

Joint Report of the Cabinet Member for
Planning, Environment and Regeneration and
the Cabinet member for Housing, Finance and
Welfare

City Centre Living- approval for two schemes

SUMMARY

- 1.1 The purpose of this report is to provide an update on progress with the City Centre Living initiative since Cabinet approval of October 2014 and to seek approval for the two applications received for combined loan and grant support.
- 1.2 The City Centre Living Fund is a recoverable loan based fund of £6.5m set up through service financed borrowing. The purpose of the fund is to develop a distinct housing and lifestyle offer in Derby city centre. It is available to property owners/ developers of vacant buildings and sites for residential use. There is also a sum of up to £250k grant funding to support projects where there are specific viability issues including additional cost due to conservation, design, sustainability or other issues related to viability for new build schemes on brownfield sites.
- 1.3 There has been a very positive response to the Council's initiative so far and the project team has dealt with over 20 enquiries on various sites across the city centre.
- 1.4 Two full applications have been received, processed and put forward for support by the City Living Fund:
 - Lodge Lane – 35 two bed new build apartments for market sale.
 - Willow House – Conversion of the two storey building opposite the Joseph Wright 6th Form College into 11 one bedroom apartments and 1 two bed apartment for market rental.
- 1.5 Significant due diligence and negotiation will be required for each scheme before the proposed financial arrangements can be completed.
- 1.6 The revenue impact over the lifetime of the proposed loans is viewed to be neutral on the Council. There is potential income of £30,000 for arrangement fees to be charged to the applicants to recover the costs of legal and property consultants and due diligence. A sum of £356,230 in form of New Homes Bonus paid over six years is expected to be received subject to delivery timescales being met. Delivery of 47 new homes will mean a maximum additional council tax income of £56,804 pa (This is at 2015/16 rates as Council Tax will be set on 3rd March 2015).

RECOMMENDATION

- 2.1 To approve in principle the funding proposal as set out in para 4.5 to 4.12 and instruct the officers to carry out the due diligence process and prepare the final loan and grant agreements.
- 2.2 To delegate authority to approve the final loan and grant agreements including the repayment schedule and security arrangements to the acting Chief Executive in consultation with the Cabinet Member for Planning, Environment and Regeneration and Director of Legal and Democratic Services and Director of Finance and Procurement.

REASONS FOR RECOMMENDATION

- 3.1 These are the first two schemes to come forward for funding approval under this initiative. Both applications meet the award criteria set for the City Living Fund and have been appraised by the Council's property consultants to ensure the deliverability of the outputs. The approval of funding to assist in the delivery of the identified schemes will help to increase the long term sustainability of Derby city centre, whilst minimising the level of risk to the Council with minimal or no additional pressure on the Council's resources.
- 3.2 It has been assumed that the changes to the city centre over the past 5 years, including improvements to the public realm, improvements to retail (Intu Shopping Centre) and to leisure (Riverlights), have created an attractive environment for young professionals who would not previously have considered living in Derby city centre. These applications, along with the interest generated by the scheme, provide a clear indication of demand for residential development within the city centre.
- 3.3 The delivery of these schemes will bring forward an additional 47 dwellings, which would be unlikely to come forward without the assistance of this funding initiative. The delivery of residential development on these sites, close to the University and Joseph Wright College, is expected to act as a catalyst for more schemes to come forward, enhancing its overall exposure and attractiveness, whilst improving the city living market and helping the Council to achieve identified housing targets.

SUPPORTING INFORMATION

- 4.1 The City Centre Living Initiative was approved by Cabinet in October 2014. It was designed in collaboration with the City Council's Regeneration, Strategic Housing, Conservation, Building Control and Planning services.
- 4.2 The two proposals seeking funding approval wholly align with an emerging trend of city centre residential proposals, and reinforce the Council's efforts to promote city centre living as a lifestyle choice.
- 4.3 There is continued on-going interest in the initiative evidenced by the number of enquiries by agents, developers and property owners for a wide ranging scale of developments.
- 4.4 The ability to approve funding for this first tranche of projects will serve to further enhance the attractiveness of the initiative and therefore act as a catalyst in respect of further schemes coming forward.
- 4.5 **Funding Proposal:**
- The total capital funding requirement of the two applications is:
- £485,000- loan fund for Willow House
 - £1,500,000- loan fund for Lodge Lane
 - £100,000- grant fund for Lodge Lane
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- 4.6 This funding will be subject to the detailed due diligence process and Cabinet approval. For the total investment of £1,985,000 recoverable loan fund and £100,000 of grant award, the outputs will be 35 two bed apartments (Band C), 11 one bed apartments (Band B) and 1 two bed apartment (Band B).
- 4.7 Interest rate to be chargeable at a minimum rate of 5.25% subject to completion of a due diligence process in relation to the applicants covenant and collateral provided to support the loan.
- 4.9 The final award of funding for the both above mentioned schemes is subject to DCC Cabinet approval and subject to the conclusion of a due diligence exercise including;
- Agreement of acceptable terms and security arrangements in line with draft Heads of Terms.

- Completion of a satisfactory due diligence exercise raising no significant issues of concern.
 - Adequate financial checks being undertaken in relation to the covenant of the applicant.
 - An up to date red book valuation will be provided to confirm the value of the completed scheme
 - Adequate security is provided for the loan.
 - Loan drawdown will be against project construction enabling monitoring of project construction.
 - Regular market updates will be provided by the applicant.
 - Longstop dates are provided for recovery of loan and interest where all repayment events have not occurred within the identified timeframes.
- 4.10 The terms of any loan finance in relation to each of the above would be provided so as to cover the Council's borrowing and administration costs. This is to ensure that there are no on-going costs to the Council of administering and servicing of any borrowing made to each project. As it stands, the combined effect of the financial package over the lifetime of the project on the Council's medium term financial plan is viewed to be neutral.
- 4.11 The Council will secure loan funding against a first charge against assets, such that the loan for the subject schemes will be no more than 66% of the completed scheme value or value of an alternative asset offered as security. A loan to value ratio at this amount is considered to provide an adequate level of security and is consistent with commercial bank and building society lending criteria. This is consistent with the agreed principles as set out in the October 2014 City Living cabinet report.
- 4.12 Loan and grant funding will be provided against certified expenditure monthly in arrears.
- 4.13 **Appraisal and Approval Process:**
- Both schemes requesting development finance (and grant funding) have undergone initial project assessment, Outline Assessment and Full Assessment in line with established project appraisal protocols. On this basis the schemes are understood to provide positive outcomes in line with the purpose of the City Centre Living Initiative. Council officers and their advisors have engaged and continue to engage with the respective applicants such that a mutually beneficial outcome can be arrived at for both the Council and the applicant.
- 4.14 Scheme proposals have already been discussed and approved in principle at the Derby Regeneration Fund Board meeting on 16th January 2015. Both schemes are considered to score highly in respect of deliverability, identified outcomes and security offered such that each of the projects will have a notable impact in respect of delivering intended outcomes with minimal resource impact and mitigated risk exposure for the Council.

- 4.15 A panel consisting of the project manager, property and legal consultants, chair of Regeneration Fund Board, Director of Finance and Procurement will meet to approve the final loan and grant agreements along with repayment schedule and agree the details of loan security. The final decision will be taken in consultation with the Acting Chief Executive and the Cabinet member for Planning, Environment and Regeneration as well as the Cabinet member for Housing, Finance and Welfare.

4.16 **Risk Management:**

As part of the due diligence checks the financial standing of the applicant is assessed and copy accounts have been provided which provide suitable comfort that the applicant is of sufficient standing to repay the agreed loan amount. It is considered that both of the applicants are of sufficient experience and standing to deliver the schemes as indicated. Additionally each of the applicants have agreed (subject to final due diligence) to offer the Council suitable security in relation to the loan funding.

OTHER OPTIONS CONSIDERED

- 5.1 An option of considering the suitability of the Builders Finance Fund in collaboration with the Homes and Communities Agency as an alternative funding mechanism to enable the development on both sites has been considered. Due to the timescales involved in processing the applications through that route, it was jointly agreed with the developers to reject that option and support the scheme with DCC funding.
- 5.2 In terms of physical development Radleigh Group considered various options in relation to scheme design, layout and density to improve viability. It is understood that the proposed scheme for which planning permission is granted (subject to the discharge of several conditions) offers the best mix of unit type, scheme design and overall quality on this key site. Watering down the quality of design of development in this prime location is not an option as it is against the Council's key objective of creating a vibrant city centre.

This report has been approved by the following officers:

Legal officer Financial officer Human Resources officer Estates/Property officer Service Director(s) Other(s)	Emily Feenan Martyn Marples and Sarah Smith NA NA Richard Williams Greg Jennings, Ian Fullagar
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List of appendices:	Appendix 1 – Implications
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IMPLICATIONS

Financial and Value for Money1.1 Capital

The total capital funding requirement of the two applications is:

- £485,000- loan fund for Willow House (to be funded from service financed borrowing)
- £1,5000,000- loan fund for Lodge Lane (to be funded from service financed borrowing)
- £100,000- grant fund for Lodge Lane (to be funded from the approved existing regeneration capital programme for the year 2015-18, from the City Centre Living budget)

1.2 Cabinet on the 18th February 2015 determined to support the City Living Initiative scheme through service financed borrowing.

1.3 £250,000 has been identified in the existing Regeneration Capital Programme for grant payments to cover abnormal development costs to include design, conservation, sustainability aspirations and issues related to city centre brownfield site viability.

1.4 Revenue

The revenue impact over the lifetime of the proposed loans is viewed to be neutral on the Council. If the Council was to provide loan finance to both the Radleigh Group and Paisley Grove Developments as identified, it would be provided in such a way so as to minimise revenue impacts on the Council, arising from any external borrowing that it needed to make to fund this proposal. The structure of any borrowing made and as detailed previously within the report, will have regard to the specific scheme proposals, the ability of the schemes to meet desired outputs from the fund and where suitable security and certainty of repayment is offered. A final due diligence exercise will be undertaken to ensure that the proposed repayments are viable for the respective applicants and the Council.

1.5 Any potential short term pressure on Council's budget, still to be captured, will be temporarily covered by the Regeneration Fund, reported through the Regeneration Fund Sub Programme Board.

1.6 **Arrangement fees:** An arrangement fee of £30,000 plus VAT is proposed and will be made payable to DCC upon entering into the grant and loan agreements. This will cover the application appraisal, due diligence and legal consultants costs.

1.7 **New Homes Bonus:** Both schemes will be eligible for receiving New Homes Bonus if the indicated timescales are achieved. DCC will receive a sum of £59,372 pa for 6 years, based on an assumption of 35 dwellings delivered in Band C and 12 dwellings delivered in Band B), adding up to a total of £356,230 in the year 2021. If further

schemes come forward for completion by March 2016, this income is anticipated to increase.

- 1.8 **Council Tax:** Delivery of new 35 homes of Band C and 12 homes of band B will mean a maximum additional council tax income of £56,804 (2015/16 charges) per year.
- 1.9 For the total investment of £1,985,000 recoverable loan fund and £100,000 of grant award, the outputs will be 35 two bed apartments (Band C), 11 one bed apartments (Band B) and 1 two bed apartment (Band B). The investment is recoverable together with accumulated interest and therefore there is no net cost of investment within the scheme subject to recovery of investment. On this basis, the only costs becomes the opportunity cost of investing within these as opposed to other potential schemes and no suitable alternative propositions have been identified at this time.

Legal

2.1 Powers

Local authorities have powers under the Localism Act 2011 to act in the same manner as any other legal person, save where those powers are specifically limited by statute. The making of loans would be permissible, subject to any statutory financial services or similar regulations that may be relevant. The fiduciary duty of the Council to the tax payer would require that there should be sufficiently robust arrangements concerning the repayment of any loans provided and adequate tangible security in place to cover the position in the event of default.

2.2 State Aid Implications

The Council must comply with EU law in relation to “State Aid” in providing any direct or indirect financial support to the Radleigh Group and Paisley Grove Development respectively. Officers are satisfied that the arrangements do not breach Articles 107 and 108 of TFEU (state aid). However, the position on State Aid will remain under review throughout the negotiation.

2.3 Legal Documentation

Freeths have been appointed as legal consultants who will liaise with the applicants’ solicitors and draft the legal documentation relating to the loans and associated security. This will be reviewed by the Council’s Legal Officers to ensure that the necessary security arrangements are put in place.

- 2.4 The standard form loan documents will contain provisions governing repayment of the monies in the event of default and, to the extent deemed necessary as a result of the approvals process, will provide for appropriate security to protect the Council’s investment. In addition, sale of the property will trigger early repayment of the loan and interest in full.

- 2.5 The standard form grant agreements will provide for the provision of monitoring information by the recipient and the right for the Council to claw back grant funding where it is not spent on achieving the specified outputs.

Personnel

- 3.1 NA

IT

- 4.1 NA

Equalities Impact

- 5.1 There are none specifically. Any development proposals linked to the City Living Fund will require Building Regulations approval covering means of escape, access and acoustics right through to energy efficiency and sustainability.

Health and Safety

- 6.1 NA

Environmental Sustainability

- 7.1 There are none specifically. General implications are:
- These schemes propose the use of empty buildings and vacant land to create more housing, reducing the impact of building on greenfield land.
 - Improving the building fabric of the vacant property will enhance their environmental performance and make them more energy efficient.
 - Housing in a sustainable location such as city centre will mean good transport links, resulting in reduction of car dependency.

Property and Asset Management

- 8.1 NA

Risk Management

- 9.1 The security provided by both the Radleigh Group and Paisley Grove Developments respectively for any loan finance provided to them will need to be sufficient to ensure that the Council is not exposed to the risk of default. Without such security being in place, the consequential on-going revenue liabilities of the Council servicing debt as a result could negatively affect delivery of other services to the public.

- 9.2 It is understood on this basis and as identified elsewhere within the report that suitable security is proposed for each of the schemes which would mitigate against a consequential and on-going revenue liabilities and therefore not affect the delivery of key and frontline Council services.
- 9.3 A detailed due diligence exercise is to be undertaken in respect of each project to fully determine the level of security offered and therefore the ability of the Council to recoup their investment in the unlikely event that the applicants are not able to repay their respective loan amounts. Red book valuations are to be undertaken for each property where security is offered such that all necessary assurances can be confirmed in the event of none or part payment. This due diligence will detail how the proposed level of security, principally offered as a first charge for each scheme, will allow the Council to recoup their investment including any additional charges associated with enacting their step in rights.
- 9.4 Loan to value ratios will not exceed the industry standard of 60/65% which is considered to offer an adequate level of security in relation to any loan investment made.

Corporate objectives and priorities for change

- 10.1 This initiative will contribute towards Derby Plan's big ambition:
- Inspiring place to live by improving inner city areas
 - Inspiring working life by improving skills and creating jobs