

<b>MEETING:</b>	<b>CABINET</b>
<b>MEETING DATE:</b>	<b>13 November 2014</b>
<b>TITLE OF REPORT:</b>	<b>Council acquisition of the Three Elms Trading Estate, Hereford, HR4 9PU</b>
<b>REPORT BY:</b>	<b>Ian Higgs – Development Manager</b>

## **Classification**

Open.

## **Key Decision**

This is a key decision because it is likely to result in the council incurring expenditure which is, or the making of savings which are, significant having regard to the council's budget for the service or function to which the decision relates.

NOTICE has been served in accordance with Part 3, Section 9 (Publicity in connection with key decisions) of The Local Authorities (Executive Arrangements) (Meetings and Access to Information) (England) Regulations 2012

## **Wards Affected**

Three Elms.

## **Purpose**

To approve the council's purchase of the Three Elms Trading Estate from the Homes and Communities Agency at market value, estimated to be in the region of £1.75 to £1.85m, which will enable the council to release value from its adjoining land.

## **Recommendation(s)**

THAT:

- (a) Subject to Council approval of the 2015/16 capital programme and subject to agreeing acceptable terms, the council purchases the freehold interest of the Three Elms Trading Estate from the Homes and Communities Agency;**
- (b) Subject to Council approval of the 2015/6 capital programme, further investment of £850k be made into the estate in order to improve the site infrastructure thus improving the prospect of further investment in the development of the vacant land and improvements to the existing buildings;**
- (c) It be recommended to Council that provision of £2.6m be made in the 2015/16 capital programme to support the above recommendations.**

## **Alternative options**

- 1 The Homes and Communities Agency (HCA) proceed to offer the estate for sale on the open market and complete a sale before March 2015. Depending upon the priorities of the eventual purchaser the estate may deteriorate further due to lack of investment which would impact on the surrounding residential estates and public open space. It would also result in a missed opportunity to maximise the economic benefit that the estate could make in the contribution to the economic growth of the city/county by providing existing and new commercial premises to attract new business and enable the growth of existing ones. The estate was purchased by HCA in support of the council's delivery of the city centre redevelopment scheme and if the council were to purchase that function would continue.
- 2 The HCA retain ownership of the estate. This is not an option as the property is part of their Local Stewardship Delivery Plan and is identified for disposal during the period 2012/15. The HCA have agreed to delay the disposal to the latest possible time in order to allow the Council to present the best possible case at the Link Road CPO Public Inquiry which closed in May. The HCA will proceed to market and dispose of the estate by March 2015 unless a sale to the Council is completed this year.

## **Reasons for recommendations**

- 3 There are several reasons why the council should purchase the estate, the main ones being as follows:
  - Financial return. Purchase of the estate has a positive financial benefit for council over the short to medium term. Assuming terms can be agreed to purchase for £1.75m the net rental income would cover the annual borrowing costs of £98k. The site is currently over 80% occupied and whilst there is a risk that the income may reduce should units become vacant or expenditure increase. Occupancy levels would need to fall to below 65% before the borrowing costs exceeded the net rental

income.

- There is further opportunity to improve the quality and occupancy of the estate by carrying out additional works including drainage and access improvement totalling £850k. The borrowing cost of this would be £66k per annum and will be met from rental income if current occupancy levels are maintained.
- To support business growth and economic development in the city/county. Currently there are limited employment sites within the city north of the river and none in Council ownership. Those employment sites there are have in the past been subject to successful planning applications/appeals to change of use to residential which has inhibited the retention/growth of some business. By securing ownership the council is not reliant solely on planning policy to control the future use of the site it is also able to deliver development at a time that meets with the demands of business rather than be influenced by other private sector objectives.

## Key considerations

- 4 The Three Elms Trading Estate was purchased by Advantage West Midlands in 2006/7 and transferred to HCA in 2011. It comprises a site of approximately 7 acres of which approx 2 acres is undeveloped and in conjunction with the Council's adjoining 0.9 acres is capable of accommodating circa 60,000 sq ft of new industrial/warehouse space. There is currently some 61,500 sq ft of existing buildings of which 83% is let to a total of eleven tenants. The leases are all relatively short term i.e. will expire or with break clauses within the next five years and some units are currently occupied under licence pending completion of a lease. The site was purchased in support of the Council's delivery of the city centre regeneration scheme, primarily as a key employment site for the relocation of business from within the ESG area. While a significant part of the ESG scheme has been delivered i.e. retail quarter, further elements remain i.e. the link road and urban village. As such this key employment site still has a role in meeting the demand for business relocation and its ownership by a body that is committed to supporting the delivery of key Council objectives is desirable.
- 5 It should be noted that the Council does not propose to undertake any direct development of new buildings. It is envisaged that new development will take place by the Council working with occupiers or developers who will provide the funding for any new buildings. Although the option of direct development should not be ruled out subject to there being funds available and a robust business case presented at the time.
- 6 The Council owns approximately 0.9 acres of land adjacent to the northern boundary of the estate, which carries an estimated value of £200k as employment use land. Whilst this land has outline planning permission for employment use, it cannot be accessed or serviced other than through the trading estate. The Council can only release the value of this area of land by either purchasing the trading estate and merging the two land areas to effectively increase the overall size of the trading estate; or by purchasing access rights and easements from the owners of the trading estate. The HCA have indicated that they would consider this but only if the land were to be sold at the same time as they sell the estate and the Council share the sale proceeds of its land on a 50/50 basis, i.e. the Council would only receive 50% of the commercial value of its land. A new owner may not be prepared to grant access or easements.
- 7 If the HCA offers the property for sale on the open market then a new purchaser will have different objectives and pressures and, while it may be possible for the Council to establish a relationship that will result in some recognition of Council priorities, these will

only be secondary and therefore delivery of Council objectives may be delayed or frustrated.

- 8 The Council already has an existing property portfolio and is experienced in owning and managing property of this type i.e. Rotherwas industrial estate. It has been managing the estate on behalf of the HCA for the last three years, albeit with short term management objectives which would need to change once owned by the Council. Initially existing staff from the Property Services and Economic Development teams would manage the property but additional support may be needed to manage the further investment and this would be funded from the surplus rental income or from the allocated capital budget.

## **Community impact**

- 9 There is unlikely to be any immediate community impact following acquisition of the trading estate by the Council. However over time following implementation of the investment the built environment of the estate will improve and this should have a positive impact on the adjoining houses and users of the public open space. Further investment will over time result in more job opportunities for local people and more and better quality premises for business growth.

## **Equality and human rights**

- 10 There are no equality or human rights issues associated with this project. The marketing and letting of vacant units will be compliant with equality and human rights policy.

## **Financial implications**

- 11 It is proposed that the Council will use prudential borrowings of £2.6m to fund the project, being circa £1.75m for the purchase of the freehold and the balance i.e. £850k for the following site improvement works. The annual cost of borrowing the total amount would be £164k for 25 years. This is made up of £98k for the purchased of the freehold and £66k for improvement works. The current net rental income generated from the estate is £180k so will fund the repayment of the borrowings over a 25 year period.
- 12 It is anticipated that as planned improvement works are carried out occupancy and rents will increase or part disposals will generate capital receipts then the borrowings could be reduced.
- 13 After meeting borrowing costs, any surplus income will contribute to the Council's overall budget position.
- 14 Purchase of the trading estate will also enable the Council to realise and retain 100% of the value of its adjoining land (£200k) which already has outline planning permission for employment use.

## **Legal implications**

- 15 Legal will need to conduct extensive due diligence to investigate key issues which could affect the viability of the proposed purchase to include reviewing all current lease and licence arrangements as if the site is acquired it will be subject to such occupation and whatever terms are in place will bind the council whether favourable or not..
- 16 Legal will need to review whether the proposed purchase improves the potential for the adjoining land.

- 17 There is no guarantee even if tenants have been paying rent and observing the covenants of their leases that they will continue to do so and thus the site could result in liabilities rather than income in the worst case scenario.
- 18 The opinion of the district Valuer will be necessary to attest to the market value of the purchase price.
- 19 It is proposed that the borrowing for the purchase is met via rents over a 25 year period. Unless the current tenants are all occupying pursuant to leases with another 25 years to run which is very unlikely this is not certain. All purchases of commercial property involve a level of risk but this does need to be accepted.
- 20 Procurement will need to be consulted as to the appointment of agents for marketing of units once the council is in a position to do so.

## **Risk management**

- 21 There are the normal risks associated with owning commercial property i.e. non-payment of rent or arrears due to tenant cash flow/trading problems, tenant bankruptcy, empty property costs, unrecoverable repair and maintenance costs etc. Through the Council's existing staff resources and procedures, careful and active management, these risks will be managed and reduced where possible.
- 22 A down turn in the economy or increased borrowing costs may squeeze the rental income or increase the expenditure. However a number of sensitivity tests have been carried out and the project can stand an approximate 20% variance to income or expenditure without while still maintaining a self-funding position.
- 23 As part of the selling process reports are being commissioned on the condition of the existing buildings and services and once these are available the future investment plan will be finalised to accord with the priorities and available budget.
- 24 In the event that the Council should not purchase the estate from the HCA it will need to work with the HCA to agree a communication statement regarding the disposal.

## **Consultees**

- 25 In addition to the seven internal consultees, the Economic Development Manager has been consulted on and is supportive of the report and its recommendations. We have consulted with the HCA regard to the Council's potential interest in purchasing the property. Following a decision on this report we will contact the tenants on the estate and advise of the (proposed) acquisition by the Council.

## **Appendices**

Appendix 1 - Map of estate and adjoining council land

## **Background papers**

None identified.