

**REPORT OF: CENTRAL AND REGENERATION SERVICES
HEAD OF CENTRAL AND REGENERATION SERVICES**

TO: THE EXECUTIVE

DATES: 19th MARCH 2015

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THE ACE CENTRE, NELSON

PURPOSE OF REPORT

1. The purpose of this report is to seek the approval for the Council to enter into a lease for the ACE Business Centre.

RECOMMENDATIONS

2. The Executive is recommended to give approval for the Council to enter into a lease with PEARL for the ACE Business Centre subject to PEARL agreeing to back-to-back sub-lease of the ACE Business Centre from the Council.

REASONS FOR RECOMMENDATION

3. To seek agreement to a lease for the ACE Business Centre.

ISSUE

Background

4. The Arts, Cultural and Enterprise (ACE) Centre was built in 2009 by the Council's Joint Venture Company, Pendle Enterprise and Regeneration Ltd (PEARL). The construction of the building was funded partly from grant (Single Regeneration Budget (SRB) and Local Enterprise Growth Initiative (LEGI)), private investment from Barnfield Investment Properties with the balance of funding being a commercial loan.

5. The building comprises four floors (c44,000 sq ft) of accommodation as follows:-

Ground Floor/First Floor

- a dedicated reception area
- a 200 retractable seat performance theatre with a control room which is used for cinema/theatre and live performances;
- two functions rooms capable of seating up to 300 people
- two meeting rooms;
- a multi-purpose room with a dance/aerobics studio
- a state of the art recording studio
- a Bistro with kitchens supporting both the bistro and functions rooms on the first floor

Second/Third Floor (known as the ACE Business Centre)

- a dedicated reception area (although this is currently not used)
- 34 individually managed office suites ranging in sizes from 350sq ft to 1,500sq ft

6. The office space is considered to be of high quality with good specification and finishes. Tenants have access to broadband connectivity both for telephony and computing.
7. The ground/first floor (gf/ff) are currently let to the Council under a 25-year lease which expires on 22nd May 2034. The rent passing for the lease is currently £193k pa. The Council has, with the permission of PEARL, subsequently let the gf/ff to the Pendle Leisure Trust on a peppercorn lease and it is now operated as a leisure facility.
8. The second/third floor ACE Business Centre was originally let to Hamill Investments, again on a 25 year lease, with the intention of providing managed office accommodation. However, the opening of the ACE Business Centre coincided with the fall-out of the recession that started in 2008 and the contraction in the local economy had a significant impact on the demand for office space. As a consequence, Hamills experienced some difficulty in securing lettings and, despite an initial rent-free period, in February 2011 it was agreed with PEARL that they would surrender their lease for the Centre.
9. Since that time, PEARL has managed the Centre directly in conjunction with the Pendle Leisure Trust. However, the prevailing market conditions have not improved and demand for office space remains low. Current occupancy is c18% and has remained broadly unchanged for the last 3 years. There appears to be little prospect of this changing in the near future without a change in the configuration of the office space. Aside from the depressed market for office space, the size of the individual offices and the lack of car parking in the near vicinity of the Centre are cited by prospective Tenants as the main reasons for not converting viewings into firm lettings.

Current Position

10. There are three key issues that the Company is currently considering.
11. Firstly, a fundamental issue for PEARL is the need to service the outstanding commercial debt on the ACE Centre. This comprises both interest (which is variable to LIBOR and amounts to c£95k pa) and principal repayments (which are fixed at £236k pa). The current loan is from Handelsbanken and is due for repayment in full in July 2016. In all likelihood, this facility will be refinanced but the current financial performance of the ACE Centre may have a bearing on the terms on which that may be achieved and the cost of debt may increase or the Bank may reduce the value of the facility. In view of this, consideration has been given to ways in which sufficient funding can be raised to repay the debt in full without the need for refinancing.

12. Secondly, as indicated above, from enquiries received for the ACE Business Centre Offices, it is clear that the demand is for smaller office units (between 250sq ft and 400sq ft). Reconfiguring the ACE Business Centre to create offices of this size would require substantial alterations not least to ensure that the newly created offices were properly serviced (heating, lighting, IT connectivity etc). An initial estimate of the works to provide c70 offices (as opposed to the 34 at present) is c£300,000. PEARL does not currently have sufficient funds for this investment.
13. And finally, PEARL's ability to undertake further investment in both the ACE Centre, the Colne Arcade Shopping Centre and, indeed, any further projects is inhibited by a lack of investment funds. Other than obtaining bank funding, which is largely dependent on commercially viable projects that add strength to the Company's capital position, funding must generally be provided by both the Council and Barnfield. Alternatively, there may be scope to divest in the Company's assets.

Proposal

14. As a means of generating funds to both repay the debt and for additional investment, PEARL has approached the Council with a view to offering a lease for the ACE Business Centre. The lease would be for 10 years at a rental value of £174,500 (or 8.45 per sq ft for 20,651 sq ft). Acknowledging that the rent would be an additional cost to the Council, PEARL has indicated that it would take a sub-let of the Business Centre thereby reimbursing the Council from within its own funds for the full value of the rent leaving no additional cost to the Council. PEARL's obligation to pay rent would, in turn, be underwritten by a Parent Company Guarantee from Barnfield who would ultimately bear the risk for meeting the rent obligation.
15. In essence, the proposal is to exploit the Council's covenant strength to obtain the maximum sale value for the building. On the terms proposed, fully let the ACE Centre would produce an annual rent of £367,710. To realise the capital value of this rental stream, the proposal is to dispose of the ACE Centre and, subject to the final value achieved, use the proceeds of the sale as follows:-
 - a) repayment of the Handelsbanken debt in full – the current outstanding debt is c£3.2m; This will mean that PEARL is debt-free with no ongoing interest costs which have served to erode the Company's ability to generate profit;
 - b) invest in the reconfiguration of the ACE Business Centre into smaller offices. As indicated above, the intention is to create office units more suited to local demand but sufficiently flexible to allow scaling-up if necessary;
 - c) invest in improvement work to the façade of the Colne Arcade Shopping Centre;
 - d) invest the balance of any funds in new projects such as the redevelopment of the old Colne Health Centre which, if it acquired by the Council and subject to an agreement to transfer the site to PEARL, would be included in the pipeline of projects for the Company.
16. In conclusion, the Council's lease of the ACE Business Centre should provide sufficient covenant strength to ensure that the disposal of the ACE Centre is an attractive long term investment for investors. In turn, this should generate sufficient funding to put PEARL on a sound financial footing and provide investment funds for current and future projects.

IMPLICATIONS

Policy

17. There are no new policy implications arising directly from the contents of this report.

Financial

18. The financial implications are as given in the report.

Legal

19. As indicated in the report, it is proposed to take a lease of the ACE Business Centre, the terms of which will be mirror in a sub-lease to PEARL.

Risk Management

20. The key risk to the Council is meeting the rent obligation arising from the lease. In this respect, it is proposed that a back-to-back sub-lease is made to PEARL for the Business Centre and that a Parent Company Guarantee is obtained from Barnfield who ultimately will underwrite the rent payments.

Health and Safety:

21. There are no Health and Safety implications arising directly from the contents of this report.

Sustainability:

22. As with health and safety implications, there are no sustainability implications arising directly from this report.

Community Safety:

23. There are no community safety issues arising directly from the contents of this report.

Equality and Diversity:

24. There are no equality and diversity implications arising from the contents of this report.

APPENDICES

None