



SHEFFIELD CITY COUNCIL

Cabinet Report

Report of: REPORT OF THE EXECUTIVE DIRECTOR, PLACE

Report to: CABINET

Date: 21st August 2013

Subject: 3 ST PAUL'S PLACE

Author of Report: Neil Jones 273 5539

Summary:

The City Centre is the major driver of the City Region economy especially for the key growth sectors of Knowledge, Creative and Digital Industries, Higher Education, Culture and Business Services. Since 2008 office development has almost ceased and whilst there has been some fall in demand, for the first time in a decade there is no high quality Grade A office space available in the Central Business District or in any current construction pipeline, a position which brought stagnation to the City Centre office market in the 1980s and early 90s.

This report seeks authority to enter into an agreement with the developers CTP Limited whereby the Council agrees to purchase new offices to be built at 3 St Paul's Place, one year after practical completion, unless CTP elects to retain the property or to sell it to another party at a higher price. Details are set out in a report in Part 2 of this Cabinet agenda.

The intention is to find a private sector buyer, however in the current market, securing funding for speculative development is practically impossible. If the Council is able to guarantee a minimum sale price, then this will enable the development to take place, provided that CTP obtain an ERDF grant that they have applied for.

The proposed purchase price will cover just the cost of development plus a minimum return. This has been negotiated by independent surveyors on behalf of the Council who are confident that the price agreed is low enough that there is a strong likelihood that once the building is completed CTP will sell to a third party at a higher price.

Reasons for Recommendations:

Officers consider that bringing forward the development of 3 St Paul's Place in order to address the shortage of Grade A office space in the Central Business District is a priority action both in terms of the Council's Economic Strategy and the regeneration of the City Centre.

Because the property is within the boundary of the New Development Deal, then 100% of any Business Rates generated from this property can be retained by the Council. In the event that the Council does purchase the property then any Business Rates generated can be used to mitigate the cost of financing and servicing the building.

The proposed terms of the agreement with CTP seek to reduce risk and protect the Council and have the potential to deliver significant financial benefits to the Council from retained Business Rates.

Recommendations:

- That Cabinet approves the proposals to enter into the agreement to acquire 3 St Paul's Place on the terms set out in this report and the report in Part 2 of this Cabinet agenda
- That Cabinet delegate authority to the Executive Director Place in consultation with the Executive Director Resources; the Director of Capital and Major Projects and the Director of Legal and Governance to agree the terms of the transaction including the terms of any other documentation required to effect this transaction
- That the Director of Legal and Governance be authorised to complete such legal documentation as she considers necessary or appropriate in connection with this transaction on such terms as she may agree to give effect to the proposals set out in this report and generally to protect the Council's interests.
- That Cabinet approves the funding of any abortive costs that the Council incurs should the agreement not be entered into, from the Place Portfolio Revenue Budget.
- That the potential for CTP to exercise the put option for the Council to purchase the property be included within the Council's Medium Term Financial Strategy, funded by the use of the retained Business Rates generated by the building. The costs and income are factored in to the MTFS report due at Cabinet on 18th September

Background Papers: None

Category of Report: OPEN

Statutory and Council Policy Checklist

Financial Implications
YES Cleared by: Anna Peysner
Legal Implications
YES Cleared by: Gillian Duckworth
Equality of Opportunity Implications
NO
Tackling Health Inequalities Implications
NO
Human rights Implications
NO:
Environmental and Sustainability implications
NO
Economic impact
YES
Community safety implications
NO
Human resources implications
NO
Property implications
YES
Area(s) affected
City Centre
Relevant Cabinet Portfolio Leader
Leigh Bramhall
Relevant Scrutiny Committee if decision called in
Economic and Environmental Wellbeing
Is the item a matter which is reserved for approval by the City Council?
NO
Press release
YES

3 ST PAUL'S PLACE

1.0 SUMMARY, OUTCOMES AND SUSTAINABILITY

- 1.1 **Summary:** The City Centre is the major driver of the City Region economy especially for the key growth sectors of Knowledge, Creative and Digital Industries, Higher Education, Culture and Business Services. Since 2008 office development has almost ceased and whilst there has been some fall in demand, for the first time in a decade there is no high quality Grade A office space available in the Central Business District or in any current construction pipeline, a position which brought stagnation to the City Centre office market in the 80s and early 90s.
- 1.2 This report seeks authority to enter into an agreement with the developers CTP Limited whereby the Council agrees to purchase new offices to be built at 3 St Paul's Place, one year after practical completion, unless CTP elects to retain the property or to sell it to another party at a higher price. Details are set out in a report in Part 2 of this Cabinet agenda.
- 1.3 The intention is to find a private sector buyer, however in the current market, securing funding for speculative development is practically impossible. If the Council is able to guarantee a minimum sale price, then this will enable the development to take place, provided that CTP obtain an ERDF grant that they have applied for.
- 1.4 The proposed purchase price will cover just the cost of development plus a minimum return. This has been negotiated by independent surveyors on behalf of the Council who are confident that the price agreed is low enough that there is a strong likelihood that once the building is completed CTP will sell to a third party at a higher price.
- 1.5 **Outcomes:** The proposals will complete the delivery of St Paul's Place at the Heart of the City, one the key projects in the City Centre Master Plan, which was endorsed by Cabinet in January 2009 and currently being refreshed. It will also address one of the key actions identified in the Sheffield Economic Growth Strategy which was endorsed by Cabinet in April 2013.
- 1.6 The St Paul's Place project is part of the wider redevelopment of the Central Business District and will contribute to Corporate Plan priorities of 'Standing up for Sheffield'; 'Focusing on jobs' and being 'Business Friendly'. The terms of the proposed agreement, with the potential to purchase at the price proposed is in line with the Corporate Plan values of 'spending public money wisely' and 'taking a long term view'. It sits within the strategic outcome of a 'Strong and Competitive Economy'

- 1.7 **Sustainability:** The proposals will facilitate the completion of a comprehensive office led regeneration scheme in the City Centre which is the most sustainable location for such a development due to the availability of public transport and the concentration of other offices reducing the need to travel between offices and for employees.
- 1.8 It is intended that 3 St Paul's Place will achieve a BREEAM Excellent rating, will be connected to the Combined Heat and Power network and include a minimum amount of car parking and approximately 40 cycle spaces

2.0 BACKGROUND

- 2.1 The City Centre is the major driver of the City Region economy especially for the key growth sectors of Knowledge, Creative and Digital Industries, Higher Education, Culture and Business Services and the major focus for Retail, Leisure and many public services. The early 2000s saw a dramatic upturn in Sheffield's office development market and the successful establishment of three new Business Districts – Central, Riverside and Sheaf Valley. However since 2008 office development has almost ceased and whilst there has been some fall in demand, for the first time in a decade there is no high quality Grade A office space available in the Central Business District or in any current construction pipeline, a position which brought stagnation to the City Centre office market in the 1980s and early 90s.
- 2.2 A study into the City Centre Office Stock by the property consultants Knight Frank in February 2013 revealed that whilst there is a total of approximately 5.5 million square feet of office space in the City Centre only 28% of this is Grade A space. However Grade A space has accounted for approximately 50% of take up of space over the past five years as businesses wish to occupy better quality buildings. At the same time there has been a reduction in the amount of Grade B and C space as buildings have been converted into alternative uses and that is likely to continue. The study concludes that there is a requirement to bring forward further new Grade A space.
- 2.3 The Sheffield Economic Growth Strategy prepared by Creative Sheffield and endorsed by Cabinet in April 2013 provides a framework for setting out the economic priorities of the city and making the right investment decisions to deliver those objectives and establishing the right conditions in the city for long term economic success to the benefit of Sheffield residents and businesses. The Strategy includes objectives to encourage a 'Dynamic Private Sector' by attracting businesses to locate and grow in the city and to provide 'Future proof infrastructure' that delivers critical connectivity, development and sustainability to support economic growth.
- 2.4 The Strategy also reflects the issue of a shortage of Grade A office space and the need to bring forward the delivery of the Central Business District to support the expansion of knowledge and business services in the city. One of the key actions identified by 2015 is to investigate the use of new funds

such as JESSICA (explained in more detail below) to bring forward investment in Office 3 St Paul's Place, the final site in the Heart of the City project.

- 2.5 City Regeneration Division are currently in the course of preparing and consulting on a refresh of the City Centre Master Plan. This work will be completed over the summer and a report brought to Cabinet in the autumn. Unsurprisingly the draft of the Master Plan also recognises the need to address the issue of a shortage of Grade A space in the core of the City Centre and recommends that the Council provides support to achieve a start on site of Office 3 St Paul's Place in 2013/14.

3.0 CURRENT POSITION

- 3.1 St Paul's Place is the most prestigious office site in the City Centre with a superb location next to the Peace Gardens. Two phases of offices and the 'cheesegrater' multi storey car park have been built on Council land by the Council's development partner CTP Limited (CTP) under the terms of a development agreement dated 3rd June 2004. CTP also have detailed planning permission for the final building Office 3 but that development has stalled due the extremely difficult economic situation over the past five years. A revised planning application has been submitted very recently.
- 3.2 CTP together with their agents and Creative Sheffield are all confident that there is significant demand from businesses wishing to relocate within and from outside of the city for new office space and that, if built, 3 St Paul's would be ideally suited to meet this demand. However at the current time it is extremely difficult to secure traditional development finance from banks or other financial institutions to fund new commercial development. Without finance the developers cannot start building but tenants will not commit to taking space without a clear date that the offices will be available. Officers have therefore been working closely with CTP to try to find ways to break this deadlock through trying to secure alternative sources of funding.
- 3.3 The current programme for ERDF is coming to an end and the Department of Communities and Local Government (DCLG) is in the process of allocating the remaining funding towards projects that can deliver against the agreed priorities by the end of 2015. CTP have been in discussions with DCLG for some time and have an in principle approval to provide ERDF towards the 3 St Paul's Place subject to detailed appraisal which is currently being carried out. If the funding is approved the development will need to start on site before the end of this year in order to meet the timescales for drawing down ERDF before the current programme ends.
- 3.4 Members will be aware of the establishment by the Local Enterprise Partnership of a £20m South Yorkshire Development Fund (SYDF) using a European funded initiative known as JESSICA (Joint European Support for Sustainable Investment in City Areas) which was approved by Cabinet in April 2012. The Fund Manager who has since been appointed to invest the SYDF is currently actively exploring potential suitable schemes to invest in.

CTP have been in discussion with the Fund Manager and terms have been agreed in principle for the SYDF to invest in the project.

- 3.5 Subject to the necessary final approvals and the whole of the wider package of funding being secured it is anticipated that the above sources of finance will fund approximately half of the total costs of carrying out the development. CTP will need to raise additional private finance for the remainder. In current economic conditions it is very difficult to secure development finance without having a clear way of repaying the finance once the development has been built. A possible solution to this has been negotiated as set out below.

4.0 TERMS PROPOSED

- 4.1 Terms have been agreed, subject to Cabinet approval, whereby the Council agrees to purchase the 3 St Paul's Place offices one year after practical completion of the building at a price set out in the report in Part 2 of this Cabinet agenda. This is likely to be summer 2016.
- 4.2 However the proposed agreement will also provide that if CTP can sell the property to another party at a higher price then they may do so, in which case the Council will not acquire it. This is the desired outcome and the purchase by the Council will only occur in the event that CTP have very limited success in letting the completed building or that the commercial property investment market will not support a price which covers the cost of development plus a minimum developer's return. Without the fallback position of an option to sell to the Council CTP will not develop the building.
- 4.3 The agreed terms will include a guaranteed maximum price. CTP will be responsible for managing the delivery of the completed building and will take all cost risk on the project. They will also be under obligations to try to secure cost savings and lettings of the offices and will be incentivised to do this through the terms of the agreement.
- 4.4 The proposed purchase price has been negotiated by independent surveyors DTZ on behalf of the Council based on the cost of development and a minimum return to the developer. DTZ are confident that the price agreed is low enough that there is a strong likelihood that once the building is completed CTP will sell to a third party at a higher price. DTZ have previously been involved in the acquisition of Offices 1 and 2 at St Paul's Place and the prices achieved for those buildings were far in excess of the price proposed for Office 3. Whilst those sales took place in a different market from at present the St Paul's Place development is, and for the foreseeable future will remain, the most prestigious office location in the city.

5.0 FINANCIAL IMPLICATIONS

- 5.1 The financial details and implications of the proposed agreement are set out in the Part 2 report. The key financial questions are how would the Council raise the funding necessary to purchase the property in the event that CTP

do not retain or sell it to a third party and then fund the on-going servicing of the debt and the building management until such time as a purchaser should be found.

5.2 Members will be aware that Central Government has approved a scheme known as the New Development Deal whereby the Council has been granted powers to retain 100% of any uplift in Business Rates that the Council receives within a specified boundary as a result of investing in new City Centre infrastructure. The site of 3 St Paul's Place is within the specified area and therefore the Council can retain the full amount of Business Rates from the completed building until 2038. Financial modelling has been carried out by Finance to establish the costs associated with ownership of the building and likely income at various levels of occupation and rental value. The details of the analysis is set out in the Part 2 report but the key point is that providing the building is occupied at a sufficient level (around 70% – 80%) then the income from the Business Rates together with projected rental income from the tenants of the building would be sufficient to cover the debt charges and servicing costs that would arise from the Council purchasing the property should that be necessary.

5.3 In a worst case scenario, should the building be completely empty while in the ownership of the Council, then the annual finance and running cost would be around £1.5m per annum. This is considered to be extremely unlikely.

5.4 The retention of 100% of Business Rates authorised by the New Development Deal will apply to this development whether or not the Council actually acquires the property. Therefore if the Council is able to facilitate the delivery of the development through the proposals set out in this report but does not eventually purchase it then the additional annual income to the Council would be up to £660k per annum depending on occupancy levels for the duration of the NDD period.

6.0 LEGAL IMPLICATIONS

6.1 The Council has the power to acquire land and buildings under section 120 Local Government Act 1972. In addition, the Localism Act 2011 introduced a general power of competence that allows Local Authorities to do anything that an individual can do subject to a limitation existing elsewhere in legislation

6.2 External legal advice has been obtained in respect of the proposed transaction and this has confirmed that the proposals are compliant with public procurement regulations and state aid principles and external property advice has confirmed that the proposals satisfy the statutory requirements of Best Consideration under section 123 Local Government Act 1972

6.3 The Non-Domestic Rating (Designated Areas) Regulations 2013 came into force on 18 February 2013 designating areas within Sheffield and other parts of England as areas where a proportion of non-domestic rates collected could be retained by the billing authority. If future lending was required against

anticipated receipts from this future income, the proposal would have to be signed off in accordance with any governance arrangements that the authority may have in place at such time.

7.0 ENVIRONMENTAL IMPLICATIONS

7.1 There are no direct environmental implications arising from the proposed acquisition. However the proposals will facilitate the completion of a comprehensive office led regeneration scheme in the City Centre which is the most sustainable location for such a development due to the availability of public transport and the concentration of other offices reducing the need to travel between offices and for employees.

7.2 It is intended that 3 St Paul's Place will achieve a BREEAM Excellent rating, will be connected to the Combined Heat and Power network and include a minimum amount of car parking and approximately 40 cycle spaces

8.0 EQUALITY IMPACT ASSESSMENT

8.1 There are no equalities implications arising directly from the proposals in this report, an Equality Impact Assessment is therefore not considered to be necessary at this stage.

9.0 HUMAN RIGHTS IMPLICATIONS

9.1 There are no Human Rights implications arising from this report.

10 ALTERNATIVE OPTIONS CONSIDERED

10.1 The provision of new Grade A office space in the City Centre is a key action identified in several current studies and strategies in order to drive an improvement of the economy of the city and wider City Region. The Council could simply do nothing and wait to see whether market forces will deliver this in isolation. It is considered that in the current economic climate this may not happen for several years. If the development does not take place for some time then the financial benefits referred to in section 5 of this report will not arise.

10.2 Officers have considered other initiatives to seek to facilitate the development such as the Council taking a lease of parts of the building or providing development finance instead of the private sector funding proposed but having considered those options it is believed that the proposed agreement is the most appropriate in terms of seeking to reduce potential risk and total cost for the Council and deferring the time when it may be necessary to borrow in order to complete the purchase. It is also hoped that there is a reasonable prospect that through the route proposed the Council may not actually need to purchase the property in which case the costs will not be incurred.

11.0 REASONS FOR RECOMMENDATIONS

- 11.1 Officers consider that bringing forward the development of 3 St Paul's Place in order to address the shortage of Grade A office space in the Central Business District is a priority action both in terms of the Council's Economic Strategy and the regeneration of the City Centre.
- 11.2 Because the property is within the boundary of the New Development Deal, then 100% of any Business Rates generated from this property can be retained by the Council. In the event that the Council does purchase the property then any Business Rates generated can be used to mitigate the cost of financing and servicing the building.
- 11.3 The proposed terms of the agreement with CTP seek to reduce risk and protect the Council and have the potential to deliver significant financial benefits to the Council from retained Business Rates.

12.0 RECOMMENDATIONS

- 12.1 That Cabinet approves the proposals to enter into the agreement to acquire 3 St Paul's Place on the terms set out in this report and the report in Part 2 of this Cabinet agenda
- 12.2 That Cabinet delegate authority to the Executive Director Place in consultation with the Executive Director Resources; the Director of Capital and Major Projects and the Director of Legal and Governance to agree the terms of the transaction including the terms of any other documentation required to effect this transaction
- 12.3 That the Director of Legal and Governance be authorised to complete such legal documentation as she considers necessary or appropriate in connection with this transaction on such terms as she may agree to give effect to the proposals set out in this report and generally to protect the Council's interests.
- 12.4 That Cabinet approves the funding of any abortive costs that the Council incurs should the agreement not be entered into, from the Place Portfolio Revenue Budget.
- 12.5 That the potential for CTP to exercise the put option for the Council to purchase the property be included within the Council's Medium Term Financial Strategy, funded by the use of the retained Business Rates generated by the building. The costs and income are factored in to the MTFS report due at Cabinet on 18th September

Simon Green
Executive Director Place