Summary Sheet

Council Report
Cabinet and Commissioners’ Decision Making Meeting – 11 September 2017

Title
Unlocking Property Investment – Beighton Link

Is this a Key Decision and has it been included on the Forward Plan?
Yes

Strategic Director Approving Submission of the Report
Damien Wilson, Strategic Director, Regeneration & Environment Services

Report Author(s)
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Ward(s) Affected
Rother Vale

Executive Summary

The Council has analysed and compared a number of commercial property development opportunities in Rotherham for the potential to stimulate business growth and generate an investment return. This has identified a preferred deliverable option on a site owned by JF Finnegan at Beighton Link and the potential to improve the attractiveness of the project through regional investment funding.

This report recommends that the Council acquires the land and enters into a development agreement for JF Finnegan to construct business units, which on completion of construction the Council will own. The project will secure economic growth benefits and an investment return which will help support the Council’s revenue budget.

Recommendations

1. That the Strategic Director of Regeneration and Environment be authorised to agree terms to acquire land at Old Colliery Way, Beighton Link, Rotherham and enter into a development agreement with JF Finnegan Ltd.
2. That, subject to an assessment of the financial viability of the proposed final terms of the agreement with JF Finnegan and formal approval of the JESSICA funding bid, the funding for the purchase be taken from the £5m Growth Fund, which was approved as part of the Capital Strategy 2017-2022.

3. That the Assistant Director of Legal Services be authorised to complete the necessary legal agreements.

4. That, in order to allow the development to proceed, an exemption to standing orders under paragraph 43.2.4 be agreed.

List of Appendices Included

Appendix 1 Business Case (Exempt)
Appendix 2 Development Appraisal (Exempt)
Appendix 3 Industrial Market Overview and Funding Options (Exempt)
Appendix 4 Location Plan
Appendix 5 Financial Overview (Exempt)

Background Papers
Rotherham Economic Growth Plan 2015 -25

Consideration by any other Council Committee, Scrutiny or Advisory Panel
None

Council Approval Required
No

Exempt from the Press and Public

An exemption is sought for Appendix 1, 2 and 3; under paragraph 3 (Information relating to the financial or business affairs of any particular person (including the authority holding that information)) of Part I of Schedule 12A of the Local Government Act 1972 is requested, as this report contains sensitive commercial information with regards to costing for works and commercial agreements which could disadvantage the Council in any negotiations if the information were to be made public.

It is considered that the public interest in maintaining the exemption would outweigh the public interest in disclosing the information, as the parties’ commercial interests could be prejudiced by disclosure of commercial information.
Unlocking Property Investment – Beighton Link

1. **Recommendations**

1.1 That the Strategic Director of Regeneration and Environment be authorised to agree terms to acquire land at Old Colliery Way, Beighton Link, Rotherham and enter into a development agreement with JF Finnegan Ltd.

1.2 That, subject to an assessment of the financial viability of the proposed final terms of the agreement with JF Finnegan and formal approval of the JESSICA funding bid, the funding for the purchase be taken from the £5m Growth Fund, which was approved as part of the Capital Strategy 2017-2022.

1.3 That the Assistant Director of Legal Services be authorised to complete the necessary legal agreements.

1.4 That, in order to allow the development to proceed, an exemption to standing orders under paragraph 43.2.4 be agreed.

2. **Background**

2.1 There are a number of development schemes in Rotherham proposing the construction of new business space that are “stalled”. These schemes are being actively promoted but in the current market will not progress to construction until an end user is identified and a “pre-let” is agreed. The exception to this is at the Advanced Manufacturing Park (AMP) where the Council’s intervention in 2015/16 to bring forward the development of new business units was successful in proving the market and has encouraged Harworth Estates to fund a further phase of the R-evolution scheme.

2.2 The need to encourage new development is articulated in the Rotherham Economic Growth Plan which includes a target to increase the amount of industrial and commercial floor space in the Borough by 12.9%. A lack of suitable new space is a barrier to business growth, when companies are unable to find the premises they need to locate and grow in Rotherham and a challenge for the Council, which needs new development to create employment and build future revenue from the business rates base.

3. **Key Issues**

3.1 Property market failure within Sheffield City Region is restricting the supply of new commercial property development. This is a result of developer costs exceeding returns (rent/capital values). In some circumstances, a lack of debt finance is also restricting development, particularly for speculative projects. The majority of banks will only fund pre-let or pre-sold schemes.
3.2 The simplest form of addressing market failure is to provide grants and subsidies. However, this would be expensive for the Council to do and raises issues around state aid. Any intervention in commercial property development should be affordable, minimise risk and provide a realistic prospect of a return to the Council.

3.3 Sheffield City Region has recently developed proposals for a “flexible fund” to work alongside the JESSICA (Joint European Support for Sustainable Investment in City Areas) programme. This is intended to unlock development through innovative approaches to improving the viability of development schemes. Working in partnership with landowners and developers this offers an opportunity for the Council to bring forward new proposals that are more attractive and deliverable for the Council and which will:

   a) Simulate development and increase business rates revenue.
   b) Encourage the development of brownfield sites for employment uses.
   c) Create construction jobs and spend in the economy.
   d) Generate revenue to fund borrowing costs (principal and interest) to fund the investment.
   e) Create additional revenue for the Commercial Property Account.
   f) Provide attractive new property on the market to support business growth and job creation.
   g) Lever in additional funding to support delivery of the Economic Growth Plan.

3.4 Previous experience from the acquisition of the units at the Advanced Manufacturing Park indicate that in addition to economic development benefits there are good prospects of generating a revenue surplus from this type of investment. The property at the Advanced Manufacturing Park generates a net annual surplus of over £50,000 after taking account of all costs to the Council of owning the unit including capital financing charges.

3.5 The proposed delivery model is that the Council purchases land from JF Finnegan Ltd and simultaneously signs a development agreement for the construction of 2 business units on the site. The Council will receive income through an increase in business rates and the completed units will be let on the open market to end users – inward investors or expanding local companies which will provide additional income to the Council. The Council and JF Finnegan will share the letting risk through a “rent guarantee fund”, using part of the purchase price paid by the Council, the developers profit and grant funding from the Sheffield City Region (via JESSICA).

3.6 The construction of business units is a public works contract. The value of the contract will be below £4.1m and therefore EU Procurement Regulations do not apply and there is no requirement to advertise the contract in the Official Journal of The European Union (OJEU). However, UK domestic law and the Council’s Standing Orders require that all contracts with a value above £25,000 are publically advertised.
3.7 As current owner of the site JF Finnegan is in a position of having exclusive rights over Beighton Link. The land purchase cannot progress with an intention that a third party constructs the development as JF Finnegan will not sell its interest on this basis. To allow the development to proceed an exemption to Standing Orders under 43.2.4 is required “Where due to exclusive rights, including but not limited to intellectual property rights, no reasonable alternative or substitute exists”.

4. Options considered and recommended proposal

4.1 Do nothing -This is a low risk option but does nothing to address the growth priorities of the Council and the shortage of supply of new commercial development.

4.2 The Council acquires land and carries out direct development. The Council is not an experienced commercial property developer and does not have the in-house skills to progress this option. In addition, JF Finnegan has control over the development of the site and will not sell the site on this basis.

4.3 Alternative funding structures - A number of developers have requested that the Council considers taking head leases on institutional lease terms on their proposed schemes. An investor’s view of the security of future income is a significant determinant of investment value. In this way, developers would be able to onward sell schemes as investments with the benefit of the Council covenant and perceived security of income. This would increase the investment value and in most cases make development viable.

4.4 This approach commits the Council to making regular rental payments for circa 25 years (or more). If the scheme is fully occupied (i.e. a sub-tenant is in place) for the duration of the lease term then a potential profit from rental income, business rates income and economic benefits would all be forthcoming. However, if the unit is vacant at any time (i.e. there is no sub-tenant in occupation) a revenue pressure is created as no income is generated to offset the Council’s rental payments and holding costs.

4.5 Work in Partnership with the private sector and access regional regeneration funding. This is the preferred option.

4.6 The Sheffield City Region’s JESSICA “flexible fund” allows the Council to substantially reduce the risk of an investment in commercial property by sharing the letting risk with the landowner/developer. This is achieved through the creation of a “rent guarantee fund”, using the developers profit and the SCR flexible fund.

4.7 The rent guarantee fund is used to pay rent until a tenant takes occupation. It will ensure that the Council receives the full rent from the date the units are completed even if a tenant is not in place. The guarantee will have sufficient funding to cover a void of up to three years. This allows costs and income to be modelled with greater certainty.
4.8 **Alternative locations** - Property consultant BNP Paribas has analysed and compared different “stalled development” opportunities on behalf of the Council. This has included independent advice on values and market demand and has identified a preferred deliverable option at Beighton Link on a site owned by JF Finnegan. The advice is commercially sensitive and is included in Appendix 3 of the five exempt appendices to this report.

5. **Consultation**

5.1 The Cabinet Member for Jobs and the Economy and Commissioner Kenny have been briefed during the development of the project.

5.2 Consultation has taken place with the Sheffield City Region Executive team and the JESSICA Fund manager on the potential availability of regeneration funding.

5.3 The Council has also carried out consultation with developers and landowners details of which is available in the exempt appendix.

6. **Timetable and Accountability for Implementing this Decision**

6.1 The Strategic Director of Regeneration and Environment will be accountable for this project and will agree terms for the acquisition and development agreement in consultation with the Strategic Director of Finance and Customer Services.

6.2 The anticipated timescale is as follows

- Development Agreement – October 2017
- Construction Start – March 2018
- Construction Completion – September 2018

7. **Finance and Procurement Implications**

7.1 Under the terms of the proposed arrangement with JF Finnegan, the Council will purchase the land at Beighton Link and then procure JF Finnegan to build the 2 business units. The purchase price of the land will be independently determined to ensure that the Council’s best value obligations are met. Subject to an assessment of the financial viability of the proposed final terms of the agreement with JF Finnegan, it is proposed that the costs of this project, detailed in the exempt Appendix 2, are funded from the £5m Growth Fund, which was approved by Council on the 8th March 2017, as part of the Council’s Capital Strategy 2017-2022.

7.2 In addition, the proposed arrangement includes a 3 year rent guarantee fund outlined in the exempt Appendix 1, which is made up of a contribution from the Sheffield City Region Jessica Property Fund, a contribution from JF Finnegan, by way of a reduction in their developer’s profit received and a contribution from the Council. As this is a rent guarantee arrangement, the Council’s contribution would be a revenue expense, so would need to be taken into account in the viability assessment.
7.3 Details of the viability assessment undertaken by BNP Paribas Real Estate for the site are shown on page 23 of the exempt Appendix 3. As the proposed site is not within an Enterprise Zone, the Council will benefit from business rates in respect of the development.

8. Legal Implications

8.1 There are no direct legal implications arising from the report. The necessary legal agreements will be completed in due course by Legal Services. In order to mitigate risk to the Council, checks will be carried out on the developer’s ability to complete the legal documentation.

9. Human Resource Implications

9.1 There are no human resource implications arising from this report.

10. Implications for Children and Young People and Vulnerable Adults

10.1 There are no direct implications for Children and Young People and Vulnerable Adults. In a broader context the project supports business and economic growth which assists in creating opportunities for children, young people and vulnerable adults.

11. Equalities and Human Rights Implications

11.1 There are no equalities and human rights implications arising from this report.

12. Implications for Partners and Other Directorates

12.1 There are no direct implications for partners and other directorates.

13. Risks and Mitigation

13.1 Property Market and Investment Risks – the property market is cyclical. A fall in market confidence could cause potential developers and end users to change investment decisions impacting on the successful delivery of the project.

13.2 Mitigation - The Council has taken professional advice which demonstrates the market potential to deliver this project.

13.3 Construction Risks – building costs could escalate or the developer could cease trading prior to completion of the contract.
13.4 Mitigation – a fixed price will be agreed for the completed development prior to construction commencing. Construction works will be managed by the developer and any unforeseen or additional costs arising during construction will be the responsibility of the developer. Checks will be carried out on the ability of the developer to complete the contract and legal agreements put in place to protect the Council’s position in the event that the developer is for any reason unable to complete the development as agreed. JF Finnegan is an experienced and established local developer and contractor with a turnover of circa £50 million per annum and net assets of £24.3 million.

13.5 **Finance Risks** – insufficient revenue is generated to fund the investment.

13.6 Mitigation - The proposed arrangement with JF Finnegan will be subject to a financial viability assessment on the final terms of the proposal. The availability of a rent guarantee will ensure that the Council is protected from the risk of voids over a 3 year period.

13.7 **Procurement Risks** – the Council may be challenged on the use of an exemption to standing orders.

13.8 Mitigation – the value of the public works contract will be below the OJEU threshold of £4.1 million and an aggrieved party would not have recourse to remedies under procurement regulations. It is not possible for the project described in this paper to proceed on the basis that development is delivered by a third party and this justifies the use of an exemption to standing orders.

14. **Accountable Officer(s)**

   Damien Wilson - Strategic Director of Regeneration and Environment.
   Tim O’Connell - Head of RiDO.

Approvals obtained from:-

Jon Baggaley, Finance Manager
Assistant Director of Legal Services:- Ian Gledhill
Head of Procurement (if appropriate)

*Report Author: Tim O’Connell – Head of RiDO*

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