

WIRRAL COUNCIL

CABINET

12 MARCH 2015

SUBJECT:	CREATION OF A PROPERTY DEVELOPMENT FRAMEWORK
WARDS AFFECTED:	POTENTIALLY ALL WARDS WILL BE AFFECTED BY THIS REPORT
REPORT OF:	STRATEGIC DIRECTOR REGENERATION & ENVIRONMENT
RESPONSIBLE PORTFOLIO HOLDER:	CLLR PHIL DAVIES INVESTMENT
KEY DECISION	YES

1.0 EXECUTIVE SUMMARY

- 1.1 This report seeks Members approval to create a Property Development Framework that would support the development of new commercial floor space in Wirral. The Framework would set out a number of alternative development models that could be used to address the economic viability of projects where the build costs are greater than the end value. This proposal would enable commercial projects to be delivered thereby meeting the objectives of the Council's Investment Strategy.

2.0 BACKGROUND

- 2.1 The industrial and office property market in the Liverpool City Region faces challenges with end values remaining relatively low and grant funding still being required to enable developments to take place. That is the total cost of constructing speculative and bespoke accommodation is currently greater than its value on completion. The issue is further compounded by banks often refusing to lend against any kind of speculative development and limiting their lending against bespoke schemes, with a known end user, to a maximum of 60% of the projected end value. One of the other constraining factors moving forward is the fact that the availability of external grant funding from organisations including the UK Government and the European Union is reducing significantly.
- 2.2 This means that some of Wirral's indigenous companies who want to expand or grow are unable to do so due to the lack of suitable accommodation and the lack of new modern premises is also a limiting factor to the Council's aspirations of attracting new inward investment into the Borough.
- 2.3 In response to these circumstances, the Council has been reviewing the current models that are available to it in terms of supporting private sector development and company growth, as well as exploring new ways of supporting such developments. The motivation for doing this comes from the Council's ambitious Investment Strategy which is seeking to grow Wirral's economy as well as providing sustainable employment opportunities for all Wirral residents.

A REVIEW OF EXISTING DEVELOPMENT MODELS

- 2.4 The Council has successfully used a number of traditional ways of supporting private sector development which can still provide some opportunities for future developments. These are considered below:
- 2.5 **Land Acquisition / Assembly.** The Council has used this method in the past to buy land and property and then sell it on to the private sector. Strategically, this approach allows the Council to intervene in the marketplace to catalyse or kickstart development, but also to assemble land in preparation for development. This may, in certain circumstances, still be an appropriate approach but it does require the Council to identify significant financial resources to buy the land in the first place and if the sell-on price, because of land values, is only equal to the purchase price this provides the Council with little if no return on its investment.
- 2.6 **Gap funding.** Gap funding is required where there is a difference between values and costs with a grant being given to gap fund the difference between the construction costs and end value. Such an approach is subject to State Aid and therefore only a percentage of the gap can be funded. This has been further affected by changes to the State Aid framework in 2014. However, depending on the project the public sector can still intervene and land remediation is an example of how this can work to support large companies.
- 2.7 This approach has proved successful in Wirral and again, in certain circumstances, may still be the most appropriate response. However, funding is required to provide a grant and there is no return on this investment. There are external funds which the Council can utilise, for example through the growth deal secured for the Liverpool City Region which is yet to be allocated to projects, but resources for this are significantly reduced when compared to previous years.

NEW DEVELOPMENT MODEL

- 2.8 **Council Head Lease.** This approach is based on using the strength of the Council's covenant to secure development. An example of how such an approach would work is that the Council agrees with Developer A to take out a head-lease on a proposed new building(s) for a period of years. For this period the Council agrees to pay the rent at an agreed figure including periodic reviews. At the same time, in a back to back arrangement, the Council agrees to lease the building to a company for the same period of time for a market rent plus a premium. This premium can be achieved because of the strength of the Council's covenant which allows money to be borrowed at a lower interest rate than would be available to a developer.
- 2.9 Such an approach should not require any up-front committed funding from the Council and the premium would result in a nominal revenue income for the Council. However, this is not without risk and there would be a need to ensure that a contingency fund was in place to cover any void periods and this is set out in detail in paragraph 8.4 below.
- 2.10 Table 1 below sets out these three Development Models and the risks associated with each of them is addressed in Section 3 below.

TABLE 1 – Overview of Development Models

OPTION	DESCRIPTION	CONSTRAINTS
1. Site/ Acquisition Land Assembly	To strategically intervene in the marketplace to address constraints causing barriers to the private sector. This may include land assembly to create developable parcels of land	Lack of available funding to support this type of option. Little or no return on the outlay.
2. GAP Funding	To address viability gaps by bridging the 'gap' between development costs and end values.	Again, the lack of available funding for this option presents a problem. However, the LCR LEP has been allocated some resources through the Growth Deal.
3. Council Head Lease	<p>Covenant strength allows a developer to secure higher levels of funding for a development, strengthening the yield of a development and addressing viability in a different way from GAP funding.</p> <p>The Council taking the head lease for a new developing significantly increases the viability of a development from the point of view of securing funding</p>	Using the Council's covenant strength in this way brings opportunities and risks. It exposes the Council to potential costs if the sub lease ends and there are void periods. However, mitigating actions can be put into place and the risk depends on the development plus the potential return for the Council.

2.11 It is proposed that a multi-disciplinary team of officers from Finance, Legal, Investment Strategy, Regeneration and Asset Management would work on the development and the implementation of the Property Development Framework which would include:

- Outlining in detail each of the delivery models set out in the above Table (Table 1);
- Setting out the criteria against which projects would be initially assessed for inclusion – namely that they would generate financial returns, floorspace, jobs, business rates income and/or be a catalyst for future development;
- Identification of potential sources of funding as outlined in 2.12.below.

2.12 Funding to progress projects within the Framework could come from a variety of sources and could include external funds such as resources identified through the Liverpool City Region's Growth Plan, or Government schemes such as Growing Places funding. The Council's Capital Programme could also be considered as a possible source of funding for specific projects. In addition funding generated by the retention of business rates within the Enterprise Zone could also be considered for re-investment into further developments (this is set out in more detail in a separate report on the Enterprise Zone on this agenda).

- 2.13 Projects coming forward through the Property Development Framework would be considered on a case by case basis in respect of the most appropriate development model and of the type of funding that could be secured. Each project would then be brought back to Cabinet with a detailed report for consideration and approval before being progressed. The report would include an assessment by the internal multi-disciplinary team of a comprehensive independent appraisal of the total project costs and end value of each scheme, a proposal as to the most appropriate delivery model and a proposal with regards to the funding route. The report would also set out how the proposal would comply with all financial and legal requirements.

3.0 RELEVANT RISKS

- 3.1 **Site acquisition/assembly and Gap funding.** The Council has a strong track record of delivering these approaches. Wirral International Business Park was created using both of these options during the 1990's and early 2000's. Since 2007, the Council has successfully worked in partnership on a number of occasions to develop and bring forward new commercial floor space with the latest one being Tower Wharf, funded using European Regional Development Fund monies. The key risk to this approach is the lack of available funding.
- 3.2 **Council Head Lease.** This approach has risks, as indeed are experienced by all such approaches to securing development. The main risk is that the company to whom the Council lease goes into receivership or liquidation at some point during the lease period. This would leave the Council in the position of still having to pay the rental amount for the period remaining on the lease as well as potentially needing to make good the building and make any alterations that might be required to meet business demand. This risk is higher in the early years when there are more years remaining on the lease and the risk will reduce as the lease period progresses. However, risk will remain until the lease period ends.
- 3.3 The risks would be mitigated by the following:
- a) a thorough independent financial check on the company prior to entering into the lease;
 - b) an independent market appraisal of the demand for the type of space which was provided by the project should it be required to be re-let. Such an appraisal would be reviewed on an annual basis;
 - b) an annual check on the company's performance by the Council;
 - c) the ability for the Council to re-lease the building should the original leaseholder go into liquidation or receivership;
 - d) in such circumstances the Council would be able to sub-divide a large building into smaller units making re-leasing easier and reducing void periods through the provisions that would be negotiated with the developer prior to the lease being entered into by the Council;
 - e) the Council identifying a financial resource to cover any void periods if the original leaseholder went into liquidation or receivership and prior to a new lease or leases being entered into. This financial resource would only be required in these circumstances;
 - f) A project group, including the Director of Resources, would monitor the number of projects undertaken using this approach and report on the Council's levels of risk as part of normal reporting procedures;

g) Members would approve all projects brought forward through the Property Development Framework.

3.4 The benefit to the Council of using its covenant strength is that this is a mechanism to ensure that a development can be implemented thereby providing new business space and creating employment opportunities. In addition the new floor space will generate revenue for the Council through the rental premium and through business rates.

4.0 OTHER OPTIONS CONSIDERED

4.1 Officers will continue to seek to secure external funds wherever possible to address the constraints to development identified in paragraph 2.1 of this report and to bring forward investment. Again, where a business case can be put forward and projects could generate returns, either financially or through floorspace, jobs and business rates income, then officers will report to Cabinet.

5.0 CONSULTATION

5.1 This report is consistent with the principles of Wirral Council's Investment Strategy which provides the framework for securing investment and growth within the Borough. This has been reviewed after extensive consultation with partners and has also been informed by consultation which has taken place with a number of private sector partners and local businesses through Invest Wirral's Business Forum.

6.0 OUTSTANDING PREVIOUSLY APPROVED ACTIONS

6.1 None

7.0 IMPLICATIONS FOR VOLUNTARY, COMMUNITY AND FAITH GROUPS

7.1 There are no implications for Voluntary, Community and Faith Groups arising directly from this report.

8.0 RESOURCE IMPLICATIONS, FINANCIAL, IT, STAFFING AND ASSETS

8.1 A multi-disciplinary team of officers from Finance, Legal, Investment Strategy, Regeneration and Asset Management would work on the implementation of the Property Development Framework.

8.2 Officers will seek and secure best practice advice from other Local Authorities currently delivering projects using such development models, but it is likely that specialist legal, finance and commercial property specialists would need to be procured as appropriate. Officers will seek to recover these costs from the projects where appropriate.

8.3 As set out in paragraph 3.3 (g) above, any project progressed through the property development framework will be brought back to Cabinet in a business case form. This business case would include a proposal for where funds would be sought, for example whether it is using external resources, for example the Pension Fund, the Council's own funds such as the Capital Programme or the potential re-investment of the business rate uplift from the Enterprise Zone.

- 8.4 In respect of Option 3, the Council Head Lease, if Members agreed to the use of this approach for a development then a contingency budget would be required to minimise the risks should there be any void periods where the property was empty ie if the company leasing the building from the Council defaulted on that lease. The resource would be needed to (a) pay the rent to the developer for the period that the unit was vacant (2) to do any works of sub-division prior to re-marketing the building and (3) re-market the building. It is proposed that the sum of £700,000 would be required for this purpose and this would be made available from reserves from the Working Neighbourhoods Fund. In addition any surplus made by the Council from the rental charged through the Head Lease arrangement would be reinvested into the contingency reserve. This would be reviewed on an annual basis as part of the annual performance report.
- 8.5 Resource implications relating to the re-investment of Business Rates from the Enterprise Zone is addressed in the Enterprise Zone report elsewhere on this agenda.

9.0 LEGAL IMPLICATIONS

- 9.1 The creation of a Property Development Framework to support the development of new commercial floor space in Wirral will (as appropriate) require the Council to rely on the Council's ability to:
- (a) acquire land by agreement for the benefit, improvement or development of their area pursuant to section 120 of the Local Government Act 1972;
 - (b) dispose of land pursuant to section 123 of the Local Government Act 1972;
 - (c) borrow money for the purposes of the prudent management of its financial affairs pursuant to section 1 of the Local Government Act 2003; and
 - (d) invest for the purposes of the prudent management of its financial affairs pursuant to section 12 of the Local Government Act 2003.
- 9.2 The Council intends to ensure that the operation of the Framework complies with:
- (a) the application of the legal requirements set out in paragraph 9.1 above;
 - (b) the application of the Public Contracts Regulations 2015;
 - (c) State Aid requirements;
 - (d) the Council's constitution; and
 - (e) such other legal requirements relating to the project under consideration.
- 9.3 The report requesting Cabinet approval for each project shall set out how the legal requirements have been and/or will be satisfied and the operation of the Framework shall require Cabinet approval for each and every project.

10.0 EQUALITY IMPLICATIONS

10.1 The potential impact has been reviewed with regard to equality and links to the existing EIA conducted for Wirral's Investment Strategy.

<http://www.wirral.gov.uk/my-services/community-and-living/equality-diversity-cohesion/equality-impact-assessments/eias-2010-0>

11.0 CARBON REDUCTION IMPLICATIONS

11.1 There are no carbon reduction implications arising directly out of this report.

12.0 PLANNING AND COMMUNITY SAFETY IMPLICATIONS

12.1 Any applications coming forward for consideration within the Property Development Framework will need to be assessed against the Council's Unitary Development Plan, the emerging Core Strategy Local Development Framework and the National Planning Policy Framework.

13.0 RECOMMENDATIONS

13.1 That Members agree to establish a Property Development Framework based on the three delivery models set out in Section 2 of this report in order to support the delivery of the Council's Investment Strategy.

13.2 That Members authorise officers to identify sources of funding to support the implementation of the Property Development Framework – both external and internal resources.

13.3 That Members agree that £700,000 from the Working Neighbourhood's reserves be reclassified as Property Development Framework reserve to be used as a contingency budget for the use of the Head Lease delivery model.

13.4 That Members agree that any surplus made by the Council from the rental charged through the Head Lease arrangement would be reinvested into the contingency reserve.

13.5 That each and every project considered under the Property Development Framework is brought forward to Cabinet for approval and is accompanied by a detailed report reflecting a full project appraisal and setting out how the specific matter complies with all financial and legal requirements.

13.6 That an annual report on the performance of the Framework is presented to Members.

14.0 REASON FOR RECOMMENDATION

14.1 To establish a Property Development Framework for Wirral to deliver the objectives of the Investment Strategy.

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