Borough of Pendle

REPORT OF:	**CHIEF FINANCIAL OFFICER**
TO:	**POLICY AND RESOURCES COMMITTEE**
DATE:	**26TH JUNE 2018**

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DISPOSAL OF PROPERTY INTERESTS

PURPOSE OF REPORT

1. The report considers the scope to dispose of the Council's interests in the following operational buildings:

   - Number One Market Street, Nelson
   - The ACE Centre, Nelson (first and second floors)
   - Elliott House, Nelson

   The report is provided in response to a policy objective of the new political administration. The objective is to dispose of the above buildings on the open market and apply the sale proceeds to reduce the Council's external debt.

RECOMMENDATIONS

2. The Committee is asked to consider the content of this report and approve the following recommendations:

   (a) That the Council's leasehold interest in the ACE Centre, Nelson not be disposed at the present time pending a resolution of matters linked to the current occupation of the building by Pendle Leisure Limited;

   (b) That further detailed work be undertaken to determine the viability of disposing of the Council's interests in Number One Market Street and Elliott House, Nelson;

   (c) Subject to (b) above, that a further report be submitted to the Committee in due course on these matters.

REASONS FOR RECOMMENDATION

3. To progress matters linked to the potential disposal of certain property interests held by the Council.

ISSUE

Background

4. During late 2016 the Council's Executive approved the acquisition of Number One Market Street, Nelson and parts of the Ace Centre, Nelson. The former was linked to a contract extension with Liberata which, amongst other matters, enabled the Council to benefit from an ongoing reduction in the unitary charge payment it made to Liberata. The intention when purchasing parts of the ACE Centre was also to generate revenue savings as a result of buying out a lease the Council was committed to until 2034, funding this with low cost borrowing from the Public Works Loan Board.

5. The above actions were formally approved by full Council and the property acquisitions were subsequently completed in April 2017 (ACE Centre) and May 2017 (Number 1 Market St). The background and context against which these decisions were taken is not repeated here as this was covered fully at the time the matters were reported to the Executive and Council. These reports are publicly available on the Council's website at www.pendle.gov.uk.

6. Grant Thornton, as the appointed auditor to the Council, also reviewed the Council's decision-making as part of their value for money assessment during their audit of the Council's accounts for 2016/17. They concluded as follows in their ISA260 report to the Accounts and Audit Committee in July 2017:

   "We are satisfied that appropriate arrangements were in place to ensure proper arrangements were in place to facilitate inform(ed) decision-making for the two decisions referred to above".

7. Following a change in the political control of the Council after the elections in May 2018, the new Administration announced a number of policy objectives. One of these is to sell the Council's interests in Number One Market Street and the ACE Centre. In addition they have also requested consideration be given to disposing of Elliott House, Nelson. The overarching aim being to apply the sale proceeds from these disposals to reduce the Council's external debt. The remainder of this report outlines the considerations involved in achieving this objective.

The Council's current debt position

8. At the time of writing this report the Council had long-term debt of £18.4m comprised wholly of loans from the Public Works Loan Board at an 'average' interest rate of 3.16%. There are 16 loans with the earliest and latest repayment dates being 31/3/2020 and 31/3/2065 respectively. All loans are maturity loans meaning that repayment is made on the maturity date with only interest paid each year prior to this.

9. Under arrangements instigated by HM Treasury the premature repayment of loans can result in either discounts or premiums (i.e. penalty). Discounts arise when the interest rate on the loan being repaid is lower than current loan rate for the equivalent period and vice versa for premiums. However, premature repayment rates are subject to an additional margin by the PWLB which adversely affects the scope of, and benefits from, the early repayment of debt.

10. In late May an analysis of our premium/discount position was requested from our treasury management advisers Link Asset Services. This identified a net *premium* position of £1.7m with premiums attached to 12 of our loans (£1.9m) with the remaining four attracting discounts (£0.2m). The four loans attracting a discount include three loans taken out in May 2017 to fund the purchase of Number One Market Street. More information on these follows below.

Number 1 Market Street, Nelson

11. The Council purchased this building from Barnfield Investment Properties for a price of £3.3m excluding stamp duty. The purchase was completed on the 3rd May 2017 and the property was subject to a number of leases, the most significant of these being with Liberata. The Council obtained independent valuations before completing the purchase.

12. The purchase was funded by drawing down three loans, each of £1m, from the Public Works Loan Board at interest rates of 2.34%, 2.35% and 2.36% for maturity periods of 43,44 and 48 years respectively. The balance of the full purchase cost (including stamp duty) was funded from *prudential borrowing*. Prudential borrowing is the use of the Council's own reserves, provisions and balances to fund capital expenditure which has not been funded from other capital cash sources (e.g. grants, capital receipts, leasing, S106).

13. If the Council wishes to dispose of its interest in this building it would be necessary to secure independent valuation advice and appoint commercial property agents to oversee the disposal on its behalf. The 'value' in the asset will be determined by reference to the existing leases, the most significant of which is that between the Council and Liberata. Under this lease the current rent is subject to a reduction in 2020 at which time the Council benefits from a further saving on the unitary charge payment it makes to Libarata. Current leases for the three retail units on the ground floor generate additional rental income but two of these expire in March 2019 with the remaining one expected to end in March 2020 when a break clause can be activated.

14. Hence, if the intention to sell is confirmed in due course and the property is marketed, a sale is unlikely to be completed until some time in 2019 or possibly even 2020 subject to market conditions. In this scenario, the 'value' of the building would most likely be determined by reference to the residual lease with Liberata from 2020 to 2030 combined with whatever arrangements are in place at the time in respect of the retail units. Subject to independent valuation advice this *could* yield a sale price in the range of £2.5m - £3.0m. If these values are confirmed it is less than the Council paid to acquire the building reflecting the passage of time and potential changes in the leases associated with the building.

15. There are other considerations linked to the use and potential disposal of the building. These include:

    - Liberata do not use all parts of the building currently;
    - Pendle Leisure Trust occupy the top floor on a peppercorn rent as a consequence of their move from Colne Town Hall – what happens to them;
    - The Council uses part of the ground floor (housing needs / planning);
    - The scope to use under utilised parts of the building for council staff;
    - The extent of control / influence the Council retains if the building is sold and loss of rent income stream;
    - Market conditions and supply/demand for office accommodation in Nelson.

The ACE Centre, Nelson

16. The Council acquired a leasehold interest in the ground and first floor of the ACE Centre in April 2017 for which it paid £2.2m (excluding stamp duty) to PEARL. The intention was to fund this purchase by borrowing from the PWLB but to-date no loans have been drawn down for this purpose. The Council has in effect funded this from its own resources thus far by way of prudential borrowing as referred to in paragraph 12 above. However, the Council still retains an underlying need to borrow for this purpose but has yet to do so.

17. The purchase enabled the Council to make revenue savings, in effect, by converting annual lease payments in to lower cost borrowing. The Council sub-leases the ground and first floors to Pendle Leisure Limited at a peppercorn rent.

18. As a result of this sub-lease arrangement there is no rent passing in respect of the Council's interest in the building. As the tenant pays no rent there is no prospect of there being commercial interest should the Council seek to dispose of its interest in the building. Whilst the Council is no longer paying lease rentals to which it was committed until 2034 there is no commercial value in the property given the current arrangement.

19. The Council would need to determine its ongoing relationship with the Leisure Trust and what it proposes for their current use of the building before deciding what action to take with regard to its own interest in the building. Subject to the outcome of these considerations it may be possible to let those parts of the building 'owned' by the Council to a rent paying tenant and thereby generate a potential sales value should the Council continue with the objective of selling its interest in the building.

20. Until these matters are resolved it is recommended that the Council defers any decision on the disposal of its interest in the ACE Centre.

Elliott House, Nelson

21. This building is currently used to provide accommodation for a number of council staff, primarily within Neighbourhood Services and Housing, Health and Economic Development. Given the reduction in staffing over recent years there may be the potential to relocate staff from this building to the Town Hall and / or Number 1 Market Street (subject to considerations outlined above in this report). Indeed, this is a project that is currently being considered irrespective of the proposals in this report.

22. If this is feasible it would provide an opportunity to dispose of the building. This would yield a capital receipt for the Council and release it from the ongoing liability for maintaining the building. No discussions have taken place as to potential future uses of the building. There is a surplus of office accommodation in Nelson and yields are generally considered low. There may be little interest in the building for office purposes but this cannot be fully established without testing the market and engaging with property advisers. It would be necessary to obtain a formal valuation of the building.

Next steps?

23. The Committee is asked to consider the content of this report and advise of its intentions in respect of the three buildings outlined above. Subject to this it will be necessary to commission further advice including property and valuation advice to help make informed decisions on those properties the Committee feels should be sold by the Council. Subject to the recommendations agreed in response to this report, further work will be undertaken by officers on these matters and reported to the Committee in due course.

IMPLICATIONS

Policy

24. The disposal of these recently acquired buildings (ACE Centre and Number 1 Market Street) would represent a change of policy and require the approval of Council.

Financial

25. At this time the assumption is that the ACE Centre is not disposed of by the Council for reasons outlined above but Number 1 Market Street and Elliott House are with completion taking place on or after 1/4/20. In this scenario the financial implications are potentially significant and arise from the following factors.

- Premature repayment of PWLB loan debt, saving on interest payments;
- Reduced level of MRP (minimum revenue provision – being the statutory charge against council tax for the principal repayment of debt);
- The capitalised value of the leases associated with Number 1 Market St including any revisions to those for the ground floor retail units on expiry of the current leases;
- The market value of Elliott House subject to current and any proposed change of use;
- The level of discount or premium on the PWLB loans to be repaid as at the precise date of premature repayment;
- Savings on the direct running costs of Elliott House;
- Any reduction in the unitary charge payable to Liberata for the management of the Council's property interests once the buildings are disposed of;
- Prevailing market conditions at the time of marketing and in the course of disposal;
- Savings arising from reduced maintenance liabilities;
- The loss of rent income to the Council, notably from Liberata.

26. There are commercial considerations to take in to account as part of this work. The Council will need to present a viable proposition to the market but in order to benefit from effective competition it is important not to disclose too much 'commercially sensitive' information in advance. Hence whilst there is more detailed information available on the above factors it is not presented in full at this time. Clearly, the market valuations (i.e. capital receipt) for each building considered for disposal together with the discount or premium arising on early repayment of PWLB loans will be the main determinants of the financial benefit to the Council. At this time an *indicative* net annual saving arising from the factors outlined in paragraph 25 above is £20k to £25k.

27. Much more detailed work is required to firm up this positon and to test the reasonableness of the underlying assumptions. Fundamentally, it will also be necessary to secure expert advice in relation to the marketing and valuation of the properties. There is no approved budget provision for the engagement of external advisers should the Committee wish to explore the disposals of these buildings more fully. It would be necessary to allocate resources to this and estimates can be obtained in due course should the Committee support this.

Legal

28. There are no legal implications arising directly from this report. Subject to further consideration on these matters the potential disposals will require support from Legal Services in due course.

Risk Management

29. Disposals of the nature outlined in this report are not without risk. This stems mainly from financial and market risk. To help mitigate this risk it will be necessary to procure external advice.

Health and Safety

30. There are no health and safety implications arising directly from the contents of this report.

Climate Change

31. There are no climate change or sustainability implications arising directly from this report.

Community Safety

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

Equality and Diversity

33. There are no equality and diversity impacts arising from this report.

APPENDICES

None.

LIST OF BACKGROUND PAPERS