CABINET

Luneside East Regeneration Project
9 November 2010

Report of Head of Regeneration and Policy

PURPOSE OF REPORT					
To report on options for progressing the regeneration project.					
Key Decision	**X**	**Non-Key Decision**		**Referral from Cabinet Member**	
Date Included in Forward Plan	October 2010				
This report is exempt from publication by virtue of paragraph 3, of Schedule 12a of the Local Government Act 1972					

RECOMMENDATIONS OF COUNCILLOR BRYNING

(1) That in the event the Head of Regeneration and Policy is able to assure the feasibility of option 1 to the satisfaction of the Council's Monitoring Officer and the S151 Officer and that further, provided that the option would not involve any financial commitment by the Council additional to that budgeted for to date, then the Head of Regeneration and Policy is authorised to vary the Building Agreement of 2 November 2005 as appropriate to facilitate option 1.

(2) That the Head of Regeneration and Policy report back on any variation made to the Building Agreement to put option 1 into effect and to enable the general fund capital and revenue budgets to be updated as appropriate.

(3) That in the event option 1 proves unimplementable that the Head of Regeneration and Policy report back on options.

1.0 Introduction

1.1 This project is a long-standing corporate regeneration priority for the Council. A Cabinet resolution of 25 November 2003 governs the project. Subsequent to this officers have reported on progress at length over the years via the Luneside East Advisory Board.

1.2 The current position is that since early 2008 the recession has prevented the Council's development partner from taking the project forward. This developer is Luneside East limited (LEL) - itself a joint venture company between CTP Ltd and Development Securities plc. Market conditions are very adverse and the site has a nil value in its present condition. The main barriers are high upfront costs in remediating (cleaning up) land contamination and difficulties in securing a developer(s) for the residential elements

1.3 Council officers have worked with LEL for over two years to try and identify a changed delivery approach that offers a way forward. Until recently though this work has been to no avail. Market conditions, including much lowered asset values, much reduced prospective profit returns and limited availability of credit finance precluded all options considered.

1.4 The recent Lands Tribunal decision arising out of a compulsory purchase compensation claim, however, has opened up the possibility of changing the programming of the project to allow a first phase "shop window" of commercial development by LEL at the entrance to the site. This combined with some clearance and tidying up works on the wider site would signal to the public and the development industry that a start had been made and increase the chances of securing a residential developer(s).

1.5 As this represents a change to the approved project issues such as procurement, state aid and the attitude of the project funders need to be addressed. In addition, the proposal does need further detailing. However, subject to this the proposal set out in outline below does appear to represent a realistic way to move forward and break the current impasse. There is an imperative to move forward - as discussed more fully in section 6 of this report.

2.0 Proposal Details

2.1 The main problem is that the delivery approach required under the Building Agreement loads the developer with very substantial cost and cost risk up front. This reflects a planning requirement for comprehensive remediation and also a development need to provide much advance infrastructure and scene setting public realm. The need for the latter arises out of the fact that developers can only invest if they are confident of securing end use occupiers and they will not be able to attract these unless the perception of the site is transformed from its present redundant industrial character to a place that is attractive.

2.2 The front loaded cost means that the economics of developing the site as per the Building Agreement, marginal at the best of times, are no longer tenable given the market conditions that now prevail in the aftermath of a recession and the banking crisis. Any changed delivery approach therefore needs to address and reduce the burden of front loaded cost and risk on the private sector.

2.3 Members will be aware of the Council's vigorous defence of a claim for CPO compensation made by Thomas Newall Ltd (TNL) and referred to the Lands Tribunal. The preliminary proceedings into this claim involved presentation of expert evidence concerning a variety of planning matters. One aspect related to the Council's long standing requirement for comprehensive remediation of the site prior to occupation. Expert independent evidence pertaining to this was presented by both parties and tested by counsel. One of the many conclusions of the Tribunal, presided by a Judge, was that while comprehensive remediation would be best, the remediation works necessary for the TNL landholding alone could be done on its own.

2.4 Officers have considered the implications very carefully; this opens up a new opportunity for taking forward the project itself via a variation to the Building Agreement, to remove the obligation on LEL to remediate the site all in one go at the start.

2.5 Subject to receipt of a satisfactory planning permission, LEL would undertake a first development phase under a temporary licence comprising a part conversion of the St George's Works mill building, plus lay out of public realm at the gateway to the whole site at Carlisle Bridge. To make for a quality entrance and setting to the site as a whole, that part of the mill closest to Carlisle Bridge would be demolished. Remediation works would be to the planning standards as set.

2.6 Also on receipt of such planning permission, LEL would assume all management and maintenance responsibility, including cost liabilities, for the rest of the site, again, under licence.

2.7 Once the initial phase of development and public realm works were complete, the Council would then transfer the entire site to LEL via a 999 year lease to develop further commercial phases, including options for a hotel on the riverfront, and to manage disposal of the other (greater) parts to third party residential developers.

2.8 The Council would oblige LEL to develop the site consistent with a revised masterplan. This agreement would grant LEL discretion in its disposals to the third parties subject to reasonable endeavours being made to attract partners and the development plans being in line with the aims of the overall scheme. All development works, including remediation works, would of course have to meet planning and other regulatory requirements.

2.9 Financial provisions would be in line with those set in the Building Agreement save to defer a land payment in lieu of land value. This means that there is no guaranteed developer contribution back into the Council but the removal of the up front charge would significantly increases the attractiveness of the development for the developer, in terms of risk.

2.10 LEL would be limited to a maximum 15% profit return over costs (as per the present Building Agreement). Above this profit would return to the Council via a preferential return. with overage shared 50:50 between the Council and the developer (but note that the Council must pass any overage to the HCA and NWDA).

3.0 Details of Consultation

3.1 Officers have worked very closely with LEL to bring forward this proposal and have also liased with officers of the Homes and Communities Agency (HCA) and the Northwest Development Agency (NWDA).

3.2 Members will recall that the development concept for the Luneside East site was informed by very extensive public engagement several years ago and officers will assure that the masterplan revision respects community aspirations. The planning process also provides an opportunity for the public to comment on the development approach to be taken.

4.0 Options and Options Analysis (including risk assessment)

	Option 1: To revise the Building Agreement with LEL to facilitate under licence a first phase of commercial development at the gateway to the site and, subject to performance in this, disposal of the whole site to LEL via a 999 year lease for development to fit to a revised masterplan for the site	**Option 2:** To effectively mothball the site and wait for economic conditions to change sufficient to make the project deliverable as per the present delivery approach	**Option 3:** Not to make a proposal to the funders and await a proposal from them with the risk that they require a disposal
Advantages	- provides for an early first phase of development at the critical gateway that should set the scene and transform developers' perceptions of the site and help bring housing developers forward - holds prospect of over time achieving a development that can rejuvenate Luneside - retain in LEL a developer partner that has performed well to date in a commercial development and, for the wider site retains it for its understanding of the site and site conditions - removes the Council of its	- retains the development opportunity	- minimises work for Council officers

	ongoing maintenance obligations for the site (including for site security) and the costs of these. - reduces the Council's exposure to clawback of ERDF funding - incentivises LEL but to a minimum practicable profit level (15% above costs) above which the Council would secure a priority return - gives the council some prospect that it can recoup capital costs incurred via the priority return - will help the Council assure it has a robust housing supply and reduces risk that greenfield sites are developed instead		
Disadvantages and risks	- If the developer does not achieve their 15% return the Council will get no income from the development. However, it is judged that under the other two options receipts would be less likely or not achievable at all.	- for the foreseeable future does not further regeneration - the site will remain in a state that blights the area and is a drag on investment in Luneside - will not permit the Council to retain LEL and the capacity, site knowledge and accumulated expertise of LEL will be lost - leaves the Council with significant cost and risk liabilities for the site in management, maintenance and security and with a certainty that the costs and risks will	- negates all the investment and effort made by the Council, the funders and LEL over the past ten years to bring forward this key regeneration site for development and unravels the land assembly - is very prejudicial to the Council's credibility in regeneration and, in particular, risks prejudicing the Council's ability in the future to bring forward regeneration backed by compulsory purchase and also to draw in development

		escalate and probably quite rapidly as buildings deteriorate - leaves the Council exposed to risk of ERDF funding clawback - reduces the Council's prospective housing supply and increases risk that greenfield sites will be developed	partners - the site will remain in a state that blights and is a drag on investment in Luneside - will not permit the Council to retain LEL and the capacity, site knowledge and accumulated expertise of LEL will be lost - leaves the Council with cost and risk liabilities for the site in management, maintenance and security and with a certainty that the costs and risks will escalate and probably quite rapidly as buildings deteriorate - leaves the Council exposed to risk of ERDF funding clawback - reduces the Council's prospective housing supply and increases risk that greenfield sites will be developed -

5.0 Officer Preferred Option (and comments)

5.1 The economic downturn has been severe and whilst the situation is better than a year ago market advice is pessimistic about prospects for an early recovery in the development sector. In terms of residential developments, recent reports from RICS have indicated further downward pressure on house prices as sellers out-number buyers. In this context, to be realistic, there is little prospect of the Council securing development of Luneside East site in line with the approved delivery approach and the Building Agreement with LEL.

5.2 Accordingly, for the foreseeable future it is unreasonable to expect LEL to proceed as per the Building Agreement. In these circumstances if the Council wants to move things forward it needs to adapt the project to fit to what are very changed market circumstances.

5.3 Since 2008, Council officers, working with both the funders and LEL, have given quite exhaustive consideration to potential options and have concluded that only three may be available and only one would move the project forward in a positive manner, this option is therefore preferred (option 1).

5.4 The option analysis presents many advantages for option 1 but an argument that requires amplification is that of regeneration need. The project concerns the city's oldest former heavy industrial site, some 7.1 ha (15 acres) of brownfield land, the site was for many years an oilcloth works and the town gasworks. In its current condition it is in many respects a blight on the wider area and a drag on its fortunes. The project is about remedying this by bringing the site into a mix of beneficial uses so as to create a new neighbourhood that better connects the city centre and historic quay with existing neighbourhoods to the west. The aim is that the development should be vibrant and help rejuvenate Luneside by transforming investment perceptions.

5.5 The project is therefore an important driver for regeneration need in this part of Lancaster and it remains imperative to move it forward. This said, option 1 is not yet fully formed. Various matters including legal considerations need to be worked through further before option 1 can be fully detailed and its feasibility assured. Officers are in continuing discussions as regards these and have sought expert advice where appropriate.

5.6 Subject to this, the option outlined would represent a reasonable and proportionate response to changes in market conditions. It would re-balance risk and reward by reducing risk to LEL but with adjustments to the priority return and overage in favour of the public sector.

5.7 Further, the option would enable the Council to retain a developer partner in whom it has confidence and that gave much support to the Council in its delivery of the first public sector stage of the project. LEL has an appetite for the proposal. It has a strong track record in delivering commercially focused developments to a high quality and has consistently maintained that it can establish Luneside East as a new location for businesses. The first phase alone should go some way to delivering on the NWDA and ERDF commercial floorspace output requirements for the project.

5.8 Not least, the proposal if adopted would rid the Council of its ongoing liabilities for the site as detailed further in financial implications below.

5.9 Time, however, is not on our side. A first consideration is that as from 24 September 2010 the Council is in default of its Funding Agreement with the HCA and NWDA In this event the Funding Agreement gives the Council six months to submit a revised proposal (i.e by 24 March 2011)

5.10 Second, if the site is not presented in a better condition before long then it may well prove extremely difficult to attract developer interest because by this time it is likely that developers will have very much easier development opportunities to pursue and invest in as the market slowly recovers. These could arise elsewhere in Lancaster District but will almost certainly be available elsewhere in the Northwest region. There is therefore real risk that if we cannot move the project forward soon it may well fail.

6.0 Conclusion

6.1 This key regeneration project is stalled. After lengthy and very careful consideration realistic options are proposed. One, option 1 affords the best prospect that the project can move forward - subject to some further work. It offers real prospect of achieving development of the Luneside East site in a considered and well planned manner to secure long standing aspirations both for the development itself and what it can effect over time in terms of area wide regeneration. Members are invited to determine how officers should proceed.

RELATIONSHIP TO POLICY FRAMEWORK

The project fits with the Lancaster District Core Strategy 2008 and is identified as a priority in the Corporate Plan 2010 - 13 Supporting our Economy, under Heritage and Cultural Tourism.

CONCLUSION OF IMPACT ASSESSMENT
(including Diversity, Human Rights, Community Safety, Sustainability and Rural Proofing)

The site is in as sustainable a location for mixed use development as is reasonably possible in the District.

LEGAL IMPLICATIONS

The preferred option has to be considered in the context of the Joint Funding Agreement with HCA/NWDA. Under the terms of this agreement the Council is now in default because of the failure to make progress with the project and the Council requires the consent of HCA and NWDA to proceed in any course. As regards option 1 the Building Agreement would have to be substantially revised to recognise the present circumstances but in principle the proposed terms are within the spirit of the original agreement and reflect a means of achieving the anticipated outcomes of all parties. However such a view is given subject to obtaining expert advice in respect of any State Aid and procurement issues arising from this variation (to the original terms of the tender procedure) to confirm that such variations are not open to challenge.

Options 2 would require the consent of HCA / NWDA under the Funding Agreement as would option 3 but otherwise do not present any direct legal implications.

FINANCIAL IMPLICATIONS

Capital

Option 1 The Council has not budgeted for any income from Luneside land with the amounts for developer contributions written off the capital financing in 2008-09 so further receipts would provide additional funding for the 5 year rolling programme. However, any receipt would be contingent on LEL making a 15 % return; it will have to be contractually defined as to what this means, for example, what measure of profit is used, when this is measured and how this would relate to profits generated from any land disposed to third parties. In addition, the Council has not budgeted for capital expenditure to maintain the structural integrity of the buildings, an issue which will likely become more pressing. Should options 2 or 3 be considered, the Council's exposure to this liability would need to be quantified. Property services have indicated that a condition survey of the I buildings – a necessary precursor to quantifying this liability - could easily cost in the region of £20K

Revenue

Under option 1 the Council could stand to recover in full, or part, the £48k which funded the developer contribution written off in 2008-09. Savings on site maintenance costs cannot be quantified or confirmed until the date of transfer to LEL is known. There is £90k currently budgeted for both in 2010-11 and 2011-12 but this is also subject to change when the security contract is renewed at the beginning of December 2010. Costs to the Council in monitoring the private sector delivery stage are estimated at £10k per annum for three years starting from 2012/13.

It should also be noted that this option is in line with the HCA/NWDA funding agreement giving the Council 6 months to submit a revised proposal. Failure to do this could put at risk the £502k contingency funding (split £78k revenue and £424 capital) which has been spent but will not be paid over to the Council until certain milestones have been achieved.

Option 2. As mentioned previously, continued revenue costs for the Council in site management and security of £90k per annum for 2010-11 and 2011-12 are currently budgeted for. If the site were held for longer than this there would be additional costs which the Council would need to budget for during the 2011/12 Budget Process in holding the site, plus substantial costs and cost risks arising from the impending need to intervene, stabilise or make safe certain dilapidated buildings. There would also be few or no prospects of recouping any of the Council's costs defrayed in the project to date.

If option 3 were chosen the costs and implications for the Council are at this stage difficult to quantify and could potentially be wholly dictated by the funders in deciding to either sell the site or finding a way to continue with the project.

VAT

The land and buildings at Luneside East have been opted for VAT. Before any transfer of land is made, the VAT consequences need to be fully assessed to ensure that LEL are aware of, and are happy with, any VAT charge on the transfer. However, as noted in section 1.2 above, the site is currently judged to have £0 net worth and so it is anticipated that no VAT would be chargeable. There would be no immediate VAT consequences of option 2 and as there is no concrete proposal attached to option 3, the VAT consequences would have to be considered once these proposals became clear.

Governance

Under option 1 the mechanism for the Head of Regeneration and policy to assure other statutory officers of the feasibility and legality of the scheme must include a full corporate risk assessment and appraisal in accordance with constitutional requirements including Financial Regulations and supporting arrangements. Should these be satisfied, the legal agreement would be entered into / signed off under the Council's normal arrangements. This applies equally to option 2, which would need to be fully planned and costed in terms of the ongoing liabilities of the site; it also applies to option 3 although this would be contingent on the default scheme proposed by the funder.

OTHER RESOURCE IMPLICATIONS

Human Resources:
None

Information Services:
None
Property:
Option 1 if adopted provides for disposal of the whole site to LEL via a 999 year lease as per the extant Building Agreement i.e. no change. The trigger point for this would be practical completion of a first LEL development phase. The proposal provides that on receipt of a satisfactory planning permission for its first phase LEL would develop this phase under Licence so that the Council can assure satisfactory completion before effecting a full land transfer. Concurrent with this though LEL would take management and maintenance responsibility for the wider site as well , thereby removing the Council of its current and onward liabilities for the site and costs in site management and maintenance.

Open Spaces:
The masterplan for the site provides for much new open space and high quality public realm and officers expect to sustain a similar level of provision in any revised masterplan.

SECTION 151 OFFICER'S COMMENTS

Potentially the recommended option presents a way forward with the scheme but as set out in the report, there are key issues to address before any firm conclusions may be drawn.

MONITORING OFFICER'S COMMENTS

The Monitoring Officer has no further comments at this "in principle" stage. Clearly the viability of the recommended option depends on whether or not further detailed legal advice still to be obtained, is supportive..

BACKGROUND PAPERS	**Contact Officer:** Julian Inman **Telephone:** 01524 58233658 **E-mail:** jinman@lancaster.gov.uk **Ref:**
Joint Funding Agreement 24 September 2004 Building Agreement 2 November 2005	