

CABINET**27 JULY 2020****LEASE FOR NEW OFFICES IN BIRKENHEAD COMMERCIAL DISTRICT**

Councillor Pat Hackett, Leader of the Council, said:

“Our plans for economic growth are about creating community wealth. They are about creating jobs and opportunities for local people, regenerating our commercial areas and inspiring ambition. Prosperous communities are happier, healthier and better places to live.

The proposals within this report set out the next steps for taking forward the strategic regeneration objectives of the Wirral Growth Company for Central Birkenhead.”

REPORT SUMMARY

This is an update report following approval by Cabinet its meeting of 24 February 2020 of the Wirral Growth Company LLP Partnership Business Plan. Council officers have been working with the Wirral Growth Company LLP to finalise the location of the proposed new Birkenhead Commercial District. This development is to be underpinned by the Council taking a lease of space anticipated to be approximately 150,000 sq. ft net for a period of approximately 40 years, with a maximum rent payment period of 35 years to enable funding for future re-developments by the Wirral Growth Company LLP.

Whilst the business case for this development was approved by Cabinet at its meeting of 24 February 2020 the report recommends to members that there should be no significant delay in proceeding with the above lease arrangements, notwithstanding the economic effects of the Covid 19 pandemic.

This report seeks authority for the Director of Law and Governance to negotiate and finalise the terms of the lease structure in consultation with the Director of Regeneration and Place and enter into a conditional agreement for the lease and such other documentation as may be reasonably necessary to progress the proposed lease structure. There are also consequential recommendations regarding the appointment of contractors and the amendment of the Milestones for entering into the agreement for lease.

This matter affects all wards within the borough and the decisions are Key Decisions.

EXEMPT INFORMATION

This report contains exempt information in Appendix 1 and 4 as defined in Schedule 12A of the Local Government Act 1972. It is in the public interest to exclude the press and public

under Paragraph 3 'Information relating to the financial or business affairs of any particular person (including the authority holding the information)'.

Appendix 1 includes the Wirral Growth Company Partnership Business Plan.

Appendix 4 includes extracts from a report detailing sensitive commercial information

RECOMMENDATIONS

It is recommended that Cabinet approves:

1. The appointment of the following consultants on the design and delivery of the new offices, in accordance with the terms of the Wirral Growth Company Partnership Agreement:
 - (a) Building Contractor- Morgan Sindell
 - (b) Architect - AHR Architects Limited
 - (c) Civil and Structural Engineer- Curtins Consulting Limited
 - (d) Fire Engineer - Design Fire Consultants Limited
 - (e) M&E Engineer, BREEAM and Acoustics- Hannan Associates Limited
 - (f) Contract Administrator- Walker Sime Limited
 - (g) Quantity Surveyor- Abacus Cost Management Limited
 - (h) Health and Safety Auditor - Walker Sime Limited
 - (i) Landscape Architect – Gillespies LLP
 - (j) Ecology – United Environmental Services Limited
 - (k) Highways - Vectos
 - (l) Rights of light and Party Wall -GIA
 - (m) Planning - Barton Willmore Planning Limited
2. The granting of authority to the Director of Law and Governance in consultation with the Director of Regeneration and Place to:
 - (a) negotiate and agree and finalise the terms of a lease of the land shown edged red on the plan attached at Appendix 2 to Wirral Growth Company LLP or such funder as may be appointed by Wirral Growth Company LLP together with a lease back to the Council of the land and/or the completed office development (of approximately 150,000 sq. ft) within the parameters set out at paragraph 1.3 of the report;
 - (b) negotiate and agree and finalise amendment of the Milestones in the Partnership Agreement and the Partnership Business Plan to reflect the revised timescales for the entering into of the agreement for lease as set out at paragraph 1.4 of the report;

SUPPORTING INFORMATION

1.0 REASON/S FOR RECOMMENDATIONS

- 1.1 The Council is a partner in the joint venture vehicle, Wirral Growth Company LLP. The Partnership Business Plan of the Wirral Growth Company LLP was approved by Cabinet at its meeting of 24 February 2020. This approved plan is Appendix 1 to this report (Appendix 1 contains exempt information as defined in paragraph 3 of Schedule 12A of the Local Government Act 1972).
- 1.2 The principle of a sale and leaseback was referred to in the Partnership Business Plan. Whilst the principle of acquiring the property under the leaseback arrangement is a commitment that was made by Cabinet at its meeting of 24 February 2020, now that the detailed drafting of the legal documents is approaching finalisation it is necessary to seek authority from Cabinet to proceed, on the basis of the terms that have been agreed.
- 1.3 Authority is sought for the Director of Law and Governance, in consultation with the Director of Regeneration and Place, to negotiate and agree terms of a lease of the land shown edged red on the plan (attached at Appendix 2 to this report) to Wirral Growth Company LLP or such funder as may be appointed by Wirral Growth Company LLP together with a lease back to the Council of the land and/or the completed office development (of approximately 150,000 sq. ft) within the following parameters:
 - (a) The land acquired or to be acquired at Milton Pavements shall be added to the Option Agreement with the Wirral Growth Company LLP on the basis that the Wirral Growth Company LLP may not acquire it at less than the amount the Council pays for it and on the basis of the existing option agreement conditions, with such specific changes as may be needed to accommodate the proposed structure of the annuity lease;
 - (b) The lease back to the Council from the Wirral Growth Company LLP or the funder shall be at no more than the rent per square foot set out in the approved Partnership Business Plan as set out in the exempt Appendix 1 to this report;
 - (c) The conditions that apply to the option agreement currently shall apply to the sale and leaseback arrangement so that the viability tests and planning tests and other tests that apply to the working arrangements of the Wirral Growth Company LLP apply to the annuity lease structure.
- 1.4 There are a number of milestones set out in the Partnership Agreement and the Partnership Business Plan. One of these, relating to the timescale for the lease, is the subject of a recommendation to seek agreement for it to be amended. The current timescales are for an agreement for lease to be entered into by 30 June 2020 albeit the parties have informally agreed an extension on that date to 31 August 2020. Authority is therefore also sought for the Director of Law and Governance, in consultation with the Director of Regeneration and Place to agree and finalise amendments to the Milestones in the Partnership Agreement and the Partnership Business Plan, to reflect the revised timescales for the entering into of the agreement for lease.

- 1.5 A report on the proposed legal structure (less sensitive information) is attached to this report as Appendix 3. Extracts from the report on the proposed legal structure with the sensitive information is attached as Appendix 4 (Appendix 4 contains exempt information as defined in paragraph 3 of Schedule 12A of the Local Government Act 1972).
- 1.6 The Council has a right within the partnership agreement to require a formal procurement process in relation to various service providers where it is taking on premises itself as a tenant. The Council has the ability to waive that right if considered appropriate. It is considered that it would not be feasible to carry out a formal procurement exercise within the available time frame. Authority is therefore sought for the appointment of the following consultants on the design and delivery of the new offices, in accordance with the terms of the Wirral Growth Company Partnership Agreement:
- (a) Building Contractor- Morgan Sindell
 - (b) Architect - AHR Architects Limited
 - (c) Civil and Structural Engineer - Curtins Consulting Limited
 - (d) Fire Engineer - Design Fire Consultants Limited
 - (e) M&E Engineer, BREEAM and Acoustics - Hannan Associates Limited
 - (f) Contract Administrator - Walker Sime Limited
 - (g) Quantity Surveyor - Abacus Cost Management Limited
 - (h) Health and Safety Auditor - Walker Sime Limited
 - (i) Landscape Architect – Gillespies LLP
 - (j) Ecology – United Environmental Services Limited
 - (k) Highways - Vectos
 - (l) Rights of light and Party Wall - GIA
 - (m) Planning - Barton Willmore Planning Limited- pre procured.
- 1.7 All the above consultants (other than the fire consultants) have already been pre-approved by the Council. Costings are considered to be reasonable and competitive.
- 1.8 The agreement for lease would be entered into by the Wirral Growth Company which would procure the development of the site, appoint the building contractor and the professional team. Once a Funder has agreed with the Wirral Growth Company to fund the development, Wirral Growth Company's interest in the land would be transferred to the Funder.

2.0 OTHER OPTIONS CONSIDERED

- 2.1 To not enter into the agreement for lease- In these circumstances the Council would be exposed to a claim that it had breached the partnership agreement and this would trigger a potential compensation payment to its Joint Venture Partner. This option is therefore not recommended.
- 2.2 Revisit the means of financing with a view to an outright purchase of the property. This is not recommended as the merits of such an option were fully considered in by Cabinet in the report of 24 February 2020. Whilst financing a purchase via the Public Works Loan Board was considered, the Council would be directly funding the preparation and construction costs from day one, placing a liability on the Council. The annuity lease mechanism means the forward funder would be funding this. Also, the timing of payments with lower amounts under the annuity lease in the early and mid-

term life of the asset mean that the annuity lease is predicted to result in lower cost on a net present value discounted cash flow basis. Cabinet agreed the recommendations in the report that an annuity lease option would be the better option. It is considered that there have been no significant changes in circumstances requiring the above appraisal to be re-considered.

- 2.3 To arrange for a funder to have the obligation to fit out the offices space- Whilst this is technically possible, it is considered that no funder would invest on the basis of such an obligation.

3.0 BACKGROUND INFORMATION

- 3.1 On 24 February 2020 Cabinet resolved (amongst other matters) that:

(1) the Wirral Growth Company Y1-3 Partnership Business Plan be approved, noting that it will be updated and reviewed on an annual basis.

(4) it be noted that the Birkenhead Commercial District 'redline' for town centre site development had been extended to include Birkenhead Market, recently acquired land (B&M stores) and land which the Council was in the process of acquiring (Milton Pavements).....

(5) the Birkenhead Commercial District Full Business Case be approved, specifically:

- approves funding arrangements set out in the report (annuity lease) as the preferred funding route;
- delegates authority to the S151 Officer, through the Wirral Growth Company, to appoint a commercial investment advisor to commence marketing of the investment opportunity; and
- notes the use of forecast business rates income generated from the BCD phase 1 as a funding contribution to the project

- 3.2 This report seeks authority to undertake the next steps in the funding process already authorised and to locate the development on land that is in the process of being acquired.

- 3.3 Since the commencement of the Covid 19 pandemic Council, the Director of Regeneration and Place commissioned a Business Case Review from Avison Young. The report concluded that there will be a need for changes in working practices and adjustments to our workplaces. Office occupation densities will be reduced, at least temporarily to reflect social distancing along with a reliance on video calls. There will be a need for smart buildings that can effectively harness data and technology to monitor, manage and minimise the risks for individuals.

- 3.4 Avison Young have concluded that the strategic justification for this project remains relevant. The supply of Grade A office space in Birkenhead remains an issue in establishing an office market in the area. This was the case prior to Covid19 and will remain as an issue afterwards. The office space will remain vital for the continuation and delivery of the overall regeneration framework for Birkenhead. Investors will therefore continue to have a strong appetite for the head lease structure approved in support of the Birkenhead Commercial District Business Case, despite relative uncertainty in the market

- 3.5 The conclusions that Avison Young have reached are considered sound. It would be appropriate for a further report to be taken to members in the Autumn 2020 regarding further amendments to the milestones and any necessary further adjustments to the Partnership Business Plan and Agreement. There will also be an ongoing process of consultation with members and workshops regarding this vitally important project.

4.0 FINANCIAL IMPLICATIONS

- 4.1 The proposed annuity lease will commit the Council to paying rent each year for the rest of the lease. It will not be possible for the Council to transfer this liability. The rent will be calculated on the basis of an amount per square foot. In addition to rent, the Council will have all repair costs, replacement costs and servicing costs. The proposed rent per square foot is as set out in the exempt Partnership Business Plan. The Council would retain any rental from sub tenants including any amounts in excess of the annuity lease rental payment.
- 4.2 The Council will be committed to paying a head lease rental which will be subject to an annual inflationary increase with limits within a 'collar and cap' likely of 1% to 4%. This will be a revenue cost to the Council. Costs will be funded from savings generated from the vacating of existing buildings and revised working arrangements and from income from sub-letting of space. These amounts are calculated to cover the costs and produce net savings. The approach and upside and downside risk was detailed in the Birkenhead Commercial District Business Full Business Case agreed by Cabinet on 24th February 2020.
- 4.3 The Council has a potential liability as tenant to pay stamp duty land tax. This is projected at worse case to be in excess of one million pounds in the case of the annuity lease. There are tax reliefs that may apply and scope to argue that relief can be claimed to reduce the stamp duty land tax liability to zero. The arguments will need to be put at the time of acquisition and will be based on the then current tax regime. The Birkenhead Commercial District Business Case approved by Cabinet on 24 February 2020, based on information available at the time, assumed stamp duty land tax of £842,000. Since then, work has been undertaken to reduce this potential liability and it is possible but not guaranteed (as it is subject to HMRC approval) that this may reduce to zero.
- 4.4 The lease will be of the shell only with fit out costs being separate. The Council will therefore need to pay for fit out costs of the building. This was detailed in the Birkenhead Commercial District Full Business Case approved by Cabinet on 24 February 2020. Fit out costs would be funded from the capital programme with costs spread out across the life of the asset. This will be subject to a separate capital programme bid.
- 4.5 A contingency sum will be included within the 2021/22 budget to allow funding for mitigation against market rental risk from void periods or other non-payment or shortfall in rent. In terms of upside risk, the Council will benefit from the retention of 100% of any rental amounts from sub-tenants that are above the head lease rental level.

- 4.6 The Council will be responsible to put disrepair right at its own cost. The Council will need to make provision in the budget at the appropriate time for such costs.
- 4.7 The Birkenhead Commercial District Full Business Case approved in February 2020 stated that the Council may be required to offer incentive packages to sub-tenants. This would most likely entail rent free periods or other assistance. This is a standard feature of lettings. Values would be dependent upon negotiation and be linked to lease terms. Under current accounting conventions the costs of any incentives can be spread across the life of the asset allowing any revenue impact to be minimised.

5.0 LEGAL IMPLICATIONS

- 5.1 The point at which the title to the land at Milton Pavements is transferred to Wirral Growth Company will follow the principles in the Option Agreement. A number of pre-conditions will need to be satisfied and the resulting price paid will need to be compliant with the duty to obtain the best price reasonably obtainable as required by section 123 of the Local Government Act 1972. Other conditions may be necessary to protect the Council. In addition, the Council is seeking to ensure that the amount it pays out for Milton Pavements is reimbursed to it by the LLP at the point of transfer to the LLP.
- 5.2 The annuity lease will not be transferable. All the commitments that are undertaken in the lease by the Council will remain the responsibility of the Council.
- 5.3 The principal terms of the leaseback to the Council are in the document at Appendix 3. Of particular note is the obligation to repair, rebuild and replace the building in the event of damage or destruction. Even if a disrepair is not the fault of the Council, the Council must still put it right at its own cost.
- 5.4 The Council will need to have appropriate forms of warranties from the building contractor and professionals to ensure it has assurance on design and construction. It will also need to incorporate rights for it to step in to complete any build project in the event of any insolvency in the supply chain. As its contract will be with its Joint Venture partner, in principle, the risk of a part built project is less likely to apply.
- 5.5 Rent will be payable whether or not premises can be occupied. If for example a pandemic meant premises could not be occupied, rent would still be payable. This event is unlikely to be something the Council can insure against. The only mitigation for rent will be if the Council chooses to and is permitted by its landlord to sublet parts of the building to generate a rental income. However, if the sub-tenant fails to pay its rent for any reason the Council will still be liable for the full rent to the landlord of the building.
- 5.6 At the end of the lease term, the Council will have the ability to own the freehold of the site again for no cost and will no longer be liable to pay any rent.
- 5.7 The Council cannot control the identity of its landlord. A landlord may be any investment type vehicle based in any jurisdiction.
- 5.8 The Option agreement and partnership agreement provide a number of protections for the Council and give it oversight on viability. Those protections are to continue to apply

and the Site Development Plan process will need to be adhered to so that any final Site Development Plan is brought back to the correct Council decision maker.

6.0 RESOURCE IMPLICATIONS: STAFFING, ICT AND ASSETS

- 6.1 Avison Young are appointed as advisers on the letting strategy of the new offices and will be responsible for management of this aspect.
- 6.2 External lawyers have been appointed to advise on the Stamp Duty Land Tax, deal structure and negotiating the lease and lease back.

7.0 RELEVANT RISKS

- 7.1 The lease and leaseback structure entails several risks. These are in the table below.

Risk	Risk of occurrence	Impact	Action to mitigate in advance	Action to mitigate if event occurs
<u>Planning and Design</u>				
Failure to secure planning permission within the timescales	Low	High	Engage with planning officers as soon as possible to map any potential constraints and objections.	Review and revise planning strategy through engagement with the planning officers.
Changes in national and local planning policy and strategy	Moderate	Moderate	Engage within the Council to ensure that appropriate changes are made to draft policies where necessary to facilitate site delivery.	Revise planning strategy to reflect new policy requirements.
Planning obligations (S.278) impacting viability	Moderate	High	Identify possible heads of terms early, understand likely impact on viability, develop robust negotiation strategy and engage with LPA early.	Assess level and type of impact, agree extent to which issues need to be addressed, design and implement strategy for negotiating amendments.
Judicial Review	Low	High	Ensure application is technically robust (if needs be with legal review prior to application submission). Ensure Council processes application in sound manner and all procedures correctly followed.	Instruct legal team to defend challenge and seek early dismissal by the Courts.

Risk	Risk of occurrence	Impact	Action to mitigate in advance	Action to mitigate if event occurs
<u>Political</u>				
Change in political control at Wirral Borough Council.	Low	Moderate	Monitor political position – forward plan working with officers.	Evaluate any changes in political instruction and revise strategy and programme accordingly.
<u>Market/ Commercial</u>				
Market uncertainty negatively impacting on rate of take-up, rents, yields and incentives	High/ moderate	High	Implementation of a Commercial letting strategy in place to mitigate commercial risk.	Assess extent of potential impact and revise strategy and timetable to reflect changed circumstances if needed.
Lack of long-term investor appetite	Low	High	Soft market testing of the investment opportunity and awareness raising of the opportunity at an appropriate time to ensure the proposition adequately responds to the market.	Assess extent of potential impact and revise viability strategy and timetable to reflect changed circumstances if needed.
Surplus office supply and competing sites impacting ability to deliver	Moderate/ Low	Moderate /High	Continually monitor pipeline of sites/schemes and delivery programmes to ensure the opportunity is offered at an appropriate time.	Assess extent of potential impact and revise strategy and timetable to reflect changed circumstances if needed.
Poor viability of scheme as a result of high enabling costs, and environmental issues negatively impacting on marketability	Moderate	Moderate	Procure all necessary works and engage with third parties to understand enabling and infrastructure costs and impact on development	Seek to secure external grant funding support for the enabling and infrastructure costs. Liaise with third party stakeholders on any financial support that can be provided
Cost Inflation on infrastructure and/or build costs negatively	Moderate	Moderate	Monitor economic position through Research Team, and run sensitivities on	Seek to secure external grant funding support for the enabling and

Risk	Risk of occurrence	Impact	Action to mitigate in advance	Action to mitigate if event occurs
impacting on viability.			appraisals completed to understand viability tolerances,	infrastructure costs. Liaise with third party stakeholders on any financial support that can be provided
Economic downturn / Recession	Moderate / High	Moderate / High	Prepare contingency plan and monitor economic position regularly via Research Team, relating this to the timing of the development	Assess extent of potential impact and revise strategy and timetable to reflect changed circumstances.
<u>Procurement</u>				
Financial stability of the main contractor/ risk of administration	Moderate/ High	High	Ensuring there is a clear strategy set out within the Developer/ Contractor agreement with financial management checks.	

8.0 ENGAGEMENT/CONSULTATION

- 8.1 The Council has previously undertaken consultation in relation to this project and these offices form part of this. A separate consultation for the action recommended by this report is not required.

9.0 EQUALITY IMPLICATIONS

- 9.1 The equality impact assessment associated with this report can be accessed here: <https://www.wirral.gov.uk/communities-and-neighbourhoods/equality-impact-assessments/equality-impact-assessments-2017/busine-0>

10.0 ENVIRONMENT AND CLIMATE IMPLICATIONS

- 10.1 Design of the office buildings will take into account the Council's response to the environment and climate emergency by promoting energy efficiency. Office buildings proposed will be designed and built to BREEAM Excellent standards

REPORT AUTHOR:

Philip McCourt, Director of Law and Governance.

APPENDICES

- Appendix 1 – Wirral Growth Company Partnership Business Plan (exempt)
Appendix 2- Site plan for the Birkenhead Commercial District Offices

Appendix 3- Report on the proposed Legal structure (less sensitive information)

Appendix 4- Extracts from report on the proposed legal structure with sensitive information (exempt)

BACKGROUND PAPERS

JV Options Agreement (Exempt)

Wirral Growth Company Y1-3 Partnership Business Plan approved (Exempt)

Background working papers as referred to in the Partnership Business Plan (Exempt)

Birkenhead Commercial District Full Business Case (Exempt)

SUBJECT HISTORY (last 3 years)

Council Meeting	Date
Cabinet – Property Company Strategic Options Report	27/02/17
Cabinet – Property Company Full Business Case (FBC)	19/06/17
Cabinet – Preferred Bidder decision	28/02/18
Cabinet – Draft BCD Business Case and Staff Relocation FBC	26/11/18
Cabinet – Land Assembly to support BCD	04/11/19
Cabinet -Wirral Growth Company	24/02/20