



## ECONOMY REGENERATION AND HOUSING COMMITTEE

Tuesday 16<sup>th</sup> July 2024

<b>REPORT TITLE:</b>	<b>THE HYTHE: PUT/CALL OPTION</b>
<b>REPORT OF:</b>	<b>DIRECTOR OF REGENERATION AND PLACE</b>

### REPORT SUMMARY

This report provides an update on the Hythe Put/Call option that the Council entered into with Peel Land and Property (intermediate) in September 2020 (which was subsequently novated to Peel L&P (Ports No3) Limited) and sets out a series of options that are available to the Council in the event that Peel exercise it's put option which will commit the council to purchase a 250 year leasehold interest in The Hythe from Peel.

Cabinet on 30<sup>th</sup> September 2019 approved the Council entering into a put/call option with Peel to enable them to nullify the risk of them constructing The Hythe, a speculative 3,116sq.m Grade 'A' office on Tower Road.

The project which achieved practical completion in December 2021 has been successful from a regeneration perspective as it has resulted in:

- The construction of a Building Research Establishment Environmental Assessment Method (BREEAM) excellent rated Grade 'A' office building in the Four Bridges neighbourhood of Wirral Waters;
- An office space which has the potential enable up to 280 gross direct and indirect jobs;
- 1 acre of brownfield land developed;
- 150 college students being assisted in their skills development; and
- Support for the development of the Mersey Waters Enterprise Zone by attracting occupiers to Wirral Waters.

This matter affects the ward of Bidston St James and is a key decision given that the value is more than £500,000.

### RECOMMENDATIONS

Economy Regeneration and Housing Committee is recommended to note the potential increase to the capital programme of £4.985m (plus, if applicable, associated purchaser's costs including Stamp Duty Land Tax and legal and surveying fees estimated to be £270,000) for the potential purchase of the Hythe.

## **SUPPORTING INFORMATION**

### **1.0 REASONS FOR RECOMMENDATIONS**

- 1.1 The Council entered into a Put/Call option with Peel L&P Investments (Intermediate) Limited on 17<sup>th</sup> September 2020 which, based on the future value of the building, committed the Council to purchase a 250-year lease in the property in the event that the Put /Call option value of £4.985m was not achieved. This was subsequently novated to Peel L & P (Ports No3) Ltd.

### **2.0 OTHER OPTIONS CONSIDERED**

- 2.1 No other options can be considered as the Put /Call option obliges the Council to purchase a long leasehold interest in the Hythe if it does not reach its pre-determined value of £4.985m. The Put/Call option will be determined by the final valuation of the office building which is scheduled for December 2024.

### **3.0 BACKGROUND INFORMATION**

- 3.1 Peel approached the Council in 2018 to enquire as to whether the Council would be prepared to share the commercial risk of them constructing the building which subsequently become known as the Hythe, a Grade 'A' office development on Tower Road South that, given its speculative nature, would have been commercially unviable even with a £3m gap funded grant that they had secured from the Liverpool City Region Combined Authority (LCRCA) .
- 3.2 The Council, recognising the need to kick start the regeneration of Wirral Waters and grow its non-domestic rates revenue stream agreed to explore a variety of options that could be made available to Peel to help them de-risk the construction of a speculative office building in a location where traditionally commercial developments were unviable as end values were less than the actual costs of development.
- 3.3 The business case that was produced to support the 2019 Cabinet paper outlined the options that were available to the Council at the time which included, as well as the Put /Call option, the do-nothing option or that the Council took out a 25-year head lease on the completed office to enhance its commercial value based on the covenant strength of the Council.
- 3.4 Cabinet subsequently agreed that the Put/Call arrangement was the most commercially viable option to pursue, and the subsequent option agreement was duly entered into on 17<sup>th</sup> September 2020, being subsequently novated to Peel L & P (Ports No3) Ltd (Peel No 3).
- 3.5 The Put/Call option works by both Peel No 3 and the Council entering into an agreement that allows for Peel No 3 to require the Council to purchase via a 250 year lease the development from them, in this case from three years from the date of the practical completion of the office scheme at a pre-determined price (the put option), or for the Council to require Peel No 3 to sell them the property within the same timescale at the pre-determined price (Te call option). The completed value of the building (£4.985m) was determined by an independent surveyor as part of the

cost appraisal that was carried out by the LCRCA when determining the 'gap' funded grant that they made available to be used by Peel No 3 to help to support the project.

- 3.6 The Put/Call option has a definitive end date of 3 years from practical completion (PC) of the office building, which is 6<sup>th</sup> December 2024 and the agreement called for the Hythe to be valued on the anniversary of PC and for that valuation to be shared with the Council. If, at any time during this 3-year period The Hythe was valued at a sum equal or greater than the Put option (£4.985m) then the Council's obligation to have to purchase the leasehold of the building from Peel would fall away. Notwithstanding this scenario and depending on valuation Peel can only trigger the put option at 3 years from the practical completion of the building that is 6<sup>th</sup> December 2024. As part of the same option agreement the Council had negotiated a right to exercise its call option any time during the 3-year period meaning that if market conditions strengthened over the period and the value of the asset increased above the option price then the Council had the right to purchase the Hythe from Peel at the pre-determined figure of £4.985m.
- 3.7 Since the Hythe was completed in December 2021 two valuations have been undertaken in December 2022 and December 2023. Despite the project being successful from a regeneration point of view, with two of the three floors fully let creating 120 new jobs, the yields in the office market generally have deteriorated over the last two years due to general economic pressures, the war in Ukraine and rising interest rates. This has resulted in the building being valued in December 2022 at £3.9m and the most recent valuation in December 2023 at £3.45m.
- 3.8 Clearly these valuations are lower than was expected at the time of the put/call option being entered into and with the final valuation of the Hythe scheduled for December 2024 there is a strong possibility that it will still be valued at a figure below the trigger value of £4.985m.
- 3.9 It should be noted that at the time of writing this report Peel No 3 has not taken a formal position as to whether it intends to trigger the Put option which will commit the Council to purchase a long leasehold in the building, but it is a possibility given the current state of the market. For reference when the scheme was originally appraised in 2020/21 to establish its value a yield of 7.75% was used as the benchmark which was considered prudent at the time. Unfortunately, the economic down-turn experienced over the last two years and in particular the global rise in inflation has pushed yields out to 9 - 9.5% which has resulted in the lower valuations reported in paragraph 3.6 of the report.
- 3.10 If Peel No 3 does trigger its Put option there is a potential that the 250-year leasehold of The Hythe will need to be purchased in the current financial year and the options open to the Council in this scenario are set out in the finance section of the report below. A full approval process will proceed in accordance with the Council's constitution within an appropriate timescale to enable the funding to be in place to enable any such purchase.

#### **4.0 FINANCIAL IMPLICATIONS**

- 4.1 If the Put option is triggered the Council would be required to purchase the property at £4.985m. As this was entered into to support regeneration of the area, this would

be classed as borrowing for regeneration purposes. It would be funded from Council Borrowing at 5% over 50 years of £0.250m per annum. Together with the statutory charge for Minimum Revenue Provision of £0.100m per annum, this would mean a total charge to revenue of £0.350m per annum that would need to be funded. The Council would then have two potential options:

- to continue to operate the property (whether internally or through an alternative delivery method), or
- to dispose of the property (as a going concern to another party).

4.2 The running costs of the property are currently unknown. If loss making this would increase revenue pressure on the Council further. Further information is being sought in this regard. However, the best understanding that the Council has is that the rent into the Council, unless the ground floor is let, will be less than the money that it will have to pay for interest payments for any loan. Other costs such as rates and landlord costs of managing and maintaining the asset would also have to be considered.

4.3 If the Council decided to sell the long leasehold, then the disposal would be classed as a capital receipt, but the revenue cost of the initial borrowing would remain and still need to be financed (either in full or in part, as the capital receipt does not have to be used for repayment of the loan).

## **5.0 LEGAL IMPLICATIONS**

5.1 The arrangements that are set out in this report were at the time that they were entered into in satisfaction of what was at the time described as the Market Economy Principle (MEOP) Test pursuant to the rules of State Aid that applied at the time. In broad terms an economic transaction carried out by a public sector body did not constitute State Aid if it was in line with normal conditions and a market operator, of similar standing, could have been prompted to enter into the transaction on the same terms. The Council, to ensure compliance, commissioned independent property experts Cushman and Wakefield to assess the project and they confirmed that the appraised put/call option was MEOP State Aid compliant. This conclusion has been further endorsed by legal advice that was procured at the time.

## **6.0 RESOURCE IMPLICATIONS: STAFFING, ICT AND ASSETS**

6.1 If the property has to be purchased it will be managed using existing staff resources supplemented by external specialist support. There will be additional resources and cost to the management of the asset, both in terms of the asset and facilities management of the asset. Any voids would have revenue implications and it is currently understood that the ground floor is not currently let.

## **7.0 RELEVANT RISKS**

7.1 The risk of purchasing the long leasehold of The Hythe is that the building is not yet fully let. It currently has tenants occupying floors one and two, but the ground floor remains vacant and this would have a long term revenue implication for the Council.

7.2 To minimise this risk the Council would, via its Asset Management team, commission its property agent to create a lettings strategy and working with the Council's communication team undertake a marketing exercise to raise the buildings profile to identify occupiers for the ground floor. This work will be regularly evaluated and reviewed to try to ensure that the Hythe reaches full occupancy as soon as is practicable.

## **8.0 ENGAGEMENT/CONSULTATION**

8.1 Planning consent was granted for the Hythe in 2019. The application for its development was widely consulted upon and Peel, at the time held a number of community engagement and consultation events to publicise its plans for the Tower Road area of Wirral Waters.

## **9.0 EQUALITY IMPLICATIONS**

9.1 The Council has a legal requirement to make sure its policies, and the way it carries out its work, do not discriminate against anyone. An Equality Impact Assessment (EIA) is a tool to help council services identify steps they can take to ensure equality for anyone who might be affected by a particular policy, decision or activity.

9.2 Whilst there are no implications arising directly from this report, the associated actions arising from the delivery may need to assess any equality issues and mitigate any negative impact that may emerge. Any associated EIA will be done at the earliest possible stage.

## **10.0 ENVIRONMENT AND CLIMATE IMPLICATIONS**

10.1 The Hythe has been constructed to a BREEAM excellent standard which is the world's leading sustainability assessment for measuring commercial buildings.

10.2 The development resulted in the re-use of 1 acre of previously used land which supports the Council's Local Plan brownfield first aspirations.

## **11.0 COMMUNITY WEALTH IMPLICATIONS**

11.1 Community Wealth Building reorganises local economies to be fairer and stops wealth flowing out of communities. Striving for a prosperous and inclusive economy where local people can get good jobs and achieve their aspirations, the Council aims to create an economy that benefits all of our residents and one which keeps money within Wirral. The Council's Community Wealth Building Strategy is a key part of how this is achieved and makes a major contribution to improving the economic, social and health outcomes of the borough.

11.2 The job opportunities that have been created by The Hythe will help to revitalise the local economy and ensure that more wealth is invested and stays within our Borough.

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## **APPENDICES**

None

## **BACKGROUND PAPERS**

The Hythe PUT/CALL Business Case 2019

## **TERMS OF REFERENCE**

This matter is being considered by Economy Regeneration and Housing Committee in accordance with section (g) “overseeing the progress of major projects (including major building, infrastructure or other projects involving the erection or significant alteration of major permanent structures or landmarks) undertaken by the Council directly or as enabler, funder or joint enterprise partner, including but not limited to the Wirral Growth Company LLP.”

## **SUBJECT HISTORY (last 3 years)**

<b>Council Meeting</b>	<b>Date</b>
Cabinet	30/09/2019