WIRRAL

ECONOMY REGENERATION & HOUSING COMMITTEE

Tuesday, 16 July 2024

REPORT TITLE:	**MARITIME KNOWLEDGE HUB**
REPORT OF:	**DIRECTOR OF REGENERATION AND PLACE**

REPORT SUMMARY

The derelict Grade II listed Hydraulic Tower on Tower Road, Birkenhead is the subject of a proposal from the landowner (Peel) to deliver a Maritime Knowledge Hub (MKH) which seeks to create a BREEAM Excellent, industry-led, world class centre of excellence for maritime business growth, innovation and sector development. The investment sought will seek to repurpose an existing water-side asset which sits at the heart of the Left Bank regeneration area to create a destination for maritime collaboration, with water access for R&D, testing and training and views across to Liverpool's iconic skyline. The economic impact assessment contained in the Outline Business Case (OBC) appended to this report identifies that the scheme could deliver net economic benefits of £18.18m, creating 48,750 sq ft of business, teaching and workspace and 275 jobs.

This Committee considered the subject matter on 27 March 2024 when it agreed to authorise the Director of Regeneration and Place to further develop the proposals for the development of a Maritime Knowledge Hub on the site of the hydraulic tower with a view to bringing back a more detailed report to a future meeting of this Committee. Members also requested more information on a number of matters including a heritage solution, changing the arrangements around the rent headroom, asset acquisition, loan finance and the creation of an SPV (Special Purchase Vehicle).

This report sets out the outcome of this work for members consideration. Specifically, the committee is being asked to consider the transaction set out in the report and choose whether or not to agree to the heads of terms.

The ability to proceed with this development is reliant on getting to a position of an agreed Heads of Terms with the Council, an agreed funding model with the LCRCA which will then be subject to passing the public sector subsidy assessment. In addition, due to a change in circumstances, the developer, Peel, will need to revisit the issues relating to planning consent. Following Committee's decision there will be a requirement for the LCRCA to consider the matter and consider whether or not it wishes to invest in the scheme. The report proposal directly supports the Council Plan (2023-27) through the key theme of working together to deliver people focused regeneration.

This decision affects Seacombe Ward, but the subject asset is close to Bidston and St James and Birkenhead and Tranmere Wards.

This is a key decision.

Appendices 2, 3 and 4 of this report are exempt from publication pursuant to paragraph 3 of the part 1 of Schedule 12 A of the Local Government Act 1972 (Information relating to the financial or business affairs of any particular person (including the authority holding that information)) because it contains or refers to information relating to the financial and business affairs of Peel and the Council and the public interest in maintaining the exemption outweighs the public interest in disclosure.

RECOMMENDATION/S

The Economy, Regeneration and Housing Committee is requested to:

(1) note the work completed since the previous update to Committee on this matter.

(2) note the regeneration benefits that the delivery of a Maritime Knowledge Hub on this site would deliver along with the risks to the Council should the committee choose to progress with the proposal.

(3) note the risks to the Council should committee choose to progress the proposal.

(4) direct the Director of Regeneration and Place to bring discussions on this matter to a close with Peel LLP and not proceed to agree the Heads of Terms.

SUPPORTING INFORMATION

1.0 REASON/S FOR RECOMMENDATION/S

1.1 The Council is working with Peel and partners to explore delivery of a Maritime Knowledge Hub.

1.2 Based on the information provided and due to the structure of the proposal, the Council would be exposed to the risk of operating the asset and servicing the proposed lease over a period of 50 years.

1.3 The risk placed on the Council's finances is not justified in comparison to the benefits outlined in the report.

1.4 It is not at all likely an alternative transaction structure, or proposal, would be developed that would mitigate the Council's risk that would be within the time horizon needed to access funding that is available to the LCRCA.

1.5 Should the Committee agree the proposal the expectation would be a contractual agreement would follow and at that stage the Council would be contractually bound to the scheme, subject to the terms. The Council cannot be legally bound to the Heads of Terms before consideration by the LCRCA or before the transaction has been considered by the Government's Subsidy Advice Unit and their advice received and taken into account by the Council before a final decision is made. This would delay any final decision and may impact the LCRCA's ability to deliver freeport seed funding to the region.

2.0 OTHER OPTIONS CONSIDERED

2.1 A range of options have been considered in preparing this report and these are set out in more detail in Appendix 1. These include a do nothing option, a third party investing in the property, the council acquiring the property, a different transaction, a different solution on the same site, delivery of a Maritime Knowledge Hub on a different site.

2.2 In summary the Council and partners have looked carefully at a range of other options over a prolonged period of time to bring forward a scheme on this site, however these have not been successful. Therefore, the only realistic options in front of the Committee are a 'do nothing' option or to progress with a scheme. Following a 'do nothing' option alternative solutions may be found in due course.

3.0 BACKGROUND INFORMATION

3.1 The project is proposed to deliver 48,750 sq ft (gross) collaboration hub, comprising of a technology lab, training centre and dedicated workspace and will be built to a BREEAM Excellent standard.

3.2 Since the last report to committee, the amount of grant funding that is possible to be accessed has varied and as a result the scheme has been reduced in size by c10%. This will mean that the planning consent for the scheme will need to be revisited. Grant funding is proposed to be £8m Freeport Seed Fund and £1.7m of Wirral

Waters Investment Fund, subject to LCRCA approval. The balance of the capital needed will be obtained by accessing private finance. The proposal will see £21.1m of funding being put into the scheme. The private funding would be secured by the Council taking a 50 year head lease of the finished building with the Council paying a rent to the funder but gathering a rent from the occupiers of the building. This is known as a lease wrap transaction. This in effect creates an annuity for the funder and it is not uncommon for the initial funder to sell this as a commodity, given that the level of return is guaranteed into the future as the Council is be compelled to pay its rent, regardless of the level of rent it collects from the occupiers, and is a good covenant.

3.3 Peel would assign a long lease to the Funder and receive a sum of money based on the value of the headlease to the Funder. This is estimated to be £11.4m. The net realisation value is £21.1m of which £9.7m would be found from the Council and the Combined Authority with the balance being Peel's responsibility. Any surplus for Peel should be added to the subsidy for the purposes of the Subsidy Control Act 2022 and should be deducted from the grants in order to comply with the legislation. Grants cannot exceed the amount of the viability gap being the estimated costs of construction less the value of the asset to Peel when completed. Although this is the best transaction that is acceptable to Peel and the LCRCA, subject to their approval, at this time, there are still very significant risks to the Council should the Committee choose to agree to the proposal. It is clear that the reasons for considering the investment are one of regeneration, and this would not therefore equate to a transaction at best consideration for the Council.

3.4 The accommodation is proposed to be a mix of office suites, suitable for a range of uses including education, flexible space, and a Café. Peel have worked to identify several organisations that are interested in taking space within the proposed building. These are from the maritime sector. Should the matter go forward then these would be converted to pre-lets which would, once a threshold of 80% occupation at certain specific terms was reached, would then trigger the scheme build. This threshold is common for a pre let scheme.

3.5 Following the committee meeting in March, Peel have further developed their proposals for the site and have presented an Outline Business Case (OBC) to the Council. This is contained in Appendix 2 to this report. Appendix 2 is exempt from publication pursuant to paragraph 3 of the part 1 of Schedule 12 A of the Local Government Act 1972 because it contains or refers to information relating to the financial and business affairs of Peel and the Council. The public interest in maintaining the exemption outweighs the public interest in disclosure.

3.6 Peel will not be able to progress the proposals further without the guarantee that the Council will, if the parameters of the heads of terms are met, commit to the scheme. The reason for this is that to progress beyond this point they would have to significantly invest in the scheme and start to incur significant costs. Therefore, should the Committee agree to the proposal then it would commit the Council to the scheme to permit its progress, but then also expose the Council to all the risks that are set out in the report. It would however also release the regeneration opportunity.

3.7 As set out in the March report, there are several very significant risks that the Council would be exposed to if the Committee chose to accept the heads of terms and the transaction continued to a contractual commitment.

3.8 The mechanism of how rent increases would be calculated is different for the rent the Council would pay the investor and the rent paid to the Council by occupiers. Rent to the investor would be protected by a capped and collared upward only rent, which would be linked to RPI (Retail Prices Index) and therefore guaranteed to grow, whereas the rent reviews of occupiers of the assets would reflect market rent at the time of negotiation. It is not at all possible to be definitive about the amount of deficit that the Council would face in this scenario as the period of the lease is long (50 years) and the Council would not be able to calculate future growth of RPI or market rent.

3.9 The normal mitigation for this would be to set a significant gap between the rent in and rent out to provide sufficient buffer over the term of the lease. It is not the case in this proposal. This level of rent is at the very top end of the market in the area and the differential between this and rent out to an investor is not sufficient to give the Council comfort that this will be sufficient to cover this risk for the lease period. The Council will be bound by the agreement for a period of 50 Years. Fluctuations in the economy would also generate risks for the Council. The Council would also be exposed to other risks, such as changes in working practices, this industry and other societal and environmental factors such as climate change. Any estimated losses to the Council over the 50 year period would have to be added to the value of the subsidy for the purposes of the Subsidy Control Act 2022.

3.10 The Council has been provided with good information about how the project would be funded, the Council’s role in this. Setting aside the issue of finance and the risks therein, it is reasonable to anticipate that the physical scheme is practically achievable, and Peel have a track record of delivery of BREEAM Excellent schemes in the area. There is risk that the scheme once in detail design has been worked up, increases in cost. There is limited information about how the property would operate. The intent is to deliver a Maritime Knowledge Hub and not just deliver another office building. There is limited understanding in the OBC, about how the Maritime aspect of the building would be developed beyond that of similar businesses being in the same building and having access to the docks system.

3.11 The property would also see a mix of occupation styles, including flexible space and a Café. There is no modelling to demonstrate if these types of uses would be profitable or would receive sufficient take up to be commercially viable. Other accommodation within the building may be set out for specific uses, which if brought to an end may mean in the future that the building would need to be reconfigured, which would have cost and rent implications.

3.12 The rent out to the investor would grow within set parameters. It is extremely likely that rent from occupiers would grow at a slower pace than this. In large part this will be due to the very different nature of the rents.

3.13 There is a value to the lease because the Council, with its strong covenant, will pay rent at set parameters over a period of 50 years. For the purposes of the Subsidy Control Act 2022 the economic advantage to Peel of obtaining from the Funder funds in excess of the market value of the completed MKH would be added to the value of the public subsidy already comprised in the grants.

3.14 The Council has previously invested in the Hythe Building and Millars Quay to support the regeneration of the area. It is noted that the Council has by the nature of these investments accepted a range of risks that will take time to crystalise or not. At the end of the 50 year period the Council would have the option to purchase the Maritime Knowledge Hub or not for a limited period.

3.15 The Council has experience of delivery of a specialist building, a Maritime Knowledge Hub in Tranmere, focused on the Maritime industry already. This was developed in 2000 and is currently not used by marine industry. Although the settings and buildings are different it does give a clear indication of the type of issues and risks the Council could face in the future, noting that the lease terms are for a period of 50 years and that the grant funding would likely focus the use of the asset to a specific business sector.

4.0 FINANCIAL IMPLICATIONS

4.1 The Section 151 officer has reviewed the proposed scheme and the associated financial consequences. Although it is anticipated that the scheme could generate economic growth the overall costs of the scheme to the Council mean that it does not represent value for money. The current, challenging, financial position of the Council must also be considered in respect of both the revenue budget and the availability of reserves to smooth any unexpected costs. Given these considerations and the overall financial viability of the scheme it is not currently possible to recommend proceeding with the proposed scheme.

4.2 Consultant costs have been incurred in assessing the viability of the scheme and the-long term financial implications for the Council due to the complex nature of the proposed arrangements.

4.3 The proposals would result in the Council taking on the liability for a headlease on the site for a period of 50 years. This would require the Council to pay rent at an initially agreed level that would increase annually by RPI with a cap/collar mechanism limiting the changes. The Council would be responsible for void costs (rent and service charge), unrecoverable service charge costs and refurbishment as required in the future. The Council would need to accept the risk around lettings and voids which could have a significant financial impact over the proposed term depending on both the macroeconomic conditions and the overall success of regeneration within the area.

4.4 The proposed terms of this lease expose the Council to a significant degree of risk. Although there are provisions within the agreement with Peel in relation to the initial occupation of the building.

4.5 The Council would benefit from any business rates generated by the site, however in considering the merits of the scheme and its financial implications the Council is not able to consider business rates as part of the transaction for the purpose of the Subsidy Control legislation. There is also no future certainty around the business rates retention pilot which supports Wirral Waters Investment Fund (WWIF) funding or indeed the overall future of business rates.

4.5 All reasonable financial projections in relation to the scheme demonstrate there would be a net cost to the Council over a significant period of time. It is unlikely that a position would be realised which would not lead to an ongoing subsidy being required. Although this assumption needs to be balanced against the wider economic and regeneration benefits of the scheme it must also be cognisant of the current financial position of the Council and its limited capacity to absorb any additional costs in the short term. The future financial implications must also be considered alongside the other commitments that have already been made, such as Wirral Waters, and the risks the Council is already subject to.

4.6 This report identifies the risks around income streams not being sufficient to cover the buildings costs. This has the potential for significant financial risk if this is deemed an onerous contract. This is where unavoidable costs outweigh the economic benefits and would result in an immediate charge to revenue for the full period to set up a provision to cover the expected costs of those future financial liabilities. This would be fully explored as part of the recommended future report on the details of the proposal. It is, however, likely that the MKH would be deemed an onerous contract because over 50 years the rental income received is unlikely to cover the outgoings. Members are referred to information in Appendix 3.

5.0 LEGAL IMPLICATIONS

5.1 There is a legal requirement in the Subsidy Control Act 2022 (“the Act”) for the Council to refer all proposed subsidies that exceed in total £10m to the Subsidy Advice Unit (SAU) of the Competition and Markets Authority for an advisory report on whether the grants would comply with the 7 Principles of the Act. The difference between the cost to deliver the scheme and the likely market value of the building on completion could be more than £10m and therefore, the subsidy (i.e., economic advantage to Peel) would exceed £10m. That report would have to be considered by the Council before it decided whether or not to agree to its share of the total subsidy which would enable Peel to construct the buildings so as to lease them to the Council for the purpose of use by advanced maritime technology firms.

5.2 The SAU would require the Council to draw up its own written Assessment of Compliance with the 7 Principles of the Act which are summarised in appendix 6:

5.3 The Assessment of Compliance document for the SAU would have to be accompanied by a business case, a value for money assessment and an independent valuation of the viability gap. A reliance on Peel’s own surveyors would not be regarded as due diligence by the SAU. Additional costs would be generated by undertaking this further work.

5.4 Prior to entering into an agreement the Council would have to consider whether it was a transaction at best value / consideration given the risk that rent payable to the funder would exceed the market rent. The Council would need to understand what the proposals for the operation of the asset were and what procurement route would be required to identify an operator to manage the asset together with the likely costs.

6.0 RESOURCE IMPLICATIONS: STAFFING, ICT AND ASSETS

6.1 The Council would benefit from the lease of the building for a period of 50 years. Currently, the Council does not have a team available that would operate the Maritime Knowledge Hub in terms of overseeing tenant's arrangements etc. Therefore, additional resource would be required to operate it. It would be likely that the Council would seek a third-party operator with the appropriate skills to operate a Maritime Knowledge Hub. The detail of the operation of the hub and costs is not clear in the OBC.

6.2 The Council would be accepting the whole risk of owning and operating the Maritime Knowledge Hub and the inherent risk of a lease wrap transaction, this is magnified by the closeness of rent in and out, risk around voids, operating costs, and rent frees in the future to facilitate lettings. The implications of which are set out in the report. The LCRCA to protect its investment is likely to restrict the use of the asset. Future refurbishment of the building would be a Council cost, either by investment of Capital or provision of future rent free periods.

7.0 RELEVANT RISKS

7.1 In March the committee was advised of the risks known at that time when the matter was previously considered. Peel have now provided more information about the scheme and as a result information about the risks of the project has been updated. Due to the commercial nature of the project these risks are contained within Appendix 3. Appendix 3 is exempt from publication pursuant to paragraph 3 of the part 1 of Schedule 12 A of the Local Government Act 1972 because it contains or refers to information relating to the financial and business affairs of Peel and the Council. The public interest in maintaining the exemption outweighs the public interest in disclosure.

7.2 The Committee when considering this proposal need to balance these risks against the potential regeneration benefits of the proposal. It will also need to take a careful view about the Council's finances and whether the opportunity of delivering this scheme outweighs the risk to the Council's finances, particularly in the short term. The Director of Finance would need to be satisfied that investment in the MKH on the terms proposed would meet the tests for prudential borrowing.

7.3 To do nothing would mean that the Grade II listed Hydraulic Tower would not be brought back into an economic use. Although the Council has an interest in listed buildings, due to its statutory duties, it does not have a direct responsibility at present towards this building as an owner of land. The regeneration benefits associated with the scheme would not be crystalised at this time. On the other hand, the money borrowed to meet the cost of the grant could be redeployed for other purposes e.g.to facilitate the performance of its statutory duties and the Council would avoid the risk of MKH running at a loss for some or all of the 50 year arrangement.

7.4 The Council will be exposed to all the usual risks of operating the asset from when it takes the lease. Although Peel has done a good piece of work to articulate how the asset would operate, it remains unclear as to the detail of how the Council as the owner of the asset would deliver a Maritime Knowledge Hub and what services and additional activity beyond occupation of the building by complementary occupiers would take place. It would be likely that the Council would have to commission or otherwise enable this additional activity as it does not have the expertise to deliver this.

7.5 The Council has been asked to agree to the Heads of Terms prior to the matter been considered by the LCRCA. This is based on an outline and not a detailed business case. Should the Committee agree the Heads of Terms the expectation would be a contractual agreement and at that stage the Council would be contractually bound to the scheme, subject to the terms. The Council cannot be legally bound to the Heads of Terms before consideration by the LCRCA or before the transaction has been considered by the Subsidy Advice Unit and their advice received and taken into account by the Council before a final decision is made.

7.6 The detail of what a Maritime Knowledge Hub's offer is has yet to be determined in detail and it is likely that this would evolve as discussions with tenants evolved and they enter into agreements to lease. There is a risk that the building would simply be leased to a particular category of tenant, which would miss the opportunity that this proposal represents.

7.7 The LCRCA understand the proposal and are encouraged that as a concept it is good. However, to protect their investment, specifically in this sector they will look to restrict the use of the asset. Given the lease to the council is for a period of 50 years this presents a risk to the Council, which would only be able to let the building to a certain category of business or those associated with that category. It is also likely that the LCRCA will also seek further controls.

7.8 The space that will be provided will be of a high quality. Accordingly, the terms offered for the space will be reflective of this quality and its high construction cost and therefore will not be set at an average for the market in the area. Although the Council does not wish to aim for mediocrity, a higher level of rent, justified by a better-quality product may present a challenge in terms of letting. It is noted that the restrictions likely to be placed on the asset will further restrict the market for this building.

7.9 The proposed development would be funded in part by grant funding and in part by a third party investor providing funding. This latter part will be assured by the Council taking a lease and then paying the investor over the period of the lease. The Council would benefit from the rent it receives from tenants in the building. The profile of rental growth of these rents is different and there is a real risk in the future that the Council will have to pay more rent than it receives. Once the agreements are in place the conditions for this will be set and the Council will not be able to exit the agreement, should it find that in the future the position is not favourable. Issues such as any costs that the Council would have to pay, and not pass onto occupiers, would also directly impact this arrangement. Periodically the Council would be responsible for refurbishing the asset, either capital investment or through rent free periods to tenants. This would directly and significantly impact the position as well.

8.0 ENGAGEMENT/CONSULTATION

8.1 The Council has engaged extensively with the LCRCA and Peel as part of this proposal. Peel have engaged with a range of businesses associated with the

Maritime Industry as part of their work to bring the proposal forward. The Council has not had sight of the detail of these discussions but understand that they are favourable but further engagement is dependent on the Council agreeing the Heads of Terms.

9.0 EQUALITY IMPLICATIONS

9.1 Wirral Council has a legal requirement to make sure its policies, and the way it conducts its work, do not discriminate against anyone. An Equality Impact Assessment 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. It is unlikely that MKH Project would affect adversely persons with protected characteristics.

10.0 ENVIRONMENT AND CLIMATE IMPLICATIONS

10.1 The Council as part of this intervention would bring a derelict building and site back into economic use, generating environmental benefits. This will reuse the carbon tied up in the fabric of the existing building.

10.2 The proposal would see the delivery of a BREEAM Excellent building. It would be reasonable to expect that the building would be able, with modification to access any future heat network, although there would be a cost associated with this.

10.3 The building would be used to deliver innovation in the Marine industry and as a result it is likely that it would be used to explore issues such as decarbonisation, giving it potential beyond its own footprint.

10.4 Environmental issues about design, sustainability, and site use have already been considered at planning, however it is understood that planning would need to be considered again due to the overall variation in the size of the building.

11.0 COMMUNITY WEALTH IMPLICATIONS

11.1 The OBC sets out a range of positives relating to regeneration and community wealth. Principally the asset will generate the opportunity to create bespoke accommodation for a specific business sector, which is cited to be of national significance. It will provide opportunities for employment and education, and it would be logical to assume act to attract similar businesses to the area.

11.2 The reuse of the iconic Hydraulic Tower, emblematic of the rise and fall of Birkenhead of the past, could act as a totem for the future and the rise of Birkenhead again. It will also help the regeneration journey of the area, generating employment during construction and building the place for the future. However, this also needs to be set against the very significant risks that the Council would take, which could impact the Council’s overall financial position, which in turn could impact its ability to deliver services which benefit the community.

REPORT AUTHOR: **Andy Kehoe MRICS**
(Head of Asset Management)

email: andrewkehoe@wirral.gov.uk

APPENDICES

Appendix 1 - Alternative Options
Appendix 2 - Outline Business Case (Confidential)
Appendix 3 - Relevant Risks (Confidential)
Appendix 4 - Heads of Terms (Draft) (Confidential)
Appendix 5 - Property Advice (Confidential)
Appendix 6 - Seven Principles of Subsidy Control Act 2022

BACKGROUND PAPERS

Subsidy Control Act 2022

TERMS OF REFERENCE

This report is being considered by the Economy, Regeneration and Housing Committee in accordance with section (f) of its Terms of Reference, “the promotion and development of the economic factors in the area, such as seeking to ensure sufficient and appropriate employment sites, investment, adult skills, apprenticeship schemes, productivity, development sites and so forth”.

SUBJECT HISTORY (last 3 years)

Council Meeting	**Date**
ER&H Committee 27 March 2024	**27 March 2024**