

## Bath & North East Somerset Council

DECISION MAKER:	<b>Cllr Paul Myers, Cabinet Member for Economic Development</b> <b>Cllr Gerrish, Cabinet Member for Finance &amp; Efficiency</b>	
DECISION DATE:	<b>On or after 22 December 2018</b>	EXECUTIVE FORWARD PLAN REFERENCE:
		<b>E3085</b>
TITLE:	<b>Commercial Estate Investment, Bath Quays South– forecast budget update funding approval</b>	
WARD:	Widcombe	
<b>AN OPEN PUBLIC ITEM</b>		
<b>List of attachments to this report:</b>		
<ul style="list-style-type: none"><li>• Appendix 1 Exempt Commercial Estate investment Business Case</li></ul>		

### 1 THE ISSUE

Bath Quays is the Council's flagship regeneration and economic development project at the heart of the Bath City Enterprise Zone.

Bath Quays South (the project) 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 includes Bath Quays Bridge (BQB) and Bath Quays South (BQS) which includes public realm and river infrastructure works and the Office building.

Detailed design of the river walls, flood defence and bridge has resolved significant technical challenges. Together these have had a consequential impact on cost and programme of the overall BQS project.

The BQS gap between the previous SMD approvals (E2680, E2838, E2903, E2991) at £25.095m and the BQS forecast budget of £29.001m is £3.906m. This report seeks full approval for £3.906m of the provisionally approved 2017/18 and 2018/19 capital budget for Commercial Estate investment.

### 2 RECOMMENDATION

The Cabinet Members are asked to agree:

- 2.1 To fully approve a further £3.906m of the provisionally approved 2018/19 capital budget for Commercial Estate investment to increase the approved budget for the BQS office development from £16.2m to £20.106m.

### **3 RESOURCE IMPLICATIONS (FINANCE, PROPERTY, PEOPLE)**

- 3.1 The principle drivers of cost inflation are as follows.
- 3.2 BQS - withdrawal of the original tenant from the office, necessitated a redesign of the office block to deliver a market facing multi let office and a Non-Material Application to the LPA to secure approval to the associated redesign of the river wall and flood wall. In addition demolition methodology adjustments necessitated by LPA requirements and steel cost price inflation since 2017 for the sheet piling have increased costs.
- 3.3 BQB - river wall technical challenges, bridge and abutment installation complexities, Avon Act compliance and environmental sensitivities involved. Challenges to deliver the superstructure installation have necessitated substantial temporary works and a larger crane. Steel cost price inflation since 2017 for the bridge fabrication has increased costs.
- 3.4 Previous Council Decisions for Bath Quays South have secured approvals to £25.095m, funded from WECA LGF and EDF and Council borrowing.
- 3.5 This report requests to fully approve £3.906m of the provisionally approved 2018/19 capital budget for Commercial Estate investment for the development of the office building.
- 3.6 This proposal links to the already approved Medium Term Financial Strategy requirement to generate additional income from the Commercial Estate.
- 3.7 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 costs, refurbishment sinking fund, the investment will provide a net return to the Council of circa £560k by 27/28. Returns prior to this will be circa £330k per annum due to the detailed assumptions about phasing of rentals and occupation plus borrowing costs as set out in the business case.
- 3.8 The Business case requires use of the Council's invest to save reserve to temporarily fund revenue borrowing costs during the construction period. The revised total drawdown from the reserve is estimated at £537k and this will be paid back within the first 5 years of the rental period. The use of the invest to save reserve has increased by £198k since the previous approval and 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 reserve. This further approval will fully commit the Invest to Save reserve.
- 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 who are working with the Council's Economic Development team to

identify prospective tenants with requirements suited to the building. VAT tax and State Aid implications are considered at each stage of the project to protect the Council's financial position.

## **4 STATUTORY CONSIDERATIONS AND BASIS FOR PROPOSAL**

4.1 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.

4.2 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 as well as delivering jobs.
- An efficient business – this development contributes significantly towards achieving the Council's strategic review targets as well as the Directorate Plan income generation aspirations.

4.3 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 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 Zone. The project will contribute to B&NES commitment to delivering up to 3500 new homes and 9000 new jobs within the EZ alongside increasing business rates income as part of the West of England City Deal.

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 approved funding of £2.0M to progress the project to planning and full business case; with planning permission secured and the two stage tender delivered, this report seeks funding to enable the direct Council delivery of 44,700 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. Bath City Riverside EZ is 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 (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 recent addition has been the refurbishment of 20 Manvers Street providing 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 & Community Regeneration, Cabinet Member for Finance and Efficiency, Section 151 and Monitoring Officers, the Corporate Director and Director for Economy & Growth.

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.

8.3 A screening discussion with the Council's Corporate Equality Officer has confirmed that previous stages in the Office and public realm project (including design, approvals and delivery) have already been considered in relation to the Equality Act and accessibility standards. Therefore there is no requirement at this stage for an Equality Impact Assessment to be undertaken purely in respect of the uplift in funding being proposed.

## 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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<b>Background papers</b>	<ul style="list-style-type: none"><li>• Cabinet decision E2680, E2838, E2903 &amp; E2991</li><li>• Budget report February 2018</li></ul>
<b>Please contact the report author if you need to access this report in an alternative format</b>	