, considered its interaction with the rules on local authority trading:** the power to advance wellbeing enables local authorities to provide goods and services, but not charge for them unless they are “*reasonable charges*”. Where a local authority does impose a charge in terms of the wellbeing power, it must publish its reason for doing so and an explanation of how it arrived at the amount of the charge. It must be clear that the power is not being used for the **purpose** of raising money. Local authorities should be mindful of that when developing their business case / economic strategy for use of the wellbeing power.
- 2.2.2 Where, however, a charge is imposed that generates an income which is greater than the costs of providing that service, it may be considered to be a **commercial activity**.
- 2.2.3 This is important because - while it is accepted that local authorities will not look to compete in the housing market purely for commercial objectives – in delivering the kinds of projects in contemplation here, there may be **particular activities** undertaken as part of that overarching objective that are, at least arguably, **trading activities**<sup>1</sup>. There is an **express prohibition** on using the wellbeing power to carry out trading operations which may be done under the Local Authorities (Goods and Services) Act 1970.

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<sup>1</sup> For example, the provision of market rental services; property management services; maintenance services, to name but a few.

- 2.2.4 It seems to us, then, that the power to advance wellbeing may be used to justify activities for which a reasonable charge is imposed, but where that activity **moves into the territory of trading**, it is the 1970 Act that applies, which is **potentially prohibitive**, subject to Scottish Ministers’ consent or a statutory limit being set on trading income<sup>2</sup> - something that the Scottish Government has not set to date, which effectively makes it zero.
- 2.2.5 To be clear, there are instances where local authorities in Scotland **do** engage in income-generating activities, but since (absent a statutory limit on income) there is nothing in the 1970 Act which allows for this without the consent of the Scottish Ministers, it must be recognised that any such trading – particularly where there is a significant level of income – could be open to challenge.
- 2.2.6 We refer above to there being an attraction in relying on a holistic, overarching, power that supports an underlying objective. We still consider this to be the preference, but given the potential “spectrum” here in terms of non-commercial/commercial activities involved in projects of this nature; with a critical tipping point where imposing “reasonable charges” goes beyond cost recovery, to the point at which it becomes commercial trading with members of the public, we think there is a clear need for **dialogue with Scottish Government**.
- 2.2.7 **As a preliminary step**, in order to move towards a proof-of concept – we think it is important that SFT (with support of interested local authorities) engages with Scottish Government on the interaction here with the rules on local authority trading – as well as, more generally, exploring the extent to which Government supports projects of this nature, in principle. In particular:
- (a) A first key question would be whether the Scottish Government is supportive, in principle, of the objective of local authorities developing housing for market rent or sale and whether they are comfortable with local authorities proceeding on the basis of the power to advance wellbeing<sup>3</sup>. Although not necessarily determinative, this could have a significant effect on local authorities’ confidence to undertake a project of this nature.
  - (b) Section 9 of the 2003 Act introduced special provision for local authorities to enter into agreements with any person for the construction or maintenance by the authority of any buildings or works. This section is, however, not yet in force – perhaps because the Scottish Ministers are yet to make regulations to restrict the exercise of this power. It is, to our mind, a helpful indication of the intention of lawmakers to accommodate this

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<sup>2</sup> Generated outside of public to public sector trading.

<sup>3</sup> Particularly, to seek assurance that “wellbeing” in the context of housing provision is considered to be broader than the statutory charitable purpose most often underpinning the activities of registered social landlords: “the relief of those in need by reason of age, ill-health, disability, financial hardship or other disadvantage” and actually encompasses the advancement of a higher level of quality of life.

kind of development activity by local authorities and may, therefore, be a useful reference point in dialogue with the Scottish Government.

- (c) It would be helpful to understand the Scottish Government's position on the distinction between "reasonable charges" under the 2003 Act and "trading operations" under the 1970 Act. There is potentially a spectrum of financial models between the two, and it would be helpful to understand how far along that spectrum "reasonable charges" can go before becoming a "trading operation".
- (d) To the extent necessary, it would be helpful to understand whether Scottish Government would, as a matter of principle, be prepared to consent to local authorities engaging in certain trading operations (or, indeed, setting a statutory limit on income), where the local authority is able to demonstrate that its intervention is limited to addressing the inactivity of the private sector (robustly evidenced) and if it is, what that evidence would need to comprise.
- (e) Finally, while we would generally hold to the view that a local authority cannot establish a separate entity with powers that go beyond that which a local authority is itself empowered to do, we would welcome a view from Scottish Government on whether it would be supportive of the argument that a separate entity (either wholly owned by a local authority or jointly with another party) may engage in trading without falling foul of the 1970 Act restrictions, providing that none of the profits are distributed to the local authority (ie. any income would be recycled by that entity and used in furtherance of that entity's activities). If Government was supportive of this argument, this might deal quite neatly with any overlap between the 1970 Act and the wellbeing power, and also provide a clear direction as to the preferred structure.
- (f) A variant of this, for exploration with Scottish Government, might see a wholly owned subsidiary of the local authority establishing a special purpose vehicle with a third party (most likely, an LLP with the subsidiary and third party as the two members) to deliver the market housing projects.

2.2.8 Subject to that preliminary dialogue, we consider it prudent for local authorities to consider whether they might be prepared to develop a business case/evidence base for reliance on the power to advance wellbeing for the development of market level housing in their area as a **stand alone initiative**; with a separate statutory powers justification for the provision of rental services (to the extent required and subject to Scottish Ministers' consent to this or an appropriate statutory income limit). If such consent/statutory limit is not forthcoming (and Scottish Government are not minded to provide direction on the alternative structures suggested above), local authorities may need to consider whether they would be prepared to develop housing to meet the needs of their communities, based on a suitable evidence base for use of

the wellbeing power (as set out below), but transfer that developed housing to a third party (for best consideration) to deliver the ongoing services. Conceivably, by developing the housing (including executing any necessary remedial site works), the local authority may have intervened sufficiently to draw in private sector interest.

### 2.3 *Ongoing Safeguards to be actioned by local authorities each time the power to advance wellbeing is implemented*

- 2.3.1 The power to advance wellbeing is not a power of general competence – **there are criteria to be satisfied by local authorities each and every time the power is utilised**. In particular, local authorities must demonstrate a **direct impact** on the wellbeing of citizens in the area, who could be said to benefit directly from the action taken under the wellbeing power. Local authorities must demonstrate, with specificity, how their area and/or the people living within it would directly benefit from this need being met by the local authority – ie. by the development of housing for market sale and rent by the local authority. Local authorities must have due regard to the criteria set out in the Scottish Government’s guidance on the power to advance wellbeing<sup>4</sup> and keep an audit trail that they have done so – ideally, by minuting the detail of the “key factors” listed in this guidance.
- 2.3.2 Local authorities should be able to clearly demonstrate that the benefit to the area/the people within it is the **primary objective** (ie. that it can be robustly evidenced that the activity is not for the purposes of enabling the local authority to raise money – any income generation is a secondary concern). Any charges imposed would need to be demonstrably **reasonable**, with a fully developed rationale for its charging structure and an explanation of how the amount of the charge was arrived at.
- 2.3.3 Local authorities must be able to demonstrate **why they consider their intervention to be necessary**. This will require identifying what the market has failed to provide, and demonstrating why it is in furtherance of the wellbeing of their area (and/or the people in it) for the local authority to use public funding to remedy that inactivity.
- 2.3.4 While consideration of key planning and housing documents such as the Housing Need and Demand Assessment (HNDA), Local Housing Strategy (LHS) and Local Development Plan (LDP) would provide a starting point for understanding market capacity and delivery against which market inactivity could be assessed, we do not think this, in and of itself, is sufficient. We consider that it would be necessary for local authorities to investigate fully the reasons for under-performance in the delivery of private housing in a particular area before its intervention can be robustly justified. We would also recommend that local authorities consider commissioning external advice from development consultants to establish whether development sites in the housing market area are viable from a housebuilder’s perspective. If it

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<https://www.webarchive.org.uk/wayback/archive/20150220071351/http://www.gov.scot/Publications/2004/04/19276/36157>

can be shown that sites are objectively viable but there is no developer interest in the sites, then that could provide support for local authority intervention.

2.3.5 A further way of establishing developer interest (or lack thereof) and of mitigating against the risk of challenge (considered in more detail below) in that respect would be to engage with the market by publishing a Prior Information Notice (“PIN”) on Public Contracts Scotland. Another route, albeit one which is slightly more unusual in this context, might be to procure a dynamic purchasing system (“DPS”). In principle, a DPS offers an open system in which interested market players can participate on an ongoing basis, which, at the very least, might help to evidence the absence of private sector interest over a period.

2.3.6 **Mitigating risk:** risk will, as a matter of course, present itself across projects in a number of guises: be it legal; financial; reputational; environmental; political; resource-based; practical etc and will be very much set within each local context. If, however, a local authority acts beyond the scope of the power to advance wellbeing, there may be grounds for this action to be challenged by judicial review. To mitigate against this, the key action is to ensure **proper decision-making**, which has taken account of key considerations including:

- (a) whether the local authority has the power to take the decision;
- (b) what **influencing factors** must and may be taken into account;
- (c) whether the decision is made in a **procedurally correct way** by an impartial and independent decision maker;
- (d) whether additional duties, such as the public sector equality duty, have been complied with;
- (e) whether the decision making process has been recorded, creating a robust audit trail.

2.3.7 In addition to ensuring a direct link has been established and ensuring that a robust evidence base exists for local authority intervention, further examples of relevant questions local authorities may wish to consider in the course of their decision-making are:

- (a) whether the land in question is already held for specific planning purposes;
- (b) whether the affordable housing needs of the local area are already sufficiently met;
- (c) whether the needs of homeless people in the local area are being sufficiently met by local authority services and accommodation;

- (d) whether the proposed development is in line with the best value obligations on the local authority and whether the proposed development adheres to the Scottish Government’s guidance on the best value concept;
- (e) whether due regard has been given to the way in which the proposed development supports the public sector equality duty;
- (f) whether the proposed development facilitates the provision of recreational, sporting, cultural and social facilities for the inhabitants of the local authority area; and
- (g) whether it furthers the aims of any local development plans which are in place.

2.3.8 Due consideration should be given to all of the above, along with any locale-specific considerations. In developing its justification, local authorities should be informed by, and be responsive to, the views of the people and communities in its area.

2.3.9 For example, Fife Council relied on the power to advance wellbeing in order to construct, advertise and sell private dwellings on part of a site which was used to develop new build residential accommodation for looked-after-children (Raithgates House). Fife Council’s approach in evidencing and justifying its decision included:

- (a) facilitating a drop-in event, at which members of the public were encouraged to engage with a number of options and subsequently respond to the Council’s written consultation on the decision;
- (b) minuting the fact that the Scottish Government’s guidance on the power to advance wellbeing had been considered and extracting the key factors mentioned in the guidance extracted for the purposes of recommending the course of action; and
- (c) recording, in considerable detail, how the young people living at Raithgates House would directly benefit from living as part of an integrated community – as opposed to the other options considered.

2.3.10 Another example is Edinburgh Living – a project of Edinburgh City Council and SFT – which has established two special purposes vehicles: one for market rent and one for mid-market rent. The aim of both is to increase housing supply for people on low and moderate incomes through the provision of housing – for both mid-market and market rent. We consider this focus on a particular category of persons in the local authority’s area to be a helpful example in the context of establishing an evidence base for intervention and in terms of identifying a clear need in the area (albeit, it is our understanding that the Council did not rely on the power to advance wellbeing in this context).



## 2.4 *Structures to Support Delivery*

- 2.4.1 Finally, in terms of next steps, local authorities should begin to consider the potential models and corporate structures to support delivery of housing development projects.
- 2.4.2 There are different options available to local authorities depending on their specific development aims, whether housing for market sale and/or market rent (recognising that local authorities that enter into tenancies directly (as opposed to through a subsidiary) would, by operation of law, enter into Scottish secure tenancies (in respect of which there is security of tenure and affordable rent levels, rather than the form of private residential tenancies available to private sector landlords)). The most appropriate option will vary according to context and preference, taking account of the best ways to manage the risk and to resource the project. We see the most appropriate structures that could be used as falling into three broad categories:
- (a) setting up a wholly owned subsidiary of the local authority;
  - (b) entering into an LLP with private or public sector members; or
  - (c) directly procuring contracts for works and services (which was the approach taken by Fife Council in the example referred to above).
- 2.4.3 One implication of each of these structures is where the procurement regulations would apply to any contracts for works or services. In the LLP model, if the LLP partner is to provide works or services (such as partnering with a housebuilder who would deliver the construction), the local authority would be required to procure the position of joint venture partner through a regulated procurement procedure. This is because the relevant contract would go hand in hand with the partner's membership of the LLP. Specific arrangements should also be considered in the context of the subsidy control regime as necessary.
- 2.4.4 We think it is conceivable that preliminary discussions with Scottish Government will involve consideration of an appropriate structure. While Scottish Government may not actually prescribe a particular model (and, in any event, local authorities will need to be comfortable with the structure as appropriate to its own context), principles may emerge from SFT's dialogue with Government that make one model more viable from a statutory powers perspective than another. For example, if Scottish Government indicates that it would be supportive of the argument that a separate entity (either wholly owned by a local authority or jointly with another party) may engage in trading without falling foul of the 1970 Act restrictions providing that none of the profits are distributed to the local authority, that may have a bearing on the choice of legal construct. Conversely, if Scottish Government indicates discomfort with the commerciality of the proposition here, and local authorities need to consider reducing the scope to – for example – the construction

of housing but not the ongoing provision of services, local authorities may be minded to procure contracts for works and manage those contracts in-house.