

CABINET

Luneside East Regeneration Project 17 March 2009

Report of Corporate Director (Regeneration)

PURPOSE OF REPORT			
To update Cabinet on progress on this key regeneration project, explain why this development is currently stalled and to present proposals for how the Council might facilitate a satisfactory and timely project delivery.			
Key Decision	<input checked="" type="checkbox"/>	Non-Key Decision	Referral from Cabinet Member
Date Included in Forward Plan	June 2008		
This report is public			

RECOMMENDATIONS OF COUNCILLOR MACE

That Cabinet:

- (1) Approve that, if the NorthWest Development Agency provide the Council with full grant funding for the purpose, the Council undertake all works necessary to clear and remediate (clean up) the site and put in place essential infrastructure in order to facilitate the subsequent development of the site by the private sector, subject to the Corporate Director (Regeneration) and the statutory officers being satisfied as to any conditions imposed by the NWDA.
- (2) Subject to Recommendation 1 being approved and the outcome of the funding bid, that the General Fund Capital programme and the General Fund Revenue Programme are updated accordingly.

1.0 Introduction

- 1.1 This is a complex and challenging regeneration project to redevelop the whole 7-hectare Luneside East site as a mixed-use new neighbourhood. The project concept is for a two-stage delivery with a public sector land assembly to be followed, after a land transfer, by the private sector development.
- 1.2 The Council completed the first stage early last year. Work on this involved a major compulsory purchase order and contracting with National Grid plc to decommission and remove the operational gasholder. The Council secured some £12 million in

external public funding for this from English Partnerships (EP) and the NorthWest Development Agency (NWDA) via a Joint Funding Agreement of September 2004 (the JFA) and also from the European Regional Development Fund (ERDF).

- 1.3 To facilitate the second stage the Council contracted with developer CTP Ltd / Development Securities plc (the Developer) via a Building Agreement of 2 November 2005 (BA). Under this, once both the Council and the Developer have met certain obligations the Council is to transfer the site and all risk and responsibility for project delivery to the Developer.
- 1.4 Planning requirements in combination with obligations on the Council under the JFA govern what the Developer is to deliver. Planning requirements are set out in the Council's Supplementary Planning Guidance Note 4, (SPG 4) 2004 and focus the need for comprehensive redevelopment, high quality urban design, public spaces that will be well used and routes that give good connections for pedestrians and cyclists. The JFA requires a minimum 8,000 sq metres of business space and 350 housing units. In summary, the Developer must clear and remediate (clean up) the whole site, put in infrastructure, construct the commercial phases and achieve the residential elements via contracting with housing developers.
- 1.5 The Developer has undertaken a substantial amount of preparatory work and was ready to proceed in the spring of 2008. This work is summarised in Appendix 1. Unfortunately, however, changed market conditions associated with the "credit crunch" and a collapse of confidence among house builders' means that the Developer simply cannot proceed in the way provided for under the BA. This report sets out how the Council might respond.

2.0 Proposal Details

- 2.1 A detailed review and draft options analysis carried out by officers in Spring 2008 suggested very clearly that the best prospects for project delivery and for mitigating all risks to the Council involved continuing to work with the Developer. Over the months since then officers have explored the options on this basis for taking the project forward. (The consultation involved in this is summarised in section 3 of this report). Unfortunately, as everyone is aware, the market situation continued to worsen.
- 2.2 Development values have fallen substantially as also have yields and these affect capital values. Confidence is at an all time low and the availability of bank finance for developments, never mind relatively high-risk developments, has all but dried up. Almost all house builders have fled the market.
- 2.3 All parties have now become seriously concerned that if and when the market begins to recover house builders will be very cautious and have appetite only for low risk "easy" to develop sites – for example those in green field locations. This could very well mean that the site in its current condition will remain unattractive to house builders for very many years to come. This would have grave consequences for regeneration across the western part of the City as a whole. This is because the site is at the gateway to Luneside and its condition shapes the perceptions of potential investors into the area.
- 2.4 The Developer reviewed its development proposals to see if it could better position the development opportunity. This led it to revise its master plan to provide for less housing but a better balance with fewer flats and more family houses. The Homes

and Communities Agency (HCA), formerly EP, has indicated that, in principle, this should prove acceptable and in due course the JFA can be varied accordingly.

- 2.5 Notwithstanding this, the Developer considers that the only way to significantly increase the prospect that Luneside East development can be delivered in a timely manner is to advance the site for development by clearing and remediating it. Council officers endorse this view, as, in principle, do officers of the HCA and NWDA.
- 2.6 In order to take this forward, the Corporate Director (Regeneration), after verbal discussions with the NWDA, has proposed to the NWDA that it make additional funding available for the Council to clear, remediate (clean up) and undertake essential infrastructure works in order to facilitate the subsequent development of the site by the private sector. The proposal involves the Council being accountable body for expenditures and responsible for all aspects of the works required including procurement and contract management. As part of the proposal, the Council would require the Developer to commit to funding and delivering a first phase of development just as soon as the Council completed its works. This first phase would include the main elements of public realm required for the development as a whole plus some 4,000 sq m of business space.

3.0 Details of Consultation

Officers have liaised extensively with the Developer and the NWDA and the HCA. In addition, officers have liaised with the Government Office for the NorthWest (GONW), which is responsible for European funding interests. Officers have also taken advice from the Council's appointed valuers for this project - Keppie Massie.

4.0 Options and Options Analysis (including risk assessment)

Options

- 4.1 Market conditions severely constrain what can reasonably be done. To make progress the only option available is

Option 1 is for the NWDA to grant the Council funding for it to clear and remediate the site and undertake essential infrastructure works and thereby ready the site for development when the market starts to recover. (The Developer costs such works at some £5.2 million).

- 4.2 The alternative, **option 2**, is to do nothing.

Analysis

- 4.3 Officers consider that option 1 is the only one available. Doing nothing is not realistic, not least because obligations on the Council under the JFA and its contract for ERDF funding put it at substantial financial risk until it delivers or at least can assure full development delivery. In total, funding for some £5 million of expenditures already made is at stake and, in the worst-case scenario, the Council would be left with expenditure to this amount unfunded.
- 4.4 In addition, doing nothing would have serious implications for regeneration and planning. The full potentials of this development in terms of the environmental improvements, homes and jobs that it should deliver will not be realised. There will be no significant inward investment into the wider Luneside area for years to come.

Failure to develop out this site and, because of this, prospectively other sites, will also mean the Council's total housing delivery is lowered and developers will be in a stronger position to force the Council to release Greenfield sites instead.

- 4.5 A related point is that terminating the involvement of the Developer is neither sensible nor reasonable at this stage. The developer has undoubted capacity, knowledge, commitment and readiness to deliver and the Council can mitigate its risks significantly by keeping the Developer with it so it can draw on its knowledge and experience. Further, the reasons the Developer cannot proceed as planned are no fault of its own.
- 4.6 Option 1 is also deliverable (subject to a positive funding decision). The NWDA (and also the HCA) has the discretion to grant the Council sufficient funding to undertake the works described and a variation to the JFA would be the mechanism. The Corporate Director (Regeneration) has the delegated authority to apply for such external funding. The Council owns the whole site and therefore would have full site control. It is practised as an accountable body. Planning Services' Engineering Team has the capacity and expertise to act as client for the works. This team is well versed in mechanisms for managing and mitigating risk (including cost risk) in contract management. To maximise efficiencies and minimise costs the Council should secure services from the Developer's expert consultancy team to assist with the client role, most particularly from Entec UK Ltd as consultant advisors for the remediation works and RW Gregory for servicing and utility works. The Developer has consented to this. The necessary procurements could be made under the Council's procurement rules.
- 4.7 Critically, the Council would need to procure an expert remediation contractor. The Council could draw from the applicable NWDA Panel of pre-validated contractors and, after clarifying capabilities, tender. The Council should also take advice from Entec's given it tendered the remediation contract on behalf of the Developer. The Council's Engineering Team consider that the procurement process will take some 6-9 months to complete with a 2-3 month mobilisation period after this before the contractor could commence. Entec, for the Developer, has planned on a nine-month period for site works.
- 4.8 If it is assumed that that tenders for a remediation contract are advertised in late Spring 2009 then prospectively, the site works should commence in early 2010 and be completed by autumn 2010. Given that most commentators predict economic recovery to commence in 2010 this should time well with any market recovery and the need then to present the site as a compelling development opportunity.

Risk assessment

- 4.9 Option 1 relies on the Council securing external funding to cover the costs of it undertaking site works and any grant secured would be capped. This would place the onus on the Council to manage costs and cost risks within the budget made available. Given the recession, the Council should be very well placed to secure very competitive tenders and to further mitigate out cost risk by drawing on the experience gained by Entec in its procurement for the Developer.
- 4.10 There are other risks including regulatory, technical and environmental risks but proper project management approaches and effective contract management should mitigate these to a satisfactory level. Again, the experience of Entec and also RW Gregory will assist. In addition, the continued involvement of the Developer itself in an advisory capacity would assist with risk management during site clearance and

remediation works and enable the Council to tailor remediation standards and infrastructure provision very precisely to the first phase construction by the Developer. The Council could accommodate for this in its project management approach.

5.0 Officer Preferred Option (and comments)

5.1 Option 1 is strongly preferred. A specific short-term gain is that undertaking site works bring local benefits in terms of jobs and economic activity. Resolving the problems of land contamination will remove the main constraint on development of the site. This will transform the development opportunity in the perceptions of potential investors and house builders and should significantly advance final project delivery. There are no other practicable options. To take forward this option it is recommended that Cabinet -

- (1) Approve that, subject to the NorthWest Development Agency providing the Council with full grant funding for the purpose, the Council undertake all works necessary to clear and remediate (clean up) the site and put in place essential infrastructure in order to facilitate the subsequent development of the site by the private sector.
- (2) Approve that £20,000 be made available from the Capital Support Reserve to fund the costs of Planning Services' Engineering Team in 2009/10 in preparing for and delivering the contract works.

6.0 Conclusion

6.1 The Council has very successfully completed the first delivery stage for this complex and challenging urban regeneration project. The planned second private sector stage is presently stalled because of the exceptional market conditions arising out of the credit crunch and the now deep economic recession. In the circumstances all parties see real merit in the public sector taking the project another step forward and funding site clearance and remediation works in order that, on completion of these, the site can present better to the market. It is very possible that such works can be completed to time with an economic recovery and in this event the site should attract substantial developer interest and full project delivery and the long planned mixed use new neighbourhood should be achieved.

RELATIONSHIP TO POLICY FRAMEWORK

The Luneside East Regeneration Project is identified in the Council's Regeneration Strategy for the District and is a long-standing corporate priority as reflected in the latest Corporate Plan.

CONCLUSION OF IMPACT ASSESSMENT

(including Diversity, Human Rights, Community Safety, Sustainability and Rural Proofing)

Community Safety: site works will give rise to environmental effects but these will be managed satisfactorily as required by planning conditions

Sustainability: It might be noted that a project aim is to deliver as sustainable a

development as reasonably possible.

FINANCIAL IMPLICATIONS

To facilitate Option 1 certain capital costs will be incurred in utilising the Planning Services' Engineering Team and in the services of those external consultancies procured (prospectively Entec and RW Gregory). The funding application to the NWDA should include for all these costs. It can be expected that any funding approval by the NWDA would cover for the consultancy elements but the position with the costs of the Engineering Team is a little more uncertain. The Team's services are time charged and would be required for the Council to discharge essential responsibilities as client. These include services that will likely be required both before and after any NWDA funding approval – including preparation and issue of tender documentation and contract management. The total cost of these services is estimated at some £20,000 in salaries. Planning Services' will seek to fund these costs from within any NWDA funding approval but, if this does not prove possible, these will be met from the Services' existing revenue salary budget.

No additional budget provision has been made for these costs, therefore they will need to be met from within existing service budgets or from the Project Implementation Reserve (subject to the remaining balance)

Under option 1 the Council will have to pay 'input tax' (tax that we pay on acquiring goods and services) on the some £5m of remediation works. As we have opted to tax we will be charged VAT on these works but will be able to reclaim it under 'partial exemption'. The Council can cashflow for this.

The Council's Legal Service can handle the Council's interests in any variation of either the BA or the JFA but it should be noted that necessary variation of the JFA will incur the HCA and NWDA in costs and these organisations will require that the Council fund these from the project budget. The costs are estimated at some £10,000 in total and the application to the NWDA should include for these.

The Council has not yet secured the developer receipts of £1.89m provided for under the BA, of which £1.7m was previously recognised as a debtor in the Council's Balance Sheet. It is no longer felt that a debtor can be justified on the Council's balance sheet due to the uncertainty surrounding the receipt and its timing. Therefore neither the Capital Programme nor the Revenue Budget makes any provision for the developer contribution being receivable. Currently this amount has been covered by the Council's own resources.

In addition, pending the Council progressing the project further, the HCA and NWDA continue to withhold some £0.5 million in project contingency due towards the Council's expenditures on the first stage of the project. Continuing delay in the timing of the land receipt and receipt of the contingency funding has financial consequences in terms of lost interest on the Council's cash balances. This is difficult to estimate due to the rapid decline of interest rates over the past 12 months. However it is reasonable to say that the Council could have lost, on average, £1500 per month over the past financial year Reducing to an average of £700 per month in this financial year.

The Council is at increasing risk of losing some or all of the £ 2.6 million in ERDF funding that it applied to the first stage of the project - given that the project has yet to achieve any of its required outputs. Officers are liaising closely with the GONW as regards this but Option 1 offers the best prospect that the risk of such clawback can be mitigated and ultimately

avoided.

In addition, for every month for which the site remains in the Council's ownership, maintenance and associated costs of approximately £10,000 are incurred. This includes maintaining the 24 hour site security necessary both to protect the integrity of assets on the site and to deter trespassers to whom the condition of the site poses real risks. The Council has provided £105,500 in the Revised General Fund Revenue Budget for 2009/10. There is however real risk that the costs of holding the site will increase in the future if remedial safety works prove to be required to buildings and structures. As timely a project delivery as possible, with an associated early transfer of responsibilities for the site to the private sector, will therefore minimise the Council's costs. Option 1 gives the best prospect of this.

SECTION 151 OFFICER'S COMMENTS

Whilst not without risk itself, Option 1 presents a positive way forward to help manage the greater financial risks facing the Council in respect of this project, given its position and the current economic climate.

LEGAL IMPLICATIONS

There are no direct legal implications arising from this report.

MONITORING OFFICER'S COMMENTS

The Monitoring Officer has been consulted and the comments have been incorporated into the report.

BACKGROUND PAPERS

Planning Services Files
Joint Funding Agreement 16 September
2004
Building Agreement 2 November 2005

Contact Officer:

Julian Inman
Telephone: 01524 582336
E-mail: jinman@lancaster.gov.uk
Ref: LE