Herefordshire Council

AGENDA

Urgent Meeting of Cabinet

Date:	**Wednesday 31 October 2012**
Time:	**10.00 am**
Place:	**The Council Chamber, Brockington, 35 Hafod Road, Hereford**
Notes:	Please note the **time, date** and **venue** of the meeting. For any further information please contact: **Sally Cole, Governance Services** Tel: (01432) 260249 Email: scole@herefordshire.gov.uk

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Agenda for the Meeting of the Cabinet

Membership

Chairman	**Councillor JG Jarvis**
	Councillor H Bramer **Councillor RB Hamilton** **Councillor AW Johnson** **Councillor PM Morgan** **Councillor RJ Phillips** **Councillor GJ Powell** **Councillor PD Price**

AGENDA

		Pages
1.	**APOLOGIES FOR ABSENCE** To receive any apologies for absence.	
2.	**DECLARATIONS OF INTEREST** To receive any declarations of interest by Members in respect of items on the Agenda.	
3.	**VARIATION OF RETAIL QUARTER (OLD LIVESTOCK MARKET) DEVELOPMENT AGREEMENT** Further to its key decision on 5 April 2012, to seek Cabinet approval to vary the terms of the Retail Quarter Development Agreement documentation.	1 - 10

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HEREFORDSHIRE COUNCIL

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Herefordshire Council

MEETING:	**CABINET**
DATE:	**31 OCTOBER 2012**
TITLE OF REPORT:	**VARIATION OF RETAIL QUARTER (OLD LIVESTOCK MARKET) DEVELOPMENT AGREEMENT**
PORTFOLIO AREA:	**ENTERPRISE AND CULTURE**

CLASSIFICATION: Open

Wards Affected

Central Ward/County-wide

Purpose

Further to its key decision on 5 April 2012, to seek Cabinet approval to vary the terms of the Retail Quarter Development Agreement documentation.

Key Decision

The key decision in this case was advertised in the Forward Plan and taken in April 2012 to proceed with agreements with Stanhope Plc and British Land Plc on the grounds that this was likely to involve the Council in incurring expenditure which is, or the making of savings which are, significant having regard to the Council's budget for the service or functions to which the decision relates. The decision now sought is to vary the terms of the agreement and is not therefore a new key decision.

Recommendation(s)

THAT:

(a) **the revised funding arrangements between Stanhope Plc and British Land Plc be approved; and**

(b) **authority to be delegated to Director for Places and Communities to finalise the necessary documentation required to address the issues raised in this report.**

Key Points Summary

- The Retail Development Agreement was originally approved by Cabinet on 25 June 2009 and was subsequently revised in September 2010 by Cabinet Member Decision in terms of phasing of the project. Further amendments were agreed by Cabinet in April 2012 in order to secure the funding for the delivery of phase 1.

Further information on the subject of this report is available from
Geoff Hughes, Director for Places and Communities (01432) 260695

- Since the Cabinet approval in April documents varying the Development Agreement have now been exchanged between Stanhope Plc, British Land Plc and the Council.

- Approval is now sought for further amendments which are described under Key Considerations in order that the agreement can go unconditional and enable the scheme to be built.

Alternative Options

1. Not to agree the amendments. This would leave Stanhope Plc without external funding to deliver Phase 1 of the old livestock market redevelopment. This would defeat the long-held objective to see the redevelopment of the former livestock market site and the community and economic benefits that redevelopment will bring.

Reasons for Recommendations

2 Following the exchange of contracts British Land Plc have taken a view that changing market conditions mean that for them to continue they need to see a change in the financial return from the development. British Land's view was also informed by the fact that the number of pre-lets achieved had not met their target. In addition to British Land's requirement to renegotiate terms, one of the original clauses in the Development Agreement provided for Stanhope Plc to satisfy themselves with the ground conditions for the development. Stanhope Plc have now completed assessments of ground conditions and have confirmed that they will need to incur costs of £1m above their initial estimates before development can be commenced.

Introduction and Background

3 After a European procurement process and subsequent detailed financial and programming negotiations, on 25 June 2009 Cabinet approved the move to conclude negotiations and enter into a development agreement for the retail quarter on the old livestock market site. This agreement was completed in November 2009.

4 Further detailed financial, design and programming negotiations took place as a result of which, on 24 September 2010, the then Cabinet Member for Economic Development & Community Services approved arrangements for the completion of a supplementary agreement to provide for changes to the phasing of the scheme.

5 Further variations to the Development Agreement were agreed by Cabinet on 5 April 2012 and were implemented following Delegated Officer Decision by the Director for Places and Communities on 27 September 2012.

6 This reports sets out additional variations sought by Stanhope Plc and British Land Plc in order to allow the development to proceed.

Key Considerations

7 The variations sought would enable:

- The Funding Agreement between British Land Plc and Stanhope Plc to go unconditional, meaning that the development will proceed and for British Land Plc to fully fund the project. This will follow immediately from the Council confirming that it is satisfied with the revised funding terms, which will allow Stanhope Plc to satisfy the funding Condition Precedent in the Development Agreement.

- Stanhope Plc will confirm that it is satisfied with the Environmental Condition Precedent in the Development Agreement. This confirms that Stanhope Plc accepts the site ground conditions.

- Stanhope Plc to meet the shortfall in the terms of its Funding Agreement with British Land Plc in part by the Council accepting a £500k reduction in the payments owing to the Council by Stanhope Plc/British Land Plc.

8 The variation sought to the payment to the Council arises as a result of changes to general market conditions which have led the funder, British Land Plc, to renegotiate the funding terms it is prepared to sanction with Stanhope Plc. These are the best terms available to Stanhope Plc, and the attached Appendix 1 [Montagu Evans Letter] confirms that this represents good value for money for the Council.

9 In consideration of Stanhope Plc accepting a 0.2% reduction in the funding yield, British Land Plc has accepted a reduction in the required pre-lets. As a result, one required pre-let has been removed as a funding pre-condition. This change has no impact on the Letting and Displacement Strategy contained within the Development Agreement which remains unaltered.

10 Subject to Cabinet endorsement of the proposed variations, it is recommended that approval be delegated to the Director for Places and Communities to finalise the necessary documentation.

11 Appendix 2 summarises the impacts and risks associated with the proposed variations to the development agreement.

Community Impact

12 The variations do not of themselves impact either the community assessments or community and economic benefits previously expressed.

Equality and Human Rights

13 In the case of this report there is no direct impact on individuals or communities in terms of equality or human rights.

14 Stanhope Plc has signed up to the Hereford Futures Sustainability Policy which includes social sustainability indicators such as: demography, community involvement, accessibility, and equality and social justice.

15 Sir Robert McAlpine, as principal building contractor, will comply with all relevant equality and diversity legislation and will accord with the council's Equality and Human Rights Charter.

Financial Implications

16 Under the terms of the Development Agreement Herefordshire Council will receive £1.5m in capital receipt from Stanhope Plc at the point of completion in respect of Phase 1 of the development. In order to meet the requirements of the revisions to the Development Agreement it is recommended that the £500k contribution requested from the Council is met by waiving £500k of this capital receipt. The £1.5m had been factored into funding capital schemes and the £500k will now be covered by capital receipts, prudential borrowing or a

combination of both.

17 Payments in respect of Phase 2 and future car park income to the Council remain unaltered.

Legal Implications

18 This development engages the European Procurement rules. Because the proposals in this report change the Development Agreement, Members should be alive to the possibility of challenge. Advice has been sought from Pinsent Masons on this matter as set out in Appendix 3. Accordingly, officers would advise Members that a re-procurement is not appropriate and that the steps outlined to protect the Council in the event of challenge being taken aim to mitigate any risk.

19 The Council may dispose of land held by them in any manner they wish by virtue of section 123, Local Government Act 1972. However there is a general obligation not to do so for a consideration less than the best that can reasonably be obtained. The advice of external valuers is that the proposed variation fulfils the statutory and fiduciary obligations of the Council.

Risk Management

20 Risks arising from the proposed variations are included in Appendix 2.

Consultees

21 The Hereford Futures Board Members have been advised of the terms of the proposed variations. The Board support the amendments sought. The development of the retail quarter has been subject to a significant consultation process, both through the selection of Stanhope Plc as preferred developer and as a part of the process to obtain planning approval.

Appendices

22 Appendix 1 – Montagu Evans Letter
Appendix 2 – Risk Register
Appendix 3 – Legal Advice from Pinsent Masons

Background Papers

- None identified.

City of London
Glasgow
Edinburgh

Appendix 1

MONTAGU EVANS

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AKH/LM/GV6390

30 October 2012

Jonathan Bretherton Esq
Hereford Futures
4 Blackfriars Street
HEREFORD
HR4 9HS

Dear Jonathan

COUNTY OF HEREFORDSHIRE DISTRICT COUNCIL ("the Council")
HEREFORD FUTURES LIMITED ("Futures")
STANHOPE PLC ("Stanhope")
(2) HEREFORD SHOPPING CENTRE GP LIMITED AND (3) UNION PROPERTY HOLDINGS (LONDON) LIMITED ("the Funder")
DEVELOPMENT AGREEMENT ("DA") RELATING TO THE RETAIL QUARTER SITE, EDGAR STREET, HEREFORD ("Retail Quarter")

I refer to previous correspondence and in particular my letter of 25 September 2012.

You are being asked to approve funding terms between Stanhope and the Funder which show a deterioration in the terms that were conditionally exchanged in late September between the two parties. This does not in itself impact the Council and I would advise that these terms are at least in line with market expectations.

Our analysis shows that neither the initial nor revised funding terms has a likelihood of overage being achieved for the Council.

Additionally, Stanhope have sought that the Council contribute £500,000 to the development, reducing the terms of the Council deal. However, the terms are highly competitive compared to what would be expected in the open market, if the Council were to re-tender the opportunity, based on the current market conditions.

If an alternative developer was to consider the opportunity they would either have to drastically reduce the quality of the development or seek greater financial assistance from the Council in order to achieve a market acceptable level of profit – being 15% to 20% of profit on gross development costs.

Stanhope are however fully committed to this project and are carrying out the project for an anticipated profit return of less than would be the market norm. The level of profit and the financial level of the Council deal do appear to me to deliver value for money to the Council, considering the Council's desire for a comprehensive, high quality, well integrated development that sees uses such as a cinema, modern multi storey car park, family restaurants and a department store, as well as retail occupiers new to the City. Attracting these uses are expensive and require to be subsidised by other uses/parties. As it stands, it is the reduced profit level of Stanhope that is a major contributor to the delivery of the quality of the project.

From our experience of other Local Authority led projects in the market at present, Stanhope's request is not surprising considering the overall viability of the development appraisal. This is in line with the funding appetite for major developments which, as has been shown, reduces end capital values and therefore impact on a developers ability to fund the upfront land and associated costs. Stanhope are therefore seeking that the upfront costs are reduced to take into consideration the reduced end value. Their detailed development appraisals and those of the Funders support this analysis. Montagu Evans are working for a number of Local Authorities who are being forced to re-negotiate terms agreed in 2007-2010 and the level of this request by Stanhope appears minimal compared to other projects we are having sight of.

We remain of the opinion that the proposed transaction is the best obtainable outcome for the public interest at this time with regard to the price and other conditions achieved. A comprehensive, high quality development for the city would not be deliverable at the same financial package to the Council if the Developer sought a market profit level as required by a new developer free from the historic costs that Stanhope have invested in this project.

I trust that the above clarification assists in your approval process. Please do not hesitate to contact me on any matter.

Kind regards.

Yours sincerely

ALAN HARRIS
E-mail: alan.harris@montagu-evans.co.uk

	Variation	Current Development Agreement Provision	Post Variation position	Risks and Mitigation
1.	The Funding Agreement between British Land Plc and Stanhope Plc to be exchanged conditionally, subject to the Council confirming that it is satisfied with the revised funding terms. The revised Funding Agreement changes the funding yield between British Land Plc and Stanhope Plc.	British Land Plc has agreed to fund the Stanhope Plc scheme based upon a funding yield equating to 6.5%.	British Land Plc and Stanhope Plc have now agreed that the yield within the funding structure will change to 6.3%, a worsening of the position from Stanhope's point of view by 0.2%.	• The risk of procurement challenge is addressed by the proposed structure of the documentation suggested by Pinsent Masons. • The general economic climate has continued to worsen throughout this negotiation. However, this variation represents the final obstacle, meaning that there can be no further variations sought from the Council in return for the Agreement becoming unconditional. As a consequence of the 0.2% yield change, the payments by British Land Plc to Stanhope Plc will reduce by £3m. By agreeing to this variation, the Council is agreeing to accept a waiver of £500k from the consideration payable to it by Stanhope Plc. • Montagu Evans confirm that this deal continues to represent the best obtainable outcome for the public interest at this time with regard to the price and other conditions achieved. • Stanhope Plc have confirmed that the deal offered by British Land Plc represents the most

				favourable terms available in the market. • As a consequence of this variation, Stanhope Plc will confirm that it is satisfied with the condition of the site and its ability to meet the remediation costs.
2.	Reduction in the number of pre-lets required by British Land Plc in the Funding Agreement.	Stanhope Plc must achieve pre-lets to six named tenants in order to satisfy the terms of the Funding Agreement with British Land Plc.	Stanhope Plc must achieve pre-lets to five named tenants in order to satisfy the terms of the Funding Agreement with British Land Plc.	• The Development Agreement between the Council and Stanhope Plc requires Stanhope Plc to achieve pre-let by 40% of the total estimated rental value of the scheme and 50% of the total floor space of the scheme. Stanhope Plc has already satisfied these thresholds and has contractually secured 46% pre-lets by value and 62% by scheme floor space. • The reduction of the number of required pre-lets from six to five in the Funding Agreement means that Stanhope Plc has satisfied the pre-let conditions within both the Development Agreement and the Funding Agreement, thus allowing the contract to become unconditional.

PINSENT MASONS REPORT ON PROPOSED CHANGE TO THE RETAIL QUARTER DEVELOPMENT AGREEMENT

1. BACKGROUND

1.1 The Development Agreement for the development of the Retail Quarter Site was entered into by the Council and Hereford Futures with Stanhope Plc on 4 November 2009. By way of a Supplemental Agreement dated 25 March 2011, the Development Agreement was varied to document the proposed phased development of the Retail Quarter Site. The phases are the currently proposed Phase One Site development and a possible future Phase Two.

1.2 The Development Agreement is currently in a conditionality stage, being the stage where Stanhope Plc are endeavouring to satisfy various outstanding Conditions Precedent, such as the Funding Condition, in order for the Development Agreement to become unconditional.

1.3 We refer you to our advice of 5 March 2012 as updated on 29 August 2012 and 25 September 2012 (copy attached for ease of reference) (the "Previous Advice") with regard to the previously proposed changes required by Stanhope's funder to the Development Agreement. By way of update these previously proposed changes were incorporated in to the documents which are referred to in the Previous Advice, and in respect of these documents:-

1.3.1 the Deed of Agreement was exchanged on 28 September 2012. This Agreement provides for the completion of the documents referred to at 1.3.2 below subject to all of the pre-conditions in the Development Agreement being satisfied (or waived where permitted under the Development Agreement) and the Development Agreement becoming unconditional by 28 December 2012;

1.3.2 the Deed of Variation, the Deed of Novation and the Phase Two Site Option Agreement have all been signed by the Council and have been released to Stanhope for completion subject to satisfaction of the pre-conditions in the Development Agreement by 28 December 2012.

2. AMENDMENT TO THE DEVELOPMENT AGREEMENT NOW PROPOSED

2.1 As a result of recent negotiations between Stanhope and its funder, the funder has required changes to the terms of its agreed funding deal with Stanhope.

2.2 The Council in the Deed of Agreement dated 28 September 2012 approved the headline terms of Stanhope's funding deal with its funder, and these headline terms are set out at Appendix 1 to the Deed of Agreement. As a result of the recent changes to the funding deal proposed by the funder, Stanhope have requested the Council's approval to the revised headline funding terms, such approval to be given by way of a letter from the Council to Stanhope and to the funder (which letter will attach the amended headline funding terms). We understand that Montagu Evans have reviewed the changes to the funding deal and that they still represent the best funding deal that is currently available in the market (see the separate Montagu Evans' report).

2.3 We understand that the changes to the funding deal mean that Stanhope will receive circa £3 million less from the funder, and that Stanhope have requested a "contribution" of £500,000 from the Council to this £3 million shortfall. The detail of how this £500,000 is to be made up is subject of further discussion. To document this "contribution" a further Deed of Variation to the Development Agreement needs to be entered into between the Council and Stanhope (the "Deed of Variation"). This deed will be completed once the make up of the £500,000 has been further discussed. See also at 3.2 below.

3. PROCUREMENT AND CHALLENGE ISSUES

3.1 As noted in our Previous Advice, whenever variations are proposed to a Development Agreement it is necessary to consider the public procurement issues resulting from the variation and we have issued advice to the Council in this regard.

3.2 As a result of our procurement advice, the Deed of Variation will include a clause which will provide that the Council's £500,000 "contribution" is subject to it not being capable of being challenged, whether on grounds of procurement or state aid, or as a result of a more general judicial review challenge.

Pinsent Masons

30 October 2012