Cabinet
10 November 2015 **APPENDIX D**

WATERSIDE NORTH PHASE 1 - APPOINTMENT OF A DEVELOPMENT PARTNER

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Cabinet Member for Economic Development Delivery

1 Purpose

1.1 This report provides an update on the current marketing process (which commenced last Autumn) to seek a suitable Development Partner for the delivery of Phase 1 of the Waterside North scheme.

1.2 It also sets out a number of decisions for recommendation to Council to enable the next steps to be taken and the scheme to be delivered. This includes the costs associated with the development which need to be approved as part of the capital expenditure programme which forms a separate report on this agenda.

1.1 Recommendations

Cabinet recommends to Council, approval of the:

i) Appointment of Developer A as the Council's development partner

ii) Inclusion of £4.02m in the capital programme in order to acquire the commercial element of the development

iii) Expenditure of £3.3m for the public realm element of the scheme (also included in the capital programme) on the basis that this money is expected to be reimbursed by the South East Midlands Local Enterprise Partnership

2 Supporting information

Background

2.1 In the last 10 years, AVDC has been leading the redevelopment of Aylesbury town centre. Its record is impressive and has resulted in the delivery of major projects in the town centre such as Aylesbury Waterside Theatre, Waitrose, Travelodge and most recently the University Campus Aylesbury Vale.

2.2 AVDC's strategy on town centre redevelopment, has three key aims:

i. To improve the attractiveness of the town centre through developments which act as a catalyst for further investment by the private sector and other public sector partners for the overall benefit of the town and the economy. An example of this is the theatre which has attracted a range of new restaurants to the town and is underpinning interest in the Waterside North Phase 1 development.

ii. To use its own developments to directly generate new jobs and new wealth in the local economy - Waitrose and Travelodge have collectively delivered 200 new jobs.

iii To create a revenue stream for the council from the rental generated by tenants of the buildings constructed by AVDC.

2.4 Aylesbury Vale District Council is committed to the successful delivery of the Waterside North masterplan (Appendix 1), as the next development to help meet these aims.

2.5 The masterplan has been worked up in consultation with a number of stakeholders including Buckinghamshire County Council (BCC) who own land adjacent to the current temporary Exchange Street car park owned by AVDC.

2.6 The plan received wide spread public endorsement through a public consultation process in May 2014.

2.7 The context for the development and delivery of the masterplan is the Aylesbury Town Centre Plan which was approved by Cabinet in 2013. The Plan sets out the Vision for the town centre, the guiding principles for future development and a series of actions for improving different parts of the centre. Waterside North is one of the major actions in the Plan.

2.8 The masterplan is capable of phased and independent development of the areas of land within the different ownerships. This is an important factor given the volatility of the retail market in particular and as part of the public consultation on the masterplan, an outline scheme for bringing forward at this stage, the first phase of the masterplan was presented (Appendix 2).

2.9 For Phase 1, the County Council is initially focussed on repurposing its former offices in Walton street for residential led mixed use and the creation of a temporary surface car park which will help offset the parking spaces lost by the development on the Exchange Street car park . The BCC scheme has required the demolition of a number of buildings including the rear of the old County Offices and the a former police station building which had been vacant for a long time. The new car park is due to open in November 2015.

2.10 The AVDC element of Phase 1, has focussed on delivering a mixed-use scheme of up to five new café/restaurant units on the ground floor, with apartment accommodation on three levels above. The site is in the heart of the town centre in close proximity to the Odeon Cinema which enables the development to capitalise on the buoyant and growing café/restaurant market.

2.11 A new public square is also included in this phase. This will enable a significant area of new public space to be created in line with the Town Centre Plan Vision. The new public square will provide a fitting setting for the lighting of the torch celebrations associated with the start of the bi-ennial Paralympic Games. The link to the Paralympic legacy was an important factor in securing the grant funding from South East Midlands Local Enterprise Partnership (SEMLEP).

3. Progress to date

3.1 In preparation for seeking a partner, the Council has undertaken a number of preliminary activities. These include:

- Submitting an outline planning application in July 2014 (approved in February 2015)
- Securing a funding commitment from SEMLEP for the new public space

- Establishing occupier demand for the cafe and restaurant units (food and beverage/F&B)

4. The procurement process

4.1 The Council's objective is to secure a development which will:

- Initiate the Waterside North masterplan through a high quality first phase in line with the outline planning consent
- Generate an income from the commercial element of the scheme
- Improve the viability and attractiveness of the town centre so as to attract further private/public investment and enable the development of phases 2 and 3 of the masterplan to be brought forward

4.2 In September 2014, Cabinet considered three delivery options for Phase 1 and gave approval for two of the options to be explored further using the most appropriate procurement process. The two delivery options were:

1. Appointment of a building contractor to construct the scheme to an AVDC specification. In this option, AVDC as the sole developer would bear all the costs and risks on both the residential and commercial space (predominantly the café/restaurant units) but also all the subsequent financial benefit.

2. Appointment of a development partner to construct the whole scheme but with the partner financing and owning the residential element and AVDC financing and retaining ownership of the commercial space.

In both options, AVDC would own the public space.

4.3 A Bidders' day was held at the Aylesbury Waterside Theatre in January 2015. The purpose of the event was to present the Phase 1 opportunity to a wide range of potential developers, and encourage the participation in the procurement process.

4.4 In February, after consideration of a number of different procurement frameworks, the Council advertised its intension to seek a partner using a Housing and Communities Agency (HCA) framework and invited Expressions of Interest.

4.5 No expressions of interest were received from developers who only wanted to construct the scheme ie delivery option 1. All expressions of interest were for option 2 - the development partner option and two potential Development Partners were subsequently shortlisted to complete a Sifting Brief as the next stage of the procurement .

4.6 In June, the two potential Development Partners were invited to submit the following details as part of an Invitation to Tender (ITT):

- Scheme design proposals (which provide the basis for taking the outline planning consent scheme to the next stage of preparing a reserved matters application).

The developers were asked in particular to consider how best to optimise areas of the outline consent which are currently shown as internal car parking and some general commercial space fronting onto Long Lional.

- A detailed financial proposal prepared as a draft business plan and cash flow.

  The developers were asked to consider the premium payment(s) required from the Council to fully fund anticipated development expenses, how these can best be cash flowed, how access to Council finance can assist viability, how profit sharing (overage) should be structured and how any new/additional or saving in costs will be accounted for.

- The proposed legal arrangements which will enable the development to proceed. The submitted and marked up draft Development Agreement and Lease address the various preconditions to development, commencement and completion of works, recalculation of costs and the usual issues of performance, insurance and dispute resolution.

- Tender Acceptance – confirmation that the Tender is deemed to remain open for acceptance or non-acceptance for not less than ninety days after the date of receipt of Tenders. The Council may accept a Tender at any time within this prescribed period.

4.7 In essence, the requirements set out in paragraph 4.6 above, formed the pre-determined criteria for evaluating the bids. Both tenders have been checked initially for compliance by the Council and a further process of competitive dialogue has been undertaken with each developer to support the evaluation process and the recommendation that Developer A be appointed as the Council's Development Partner.

4.8 The evaluation was carried out by a combined panel of AVDC officers, the Council's general advisors on this scheme, Lambert, Smith, Hampton and specialist advisors including the Council's planning advisor (who submitted the outline planning application on behalf of the development arm of AVDC) and Strutt and Parker the letting agents for the food and beverage units.

5. The winning bid

5.1 It is important to recognise that the submission at this stage is not complete. If Council approve the appointment of Developer A as its Development Partner, there will be an intense period of progressing the scheme to detailed design as well as the need to finesse the draft Development Agreement which forms the detailed contract between AVDC and Developer A for the delivery of the scheme.

5.2 Meanwhile, a summary of the how the recommended bid from Developer A has sought to address the points in paragraph 4.6 is set out below.

5.3 **Scheme design proposals –** Developer A's bid proposes 4 café/restaurant units fronting the new public square with the commercial space fronting Long Lional designed to accommodate a further café/restaurant use in due course or alternative use as A1 (shops) or A2 (financial and professional services). The use of this unit will be a matter for the Council to decide and take forward.

5.4 Letting agents, Strutt and Parker, have confirmed that the café/restaurant space is marketable as configured and would be well received by operators. Up to three units would be pre-let. All four units would be let on 15 year certain leases.

5.5 Developer A proposes that the integral car park is not the best parking solution and should be replaced with a parking permit scheme. The integral parking space would be used to maximise the residential space and provide up to 47 one and two bedroom apartments.

5.6 The financial implications of losing parking spaces from Exchange Street car park both during the construction period and permanently are explained in section 6 of the report.

5.7 **Financial implications –** section 6 provides an overview of the key financial elements of the scheme many of which are requirements of the Council set out in the draft Development Agreement. The specific financial implications of Developer A's bid are set out in Appendix 1 of the confidential pages of the report.

5.8 **Legal arrangements –** whilst there are a number of area to finesse with the Developer A regarding the draft Development Agreement and a number of actions for the Council to take eg completion of a Right of Lights survey, there are not considered to be any insurmountable issues outstanding points of commercial negotiation.

5.9 **Tender acceptance** – the necessary confirmation has been received.

6. **Key financial elements of the scheme**

6.1 The financial structure of the scheme is that the Development Partner will accept the site from the Council and then build, at their own risk, the agreed development of residential and retail.

6.2 Upon completion of the construction phase, the Development Partner will sell the residential unit on the market and capture the value from doing so. The profit from the sales of the residential units will partially offset the cost of constructing the retail units and the Council will pay the Development Partner the previously agreed unfunded balance in order to take freehold ownership of the retail units.

6.3 The Council will let the commercial space to tenants and the income stream from doing so will represent the Council's return from the investment.

6.4 In return for an agreed profit element, the Development Partner accepts both the construction risk and the sales risk on the residential units.

6.5 In the event that property prices increase significantly during the development phase such that the Development Partner makes greater profits than envisaged, there will be an overage clause within the agreement to enable the Council to benefit from the unexpected uplift in values.

6.6 In the event that property prices fall then the Development Partner is committed to the sales values used in it calculation of the unfunded balance and any loss resulting from it is borne by the Development Partner.

Construction finance

6.7 Within the arrangement, the Council ultimately pays the unfunded balance, also termed the net estimated residual cost, of the scheme to the development. If the Council can mitigate the construction costs, or increase the sales values in any way during the negotiation process then it will benefit directly through achieving a lower net residual cost.

6.8 As the Development Partner cash-flows the construction phase (ultimately offset by the value of residential sales), the Development Partner 's financing costs would be a significant element of the proposal, which the Council would end up paying as it contributes to the residual net sum.

6.9 In recognition of its significantly lower borrowing costs, the Council has indicated to both Development Partners that it would cash-flow up to the 75% of the Development Partner 's costs (beyond the unconditional stage) and would request only a very small margin for doing so.

6.10 By capping its lending to 75% and requesting security over the partially completed asset, as a lenders charge, together with a parent company guarantee, the Council's financial interests are protected whilst at the same time ensuring that the cost to the Council of the Development Partner financing the scheme are minimised.

Public realm

6.11 Wrapping around the scheme and completing the area between Walton Street, the County Council's buildings and the existing Odeon complex is an area of public space. Government Growth Funding of £3.3m has been awarded for this element of the scheme by South East Midlands Local Enterprise Partnership. The grant is split between AVDC and the County Council - £3m is to be used for the public space that falls within AVDC's land ownership and this will cover the entire costs including design fees. The remaining £300k will be used towards the public space on land within BCC ownership. A public space architect has been appointed to design the whole scheme but will cost the two areas separately.

6.12 The Development Partner will be commissioned to undertake these works in order to reduce disruption to the town. The commissioning formed part of the procurement process and the works will be conducted on an open book basis with capped Development Partner fees so as to ensure both value and transparency.

Impact on car parking

6.13 The development on Exchange Street car park will see the permanent loss of approximately 90 spaces and potentially another 40 more during the construction phase.

6.14 The car park is popular with visitors to the town and generates income for the Council. The loss of spaces will, therefore, have an impact on income, but the exact implications are hard to predict.

6.15 Opening next door in November, is the County Council's temporary car park behind the Old County Offices. In capacity terms, this replaces the majority of the permanent spaces lost.

6.16 With or without the proposed development of this scheme, the opening of the County's Car park would have had an impact on car parking revenues from this site. It is, therefore, important not to confuse or attribute the revenue loss from one event to the other.

6.17 The development, in itself, will create additional demand for car parking within the town centre and it is reasonable to assume that the remainder of Exchange Street and the County Council's car park will be premium in meeting both existing and new demand. This should increase the already high levels of usage and this will in part offset the revenue from the reduction in spaces.

6.18 The Council also has lower utilised car parks within the town which could be used to accommodate the higher demand. Signing and pricing will be important factors in making sure that visitors are able to park in locations that satisfy their needs and these will be considered as part of the wider review of car parking provision in response to changes in both demand and provision.

6.19 Ultimately whilst there will be some impact on car parking provision within the town, through better utilisation of exiting car park s and through the additional provision represented by the County Council's new car park, there is enough parking provision to accommodate it.

6.20 The effect on revenue is, consequently, hard to predict as higher demand might offset lower provision in this favoured location. To demonstrate that the business case is robust in this regard an element of lost revenue to the Council has been factored in at 1/3 of the existing revenue assumed to be generated by these spaces, less the savings in direct operational costs.

6.21 The lost income represented by temporary loss of provision during the construction phase is assumed to form part of the Capital Sum and Fees.

Rental Income

6.22 The Council's advisors in respect of the commercial element of the scheme, Strutt and Parker, have reviewed the proposals put forward by the Development Partner and considered its commercial value in terms of location, the local market place and layout. Based upon this they have provided an assessment of the rental income the commercial space is reasonably likely to attract.

6.23 The numbers provided by the advisor have been used in the financial model, together with the standard terms that would usually be expected by the tenants. The one important point to note is that normal conditions expected within the market place include a rent free period of one year in order to develop the business and a capital incentive, equal to a further year, in order to defray fit out expenses.

6.24 So, in line with all similar commercial developments, the Council should not expect to receive any rental in the first two years of operation. Longer term, these incentives are recouped through the proportionally higher rental numbers. Lease rental periods would normally be for 25 years, with a potential break clause after 15 years has elapsed, thereby providing a reasonable degree of income security to the investor. Industry standard is for rent reviews (upwards only) every five years.

Funding of the Scheme

6.25 Because of the wider funding pressures being experienced by all of local government, any period of financial outlay not matched by equivalent income makes funding a scheme difficult. The returns from the scheme are sufficient to support a Prudential Borrowing case to be made, but the short term borrowing repayments would create an unfunded pressure on the revenue budget which would be undesirable in the current environment.

6.26 For this reason, together with the fact that the scheme is as much about the provision of leisure and social infrastructure associated with the expansion of Aylesbury, it is proposed that the capital cost of the scheme is funded from 2016/17 expected allocation of New Homes Bonus. Should, for any reason, (see Budget Planning 2016/17 Paper) the funding through New Homes Bonus not be available, then it is proposed that the scheme is funded instead from the available balance of the Capital Programme.

Funding via this route would ensure that there is no cost (other than opportunity costs) associated with the financing of the scheme and the entire net revenue generated by the scheme would be available to support the provision of other Council services.

Risk and risk mitigation

6.27 A risk and mitigation statement is attached as Appendix 3 highlighting what are considered to be the major risks facing the progression of this project.

6.28 A number of the risks, around viability, acceptability of the final design and consent, will be mitigated through a “Go, Don’t Go” decision point early to middle of next year. If either the Development Partner or the Council cannot reasonably be satisfied that the commercial terms or design requirements of the Council (as Planning Authority) are within the parameters laid out within this report then the decision will mutually be taken not to proceed with construction.

6.29 Within the private sector there is a general nervousness that the public sector sometimes takes decisions for political rather than commercial reasons and, therefore, they are reluctant to work, at their own financial risk, with the public sector where there is a significant risk of loss to them that could be caused through the Council’s action.

6.30 For this reason we have been advised that it is normal in such development schemes for the promoting party (the Council in this instance) to carry the financial risk to the Development Partner should the Council decide to withdraw prior to the point where the scheme goes unconditional and up to a capped maximum sum. This requirement has been explored with potential development partners and it became evident that such a requirement was necessary to ensure that any potential partners would even bid for the scheme.

6.31 The maximum contribution required by the Development Partner is £330,000 and reflects the fact that there is considerable investment on their part leading up to the “Go, Don’t Go” decision point around design and planning consent. As the Council has the option to exit for reasons over which the Development Partner has no direct control, they require this to be reflected in the potential share of abortive costs.

6.32 In the lead up to the final decision point there are various sub elements and issues that will need to be resolved satisfactorily and costs incurred will be staged and minimised in order to ensure that any financial risks under this obligation are minimised.

Overage

6.33 Although the Development Partner requires risks outside of their control to be shared they are also happy to share in upside gain. To this end they have offered two potential opportunities to share in betterment on the scheme. In the first instance, at the point of “Go, Don’t Go”, if costs or sales values have improved they are happy for these to be reflected and fixed into a, (lower only), agreed revised deficit payment from the Council upon completion.

6.34 The second opportunity is in terms of actual residential sales values, where, if values increase above a fixed level, being that which is required to make the scheme viable for the Development Partner, then they will share in the additional value 50/50 with the Council in the form of an overage payment.

Financial model

6.35 The detailed financial appraisal is set out as Appendix 1. It is contained within the confidential pages of the report as it contains assumptions around rental income which, if made public, would prejudice future negotiations with prospective tenants

7. Next steps and indicative timeline

7.1 If Council approval is given for the appointment of Developer A and the associated capital programme expenditure, the next steps and anticipated time line is:

Risk workshop and formulation of the AVDC/ Development Partner delivery team Legal agreements including Development Agreement completed	December 2015 January 2015
Formal pre-application submission	January 2016
Referred matters planning application	Spring 2016
Start on site	Autumn 2016
Completion	Spring 2017

8 Options considered

8.1 The strategic business case for AVDC's commitment to the delivery of Phase 1 of Waterside North was set out in the report to Cabinet, September 2014.

9. Resource implications

9.1 The resource implications are referred to in section 6 of the report and Appendix 1 of the confidential part of the report.

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Background Documents
Cabinet report June 2014
Phase 1 outline planning application and consent (Ref 14/01794/AOP)
Cabinet report Sept 2014
HCA DPP2 Framework documents including Sifting Brief and Invitation to tender
Aylesbury Town Centre Plan


PHASE 1

Risk and mitigation plan		**Appendix 3**
	Detailed Risk	Risk Mitigation
Certainty of Rental Income	The viability of the scheme is dependent upon generating the income predicted in the financial model. There is no advantage to the Council, or the residents of the Vale, of building the units only to find that they cannot be let.	The risk of building an unsuccessful venture can be mitigated by making the decision to move into the construction phase dependent upon achieving a number of pre-lets on the space. For the purpose of gain approval it is suggested that this should 3 of the 5 units. The leases offered to prospective tenants will tie them into the arrangement for a fixed period of time which will effectively guarantee the Council income over a set period of time. The quality of the tenant will be an important consideration when agreeing pre-lets.
Decision on the part of either party not to proceed with the development	The agreement is precedent on a number of detailed issues being resolved, a number of which are not wholly in the developers control. If the conditions can not be satisfied then the either party may chose not to proceed and abortive costs incurred will need to be shared.	The Council was unable to attract any potential bidders without committing to share in the abortive cost risk up to a capped maximum of £330,000 should the Council decide not to proceed. This risk is solely down to Council to control as it would only be invoked through decisions on its part. The risk can be minimised through control of development costs and the phasing of key decision points so that lower value risks are hedged earlier in the process.
Failure to Secure Funding for the Public Realm	The Public Realm is important to the scheme as creates a vital public space that enhances the Town centre and increases the attractiveness and viability of the commercial and residential schemes. A business case for the commercial and residential elements of the scheme cannot be made if the cost of highly specified public realm scheme is added to the total scheme cost. For this reason an application was made to SEMLEP for Government Grant funding and this has been approved. In theory all Government funding commitments are at risk as part of the Government's wider spending	The view from SEMLEP is that this funding is reasonably secure as it comes from one of the Government's earlier funding rounds and many national schemes are in progress on the back of this promised funding. Thus, it would be difficult for the Government to remove this funding. However, in the event for any reason it was withdrawn then there is sufficient unallocated funding within the Capital Programme to deliver this element of the scheme if the Council believed it to be a funding priority.

	review scheduled for late November.	
Cost Overruns	That the cost to the Council of the final Commercial space might increase as a result of ground condition, weather or other factors.	The developer commits within the agreement to a fixed maximum cost to the development, negotiated through the procurement phase. Any increase in costs will need to be managed and, ultimately, borne by the developer.
Downturn in the Housing Market affecting sales values	That a lower total income from the sale of the residential units pushes up the residual net cost to the Council for the Commercial space.	Similarly to the above risk, the developer has committed to the minimum amount of income it believes it will achieve from the residential scheme and thus takes any market risk from the prices not be achieved because of market conditions.
Financial Failure of the Developer	Meeting the developers financing costs leaves the Council at risk should the relationship or the developer fail.	The amount loaned to the developer by way of development finance through the construction period would be tied to and will not exceed more than 75% of the certified development value at that point. The will secured over the value of the development as a legal charge, so that in the event of financial failure the Council can realise its value through the asset. All necessary due diligence has been performed on the developers and their current financial standing has been assessed to be suitable in order to undertake this contract.