

CABINET

Chatsworth Gardens – Potential for Private Sector Led Delivery 23 April 2013

Report of the Head of Regeneration and Planning

PURPOSE OF REPORT			
To seek approval to conduct a new preferred developer procurement route to test viable private sector led refurbishment solutions for the Chatsworth Gardens project following recent developer interest.			
Key Decision	<input checked="" type="checkbox"/>	Non-Key Decision	Referral from Cabinet Member
Date Included in Forward Plan	25 March 2013		
This report is public			

RECOMMENDATIONS OF COUNCILLORS KAREN LEYTHAM AND JANICE HANSON:

- 1) That Members note private sector developer interest in the Chatsworth Gardens properties/site and the receipt of an outline proposal for refurbishment on a managed private market rent tenure model.
- 2) That officers implement Option 3:
 - Conduct a new preferred developer competition to test all current private investment interest.
 - Agree Heads of Terms on a proposal which secures best consideration with respect to the policy objectives of the council and the Homes and Communities Agency.
 - Officers continue with eligible preparatory and enabling works on the previously approved council led scheme as a contingency against being unable to secure a viable private developer proposal.
 - The revenue budget be updated for the spend and external financing associated with the preparatory and enabling works.
- 3) The outcome of the developer competition, the recommended scheme and the initial heads of terms proposed are reported to Cabinet for approval to proceed towards a binding development agreement.

1.0 Introduction

1.1 Members will be aware of the work undertaken to develop a contingency proposal for the Chatsworth Gardens site following the withdrawal of the original preferred developer partner and the collapse of their demolition and new build redevelopment scheme. At its December 2012 meeting Cabinet resolved (minute reference 82):

(1) That Option 2 be approved and the Head of Regeneration and Planning be authorised to accept the £1.9M Clusters of Empty Homes Funding and deliver the Chatsworth Gardens project through the approach as set out.

(2) That the Head of Resources be authorised to update the Capital Programme and Revenue Budget accordingly to allow progression of the project under (1) above.

(3) That the Head of Resources investigate the viability of finance schemes that might assist prospective home buyers in the Chatsworth Gardens area, through means such as the lend a hand scheme or other deposit guarantee schemes and government initiatives, for consideration as part of future years' budgets.

1.2 In summary it was agreed that the council would lead on a substantial refurbishment project bringing contingent risks associated with construction, project management and, importantly, end sales. Securing regeneration objectives on Chatsworth Gardens is therefore risky both in terms of execution of the project and financial exposure. This was made clear to Cabinet who accepted the risks in order to secure a way forward and exit a difficult situation. It also allowed the council to take advantage of and maximise the Homes and Communities Agency's (HCA) Clusters of Empty Homes Funding (CEHF). The CEHF resources are, in the main, targeted at the Chatsworth Gardens site which enabled officers to develop the approved refurbishment option.

1.3 It is clearly preferable if the scheme objectives could be achieved by the private sector without the council taking on this risk. However, major developers would not have been able to work with the council without multi-million pound public gap funding. A 'traditional' development model (see Section 2.2 below) would require funding far in excess of that currently available or which is likely to be secured in future.

1.4 While this situation is not thought to have changed, the wider housing market has generated a greater national requirement for quality private homes to rent at market rates. This trend has arisen very recently in response to the difficulties faced by potential home buyers in meeting large deposit requirements of the mortgage market and a general lack of confidence in the economy. The opportunity to meet the needs of those who would formerly have been first time buyers has resulted in some debt and equity institutions softening their attitude towards the returns available and the attractiveness of investing in private rented housing. On the back of this movement the council has received new developer interest in refurbishing the Chatsworth Gardens properties for the private rental sector. Officers think that this interest should be formally explored for its potential to reduce the council's

exposure to the risks of delivering a multi-million pound housing regeneration project.

2.0 Background

2.1 The Chatsworth Gardens project objectives are outlined in the Relationship to Policy Framework section of this report. The council owns 47 properties on the site (Appendix 1a) bought with HCA grant (approx £7M spent to date). Outside of the Chatsworth Gardens area the council also owns a number of “non-project properties”¹ (NPPs) across the West End, also bought with HCA grant. The NPPs are earmarked for sale to provide funding for the main Chatsworth Gardens project.

2.2 As noted in Section 1.0 the increasing availability of long term rental income at market rents, and a belief that this demand will continue in the long term, is attracting interest from those funders/developers that have:

- Patient capital seeking steady/reasonable long term returns;
- A commitment to long term management of built developments and an interest in improving the wider area and context for their investment.
- The ability to see potential for investment growth above normal returns arising from a continuing role in improving the property/neighbourhood.

This approach contrasts to traditional large scale private housing development models predicated on: high risk/return; short-term realisation/gain through sales; highly leveraged propositions; and exit/minimising future management responsibility. This latter model is currently only available and working in areas of high demand/low risk or where major gap funding is available.

2.3 Officers have received interest in the Chatsworth Gardens properties from a developer, introduced by the HCA, pioneering the new approach to delivering private market rent housing. The developer has expressed a willingness to work on large scale refurbishments in housing market renewal/regeneration areas and is currently working with a number of other public bodies.

2.4 The approach has been made in outline and there is no detailed or fully appraisable information on the table at the present time. However, officers think this model has real regeneration potential and could bring many advantages in terms of the transfer of the majority of the Chatsworth Gardens development risk to the private sector. The developer has strong institutional backing; a long term approach to investment/return; a high degree of competency in design/delivery; a relatively simple investment model; and enthusiasm for Morecambe/West End as a place. At face value their initial proposition is a compelling one, outlining a situation where the council is able to meet its regeneration objectives without either needing to take on sales risk or bring additional investment to the table over that currently secured via CEHF.

¹ Non-Project Properties were acquired in 2004 when the Masterplan was in an embryonic stage and the HCA and LCC wanted to make early progress with strategic acquisitions. 25 properties were acquired for £2.2M all located in what became the high intervention Masterplan areas that would be brought forward under various projects e.g. Clarendon Road Remodelling, Adactus Live/Work Units, Chatsworth Gardens, Marlborough Road, Bold Street, the ceased Central Park project and the Co-Op Building.

- 2.5 In the context of the council's general obligations to secure best consideration for land and, more specifically, the need to respect the interests of the HCA as key funder, it is not appropriate for officers to engage in further discussions with a sole developer as single 'special' purchaser (see Legal Implications). The developer may not be the only firm active in exploring new approaches to private housing provision and the wider situation in the 'traditional' housing development approach should also be confirmed. A number of questions around the particular approach to private market rent sector remain and these can only be fully explored via a more structured procurement.

3.0 Details of Consultation

- 3.1 The issues around conducting a new procurement on the basis of renewed developer interest have been presented to and discussed at Housing Regeneration Cabinet Liaison Group (HRCLG) prior to this Cabinet meeting. HRCLG views will be reported to the meeting. HRCLG have previously given strong support to the council's approved proposals and are keen to see the CEHF funding offer taken up to tackle a large number of empty homes.

4.0 Options and Options Analysis (including risk assessment)

- 4.1 The available options are detailed in the table on the next page of this report.

5.0 Officer Preferred Option (and comments)

- 5.1 **Option 1** has previously been agreed by Members as a way forward. However, the ultimate risk in the council led project is that of securing sales of remodeled houses. Sales are required to generate further income to continue further phases of intervention, otherwise the project will stall. The mortgage market is still difficult for homebuyers, shows no real signs of abating and the introduction of a mortgage assistance scheme may only partially mitigate this situation. Members should be under no illusion about the challenge of securing rolling house sales in the West End of Morecambe in the current economic climate and the risks to completing the project.
- 5.2 Given these risks the appearance of a potentially deliverable proposal from a private developer and a new procurement process as described in **Option 2** must be a serious consideration. This would enable officers to formally test proposed solutions and to flush out any competing bids which may better contribute to the achievement of the council's objectives.
- 5.3 With support of the HCA, the procurement process will be undertaken to the terms of the council's Property Disposal Procedure under the General Disposal Consent allowing officers to consider a number of criteria other than price to secure the non-monetary regeneration (in effect 'well-being') objectives. The process will be an "informal" tender to explore the most advantageous proposal and proceed to secure appropriate heads of terms for a formal developer agreement (refer to Legal Implications).

	Option 1: Do Nothing - continue with previously approved council led £1.9M Clusters of Empty Homes supported scheme.	Option 2: Undertake a new preferred developer tender to test new private investment interest and secure heads of terms for a development agreement.	Option 3: As Option 2 but officers continue with preparatory/enabling work on the approved council led scheme as a contingency (PREFERRED OPTION)
A D V A N T A G E S	Provides a positive solution to Chatsworth Gardens regeneration objectives. Utilises existing regeneration funding and poses no further budget costs on the council. Brings empty homes back into use. Clearly sets out council's commitment to local residents and owners in the area. Demonstrates delivery to HCA boosting chances for future funding.	Potential to provide all advantages of Option 1 in addition to the following advantages. Formal process/test of new private interest and investment/management models. A viable proposal transfers construction delivery risk to private sector. Takes away sales risk on refurbishment. More control over private sector investment in the area to draw down Clusters of Empty Homes funding. Mitigation of council financial risk.	Retains the potential advantages of Option 2 and provides a 'hedge' against the risk of an unviable/unachievable private led refurbishment scheme. Mitigates adverse community reaction to delay or failure to secure private developer agreement. Introduction of appropriate deadlines for negotiating the development agreement should give time for implementation of the approved council led scheme as contingency (if necessary) and meet Cluster of Empty Homes Funding spend deadlines.
D I S A D V A N T A G E S	Ideally requires co-operation from owner occupiers & landlords to avoid costly legal action. Uncertainty of delivery remains for the Regent Road terrace in the Eastern block. Misses out on potential to test new private sector interest to transfer development risk away from the city council.	Further delays in progressing action. Any proposed solution will still require co-operation from owner occupiers and landlords Uncertainty of extent of intervention achievable and certainty of delivery until tender/conclusion of development agreement negotiations. Complexities of mixing eligible elements of Clusters of Empty Homes Funding to create a 'best scheme'. Potential for deal to be based on nationally untested private tenure/management models. Ongoing management costs of properties while resolving tender/negotiations.	Implementation issues/disadvantages are as Option 1/Option 2 depending on which route is eventually taken. In addition the following can be identified: Build costs and sales value may change over time with adverse consequences for the extent of a council led scheme if private sector led scheme is not agreed/implemented. To maintain a capability to quickly implement (if necessary) a contingency council led scheme some continuing spend is necessary. This requires mitigation of audit issues concerning technical definitions of capital/revenue, eligible spend of current public funding and whether works are 'abortive' if the private led scheme is contracted (see Financial Implications).
R I S K S	Involves the council taking the delivery risks on a capital housing development project. The council will face a sales risk on the direct refurbishment properties that needs to be mitigated by some form of mortgage assistance scheme. Limited control over private sector match required to access part of HCA funding. Build costs and sales date/value can adversely impact project (although a reasonable contingency is built in).	No guarantee that on detailed review /appraisal a private led scheme for comprehensive refurbishment is viable or achievable. No site disposal deal with private sector is made. Adverse community reaction to further delay and breakdown of any deal with no back up plan. Potential to miss spend deadline for Clusters of Empty Homes funding if a private scheme is not agreed.	Option 2 risks are mitigated through Option3 although the following should be noted if the contingency plan is required: Option 1 risks will come into play should the council led scheme be required and costs and sales impacts caused by delay will have to be allowed for. Meeting the final deadline for Clusters of Empty Homes Funding will also be more challenging

- 5.4 However, taking this route brings with it a number of key risks:
- There is no guarantee a deal with a private developer can be made: the Chatsworth Gardens site/properties are hard/expensive to deal with and no detailed appraisal has been made by any interested parties at present.
 - The Clusters of Empty Homes Funding needs to be committed by end of March 2014 and spent by September 2014. Should a final negotiated agreement with a private developer not materialise it will be difficult, given the work involved to mobilise and secure statutory consents, to resurrect the council's approved scheme and secure CEHF spend by this deadline.
- 5.5 **Option 3 is therefore the preferred option** - officers continuing to undertake preparatory work for the council's current approved scheme as a contingency against being unable to secure a development agreement.
- 5.6 The developer procurement will be open to all tenure models but it is likely the only viable private developer route to a comprehensive scheme will involve a model based on private market rent. The introduction of privately rented stock, if managed correctly, is compatible with the overall regeneration objectives for Chatsworth Gardens (see Relationship to Policy Framework) and is consistent with trends in the housing market. However, Members will be alive to the need for robust management protocols and enforceable legal agreements to prevent reversion of properties to uncontrolled market rent in a regeneration area.
- 5.7 The developer proposal assessment will explore these issues in detail and develop appropriate heads of terms to mitigate risks. The successful proposal and the broad terms of the expected deal will be presented to Cabinet for agreement prior allowing officers to move towards detailed development agreement. It will also be important for Members to agree deadlines for completion of any deal to secure the use of CEHF funds.
- 5.8 Members should note that integration and eligible use of the CEHF funding package to create a 'best scheme' will form part of the developer competition process.

6.0 Conclusion

- 6.1 The private developer proposal is in outline only and its potential unproven. However, officers think there is real regeneration potential and advantages in the transfer of risk, which the recent interest in schemes for market rental return presents. A new developer competition will take time to complete and lead to further delays in bringing activity to site. From the point of view of the council's risk burden it is an opportunity that officers think the council should explore.
- 6.2 There is no guarantee that a private scheme will ultimately be deliverable in the Chatsworth Gardens context and retaining the ability to spend CEHF resources is critical. It is therefore prudent to continue to work on and reserve the council's current approved scheme as a contingency.

RELATIONSHIP TO POLICY FRAMEWORK

In January 2011 council resolved that housing regeneration be included as a theme in its corporate priorities. This was reaffirmed in the 2012-2015 Corporate Plan.

The Chatsworth Gardens Project is a key element of the West End Masterplan and was ranked as a high priority by Cabinet as part of review and refresh exercise carried out on the Masterplan in 2009. The council has been working with the Homes and Communities Agency (HCA), formerly known (prior to December 2008) as English Partnerships, to deliver the Chatsworth Gardens Housing Exemplar scheme. The objectives of the proposal are as follows:

- Attract families and long-term residents to live and work in and near the town
- Create a more balanced community
- Reverse the negative perception of Morecambe's West End as a place to live
- Reduce the number of HMOs (Houses in Multiple Occupation)
- Kick-starting public/private investment in the area;
- Creating confidence in the market – to show that family housing is possible and have a catalytic effect (along with the other interventions)
- Deliver quality housing stock
- Address crime and social conditions in the area
- Act as a demonstration to the market in terms of the standard and quality of housing that should be delivered in the Masterplan area

As 40% of the districts homelessness derives from failed private sector tenancies in the West End, these schemes will help reduce homelessness correct housing supply imbalances are corrected and help stabilise a transient community

There is a relationship between bringing empty homes back into use and the allocation of proposed sites for housing in the Local Plan. Empty property reuse is significant element of providing for the District's housing needs.

CONCLUSION OF IMPACT ASSESSMENT

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

The West End Masterplan has carefully considered issues of sustainability and is based on sustainable principles. Any proposal received will need to be designed and built in accordance with specifications/standards which ensure high quality urban design, including safer by design and life time homes standards as well as high environmental standards. Human rights and diversity issues are given special consideration as remaining owner interests are acquired.

LEGAL IMPLICATIONS

Legal Services have been consulted and their comments inserted within the body of the report where appropriate.

The legal implications of progressing with **Option 1** are fully discussed in the report/recommendations of 4th December 2012 Cabinet (Minute 82).

In terms of the legal implications of progressing with a new developer competition as in **Option 2** (and by implication as a part of preferred **Option 3**) Members should be aware of

the following:

The developer competition suggested is effectively a disposal of land and the terms of the disposal will be taken forward under the terms of the council's disposal procedures. Section 123 of the Local Government Act 1972 requires authorities not to sell land for "a consideration less than the best that can reasonably be obtained". However, ODPM Circular 06/2003 provides a General Disposal Consent where the disposal contributes to:

- The promotion of economic well being
- The promotion or improvement of social well being or
- The promotion and improvement of environmental well-being

With the wide ranging regeneration objectives sought officers are therefore able to construct a developer competition with a focus on non-monetary factors which is compatible with the Corporate Property Strategy and these statutory provisions.

Given the approach by a single developer the possibility exists of negotiation on the proposal as a single (special) purchaser deal. Given the lack of wide commercial interest in West End housing development it may be considered prudent and timely for officers to deal with best consideration issues on a negotiated/valuation basis. However, the HCA has funded the Chatsworth Gardens property purchases and under the grant agreement they are the ultimate holder of the current property portfolio value. While happy to agree with a developer competition that emphasises "non-monetary" factors and regeneration impact, the HCA has indicated it wishes to see equal opportunity for others to submit alternative schemes to ensure the impact of their initial investment is maximised.

The chosen method of disposal must be fair, consistent and transparent. As a complex development scheme the appropriate method in this instance is an Informal Tender procedure which explores the quality of scheme proposals, deliverability and the financial bid.

Heads of terms for a Development Agreement will be sought to ensure the council retains control over this major scheme and ensure that the disposal will be in accordance with Section 123 of the Local Government Act 1972, and/or the General Disposal Consent. The agreement will be required to incorporate provisions for monitoring the performance of the developer and the ability to grant disposals in a phased manner. The terms of the proposal will be reported to Cabinet prior to moving towards a final Development Agreement.

FINANCIAL IMPLICATIONS

The Financial Implications of progressing with **Option 1** are fully discussed in the report/recommendations of 4th December 2012 Cabinet (Minute 82).

In terms of the Financial Implications of progressing with a new developer competition as in **Option 2** (and by implication as a part of preferred **Option 3**) Members should be aware of the following:

A viable private scheme should remove the council from the burden of contingent risks in respect of construction, refurbishment, project management and end sales and on that basis should be pursued.

A further report will need to be brought back to Cabinet to cover the outcome of the developer competition and to consider any financial implications arising from a proposed

development agreement and future management of the private developer scheme.

The principal financial risk from engaging with a new developer arises from the ability of the council to secure Clusters of Empty Homes spend. To maintain capability to deliver the originally approved council led refurbishment scheme some continuing expenditure is necessary. In accordance with the accounting code of practice such expenditure would need to be charged to revenue as there would be no certainty that the original council led capital scheme would continue. However, the additional costs are minimal at just over £1K and would be funded by the HCA who currently finance all revenue costs associated with the council owned Chatsworth Gardens properties.

OTHER RESOURCE IMPLICATIONS

Human Resources:

The human resources required to deliver Option 1 are fully discussed in the report/ 4th December 2012 Cabinet (Minute 82) report - these are principally from Regeneration and Planning, although other services support is required, including Financial, Property and Legal. For progressing with a new developer competition as in **Option 2** (and by implication as a part of preferred **Option 3**) Legal, Financial and Property Services will assist Regeneration and Planning officers in drafting the developer competition criteria and negotiating and drafting the terms of the underlying development agreement. If deemed appropriate specialist legal advice will be engaged to assist in the preparation of the agreement.

During the developer competition there will be a particular role for Financial services in performing the necessary due diligence on the sponsor of a preferred proposal to ensure their viability, covenant strength and anything else deemed material.

Information Services:

No Information Service implications.

Property:

The major implications for the involvement of Property Services in the developer competition are discussed in the body of the report and Legal Implications section. The developer competition involves the disposal and future development/management of refurbished residential and some commercial property to the terms of the council's Corporate Property and Disposal Strategies. The progression of the competition requires input from the council's property services staff in conjunction with Regeneration & Planning staff leading the project.

Open Spaces:

No Open Space implications.

SECTION 151 OFFICER'S COMMENTS

The s151 Officer has been consulted and has no further comments.

MONITORING OFFICER'S COMMENTS

The Monitoring Officer has been consulted and has no further comments.

BACKGROUND PAPERS

Winning Back Morecambe's West End

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Masterplan - available on Lancaster City
Council Website:
<http://www.lancaster.gov.uk/planning/regeneration/morecambe-s-west-end/>

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