

Bath & North East Somerset Council

DECISION MAKER:	Cllr Gerrish, Cabinet Member for Finance & Efficiency Cllr Paul Myers, Cabinet Member for Economic Development	
DECISION DATE:		EXECUTIVE FORWARD PLAN REFERENCE: E2991
TITLE:	Commercial Estate Investment in the Bath Quays South Office Development	
WARD:	Widcombe	
AN OPEN PUBLIC ITEM		
List of attachments to this report: <ul style="list-style-type: none">• Appendix 1 Exempt Commercial Estate Business Case		

1 THE ISSUE

Bath Quays is the Council's flagship regeneration and economic development project at the heart of the Bath City Enterprise Area. Bath Quays South will deliver much needed employment space alongside the comprehensive regeneration of the Newark Works to bring derelict buildings back into beneficial use for much needed creative workspace. The project will contribute to B&NES commitment to delivering up to 3500 new homes and 9000 new jobs within the EA alongside increasing business rates income as part of the West of England City Deal.

The supply of good quality office space in the city centre of Bath has declined from around 360,000 sq ft in 2011 to only 55,000 sq ft in 2016. The most significant addition over the past 12 months has been the refurbishment of 20 Manvers Street. The building has provided over 45,000 sq ft of high spec office space. This development was the first major speculative development in Bath for a number of years and was fully let during the initial stage of construction achieving rents of up to £31 per sq ft.

This report seeks approval to drawdown £16.2M of total funds of £53.6M included in the budget for Commercial Estate Investment against a full business case to deliver the project.

A previous decision E2903, which was made in May 2017, noted an opportunity for the Council to deliver this scheme and referenced the role this could play in achieving the financial objectives of increased income for the commercial estate as well as helping to diversity the estate.

This report seeks approval to now bring that scheme forward and for the Council to deliver this project to achieve regeneration benefits as well as revenue for the Council. That revenue is needed to help the Council fund essential services whilst achieving its financial targets.

2 RECOMMENDATION

The Cabinet Members are asked to agree:

- 2.1 To fully approve £16.2M of the provisionally approved 2017/18 and 2018/19 capital budget for Commercial Estate investment.

3 RESOURCE IMPLICATIONS (FINANCE, PROPERTY, PEOPLE)

- 3.1 Following the Council decision E 2903 taken on 29th April to fully approve £6.245m of the £9.012m provisionally approved 2017/18 capital budget for Innovation Quay - Economic Development Funding Enabling Infrastructure this report seeks approval for the Commercial Estate to fund the development of the new 46,000 ft sq office development on the Bath Quays site
- 3.2 A budget of £53.6m was provisionally approved by Council in February 2017 for property acquisitions and investment which lead to future revenue generation made up of £29.1 million in 2017/18 and a further £24.5 million in 2018/19.
- 3.3 Release of this funding has been subject to individual business case for each investment opportunity. Total costs of this proposed development is £16.2m (£3.9m in 2017/2018 and £12.3m in 2018/2019).

Taking into account Commercial Estate Investment spend approvals that have already been agreed, or are currently seeking decision, leaves provisionally approved funding of £3.94 million remaining in 2017/18 and £24.5m in 2018/19 available for this and further schemes.

- 3.4 This report requests the full approval of the capital funding for the development of this property.
- 3.5 This proposal links to the already approved Medium Term Service Resource Plan which places a requirement to generate an additional £1.475 million (net) of income from the Commercial Estate as part of the 2017-18 to 2019-20 budget period.
- 3.6 The acquisition and build costs will be funded by service supported borrowing, costs of which have been factored in against future rental income projections as detailed in the attached business case. After allowing for borrowing cost, refurbishment sinking fund, the investment will provide a net return to the Council of circa £600k by 25/26. Returns prior to 24/25 will be £370k per annum due to the detailed assumptions about phasing of rentals and occupation plus borrowing costs as set out in the business case.
- 3.7 The Business case requires use of the Council's invest to save scheme to temporarily fund revenue borrowing costs during the construction period. The total drawdown from unearmarked reserves is estimated at £339k and this will be paid back within the first 5 years of the rental period. This approach has been agreed by the S151 officer in consultation with the Cabinet Member for Finance & Efficiency in line with the approvals required for accessing the scheme.

- 3.8 Previous funding for the Bath Quays development include

- a. Full approval of £3.137m of Cycle City Ambition Fund 2 (CCAF2) on Bath Quays Bridge and connecting infrastructure (approved under previous Council Decision E2838).
- b. Full approval of £7.1m Revolving Infrastructure Funding (RIF) for the delivery of Bath Quays Waterside Flood Mitigation works of which the relevant part for this Decision is £1m.
- c. Outline approval for £36m Economic Development Fund (EDF) of which the relevant part for this Decision is £6.245m.

3.9 The financial objective of this phase of the Bath Quays programme is to support economic regeneration and to optimise revenue via the commercial letting of new grade A flexible office space.

3.10 Overarching financial risks within the scheme as a whole include direct delivery risks associated with the development and construction of assets and time related inflation risks associated with the development process.

3.11 There is risk that the office development will have voids following completion leading to revenue pressures. To mitigate this, the Council has already appointed letting agents and working with the Council's Economic Development team, identified a number of prospective tenants with requirements well suited to the building. Failing market interest, the Council has the option to reconsider the application for Local Growth Funding via the LEP to operate part of the building as innovation grow-on space. If the LEP accepted and approved a new business case this would reduce the Council's financial exposure to market occupation.

3.12 VAT tax and State Aid implications are considered at each stage of the project to protect the Council's financial position.

3.13 Financial due diligence for the scheme has been provided by EY.

3.14 Commercial Letting Agents have been appointed to produce a market demand report. This indicates a strong demand for new grade A office space in Bath from both Bath based business who are looking to expand and from companies looking to relocate to Bath.

4 STATUTORY CONSIDERATIONS AND BASIS FOR PROPOSAL

4.1 In terms of the Corporate Strategy this development has direct relevance in the following areas:

- A Strong economy & growth – The Council is able to exercise active management over its property holdings and seek to ensure a varied portfolio mix and diversification of risk.
- An efficient business – this development contributes significantly towards achieving the Council's strategic review targets as well as the Directorate Plan income generation aspirations

4.2 In line with the Council's Financial Plan the income will be earmarked to protect frontline services, including the provision of adult social care; children and environmental services pursuant to the Councils general power of competence under s.1 Localism Act 2011

4.3 The investment in developing the property is in pursuance of the benefits (and in particular those of an economic nature) that it will confer upon the Council and its area, in accordance with s120 of the Local Government Act 1972. The investment aligns itself with the emerging strategy for the future management of the Council property portfolio.

4.4 The economic benefits conferred to the Council and its area specifically include;

Economic Regeneration

Diversification and mitigation of risk to the commercial estate portfolio, in terms of sector and type

Council resourcing - the investment will provide revenue required to assist in the delivery of the Council frontline services, which benefits the Council and its area directly

5 THE REPORT

5.1 Bath Quays South will deliver much needed employment led regeneration at the heart of the Bath Enterprise Area. The project will contribute to B&NES commitment to delivering up to 3500 new homes and 9000 new jobs within the EA alongside increasing business rates income as part of the West of England City Deal (refer Appendix 1).

5.2 The February 2017 budget report, approved by Council, includes provisional funding for commercial estate investment £53.6M and Bath Quays regeneration delivery £57M, both subject to business cases demonstrating investment return. Previous Decisions E2838 and E2903 have approved funding of £2.0M to progress the project to planning and full business case; with planning permission now granted, this report seeks approval of total funds of £16.2M against a project business case to deliver the project. The approvals sought for this phase are:

- a. Funding to enable the direct Council delivery of over 45,000 sq ft of net lettable grade A office space.

6 RATIONALE

6.1 City Deal agreement with the WoE Authorities have set out their growth ambitions. It is anticipated that the Bristol EZ and neighbouring EAs will deliver in excess of 60,000 new jobs by 2030 with the Bath City Riverside EA expected to contribute up to 9,000 jobs. Securing existing businesses in Bath maintains a healthy business community underpinning the ambition to create a vibrant critical mass of commercial employment space on Bath Quays.

6.2 Over the past 20-30 years, Bath has failed to develop modern office accommodation within the city. This is continuing to have a significant effect on the economy of Bath and the city now faces a tipping point in terms of maintaining a viable and attractive office sector. Neighbouring centres are increasingly proving more attractive to businesses due to the delivery of attractive, affordable and modern office schemes.

- 6.3 The private sector has failed to respond to demand, choosing instead to deliver more profitable residential accommodation in locations required for office delivery. This has resulted in the gradual decline in quality of Bath's office stock meaning that the city now has very little, if any, Grade A office stock which caters for the needs of modern office occupiers. Furthermore, the city's existing office stock is also coming under increased pressure from developers seeking to secure change of use to residential.
- 6.4 Bath is currently failing to offer suitable business accommodation and this is resulting in the loss of existing Bath-based businesses to surrounding localities where more modern, flexible office buildings can be secured and means that Bath is failing to attract new occupiers. This is having a direct impact upon the city's ability to retain and increase job provision and is affecting the city's ability to maintain its position as a location for high value added, low carbon and high-tech creative businesses.
- 6.5 BQS will yield additional net new floor space of 8,389sq m of additional floor space (net lettable area) across a variety of uses. This will create or protect 638 FTE gross direct jobs based on floor area and HCA jobs per floor area guidance. These new jobs support the generation of £54.1m of direct GVA and £48.9m of net additional GVA (per annum). It can generate £29.1m of direct incomes and £26.3m of net additional income in the B&NES / West of England economy.
- 6.6 The supply of good quality office space in the city centre of Bath has declined from around 360,000 sq ft in 2011 to only 55,000 sq ft in 2016. The most significant addition over the past 12 months has been the refurbishment of 20 Manvers Street. The building has provided over 45,000 sq ft of high spec office space. This development was the first major speculative development in Bath for a number of years and was fully let during the initial stage of construction achieving rents of up to £31 per sq ft.
- 6.7 As part of the Council's medium term financial plan, investment in strategic property assets supports the long term financial objective to generate secure revenue income for the Council.
- 6.8 This project facilitates delivery of the above targets. The full business case is included in the appendix to this report.

7 OTHER OPTIONS CONSIDERED

- 7.1 Options for the delivery of the Quays' programme have been considered and have focused on potential routes for delivering development on Bath Quays South. Options considered have included;
- a. Do nothing – this would involve leaving the site in its current state, continuing to incur significant security costs. This is not a viable option as it would not realise the Council's wider strategic policy ambitions for the site and would not represent an appropriate use of such a strategic property asset. Significant revenue reversion risk on resources deployed to date.
 - b. Disposal – the option for the Council to dispose of the freehold or long leasehold interest of the Newark Works on the open market was considered and discounted early in the options evaluation. A Bath based business had approached the Council to acquire this site; however the offer failed to realise

best consideration. The option to market the site for general disposal was discounted on grounds that the economic outcome could be best met by the Council in its regeneration capacity to deliver office led regeneration where the private sector has failed to do so. The decision not to progress this option but, rather to deliver this scheme ourselves, ensures we can control expenditure, avoid the additional payment of developers profit and ensure we deliver a scheme in line with Council aspirations based around the market advice we are receiving from our commercial advisers. The financing route can also be very efficient. Freehold disposal would not guarantee office delivery to meet occupier requirements and risk losing further significant employers to locations outside B&NES, negatively impacting the economic vitality of B&NES.

8 CONSULTATION

- 8.1 This report has been prepared in consultation with the Leader of the Council, the Cabinet Member for Economic Development, Cabinet Member for Finance and Efficiency, Section 151 and Monitoring Officers, the Strategic Directors for Place and Resources and Divisional Director for Community Regeneration.
- 8.2 Consultation with ward councillors, statutory and non-statutory consultees has been undertaken as part of the development of the scheme proposals leading to the submission of the planning application

9 RISK MANAGEMENT

A risk assessment related to the issue and recommendations has been undertaken in compliance with the Council's decision making risk management guidance.

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Background papers	<ul style="list-style-type: none"> • Cabinet decision E2680, E2838 & E2903 • Budget report February 2017
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