

Part A

Report to: Cabinet

Date of meeting: 9 September 2019

Report author: Head of Regeneration and Property

Title: Croxley Park Update

1.0 Summary

- 1.1 This paper updates Cabinet on progress on the Croxley Park transaction and changes made to the proposal which was submitted to and agreed by Cabinet on the 21 January 2019 and Council on 23 January 2019.
- 1.2 After further negotiations with Columbia Threadneedle Investments (CTI), the completion of the grant of the lease and other associated contracts occurred on the 26 July 2019.
- 1.3 The main change to the transaction previously reported to Cabinet and Council was that there was a revision of the Retail Price Indices (RPI) cap and collar on the rent guarantee which was changed from 2% - 4% to 0% - 5%. This resulted in an increased payment of £4m to the council by the freeholder to cover the additional risk underwritten by the Council. This change was agreed by the Managing Director in consultation with the Mayor on 21 June 2019 in accordance with the delegated authority given by Council on 23 January.
- 1.4 In addition prior to completion the original freeholders sold on their freehold interest so the council entered into the lease with a new freeholder named Croxley 1 Limited and Croxley 2 Limited as nominees of Croxley Master Trustee Limited, Trustee of Croxley Master Property Unit Trust. This is a vehicle in which Goldman Sachs and BAE Systems Pension Fund Trustees Limited have an economic interest and is being registered in Jersey. The council were consulted on the changes and the delay in completing this transaction is primarily as a result of this new party undertaking additional due diligence. This involved additional legal work for the council and it was agreed as part of this change that a contribution of £150,000 would be made by CTI to cover additional legal fees the council incurred. Approval to complete the lease from the new freeholder was given by the Managing Director in consultation with the Mayor on 26 July and confirmed in writing on 29 July 2019.
- 1.5 The ongoing Asset and Property Management arrangements remain with CTI and Workman respectively and contracts with them also completed on 26 July 2019. Reporting structures have been formalised and regular marketing and asset

management meetings have been programmed throughout the year. Additional contracts for letting agents, to provide marketing and lease renewal advice have been agreed with the existing team so the momentum can be maintained on the letting, marketing and performance of the Park

- 1.6 Regular quarterly Asset Management reports on the Park's performance, covering rent collection performance, lettings, capital expenditure and general issues will be presented at Property Investment Board together with updates on the Park's Investment Strategy and Business Plan. This will be in addition to regular weekly meetings on the Park. Updates will also be provided to Major Projects Forum.
- 1.7 A detailed Business Plan is being developed which will look forward over the next 5 years, with a more detailed review of the next 12 months. The Business Plan is expected to be ready by early October 2019 whereupon it will be taken to the next available cabinet to request sign off. Part of the purpose of the Business Plan will be to set out required delegated powers for selected members of the asset management and property management team to streamline the decision making processes. Until the business plan is in place the existing delegation limits of the Property Investment Board (PIB) will apply and delegation will be exercised by the Head of Regeneration and Property.
- 1.8 The £92M, received upon completion in respect of rental shortfalls and planned programmed maintenance, has been invested with in the Government's Debt Management Account Deposit Facility to allow an investment strategy to be developed and procured working with the Council's treasury advisers Link Asset Services. The council resolution provided for this amount to be invested to act as a buffer against the risks associated with the project.
- 1.9 Two new posts funded out of Park monies will be created. One in the Investment Property Team to closely oversee the performance of the Park and the appointed consultants, reporting to the Head of Property and Regeneration, currently a member of LSH's team is seconded to the council for a day a week to assist until the post can be recruited to. The second is a senior property solicitor post in Democracy and Governance. This is due to the fact that by taking on the Park the council will now have the associated additional legal work of dealing with 60 under tenants. Initially it has been decided to recruit to this post for a 1 year fixed term to gauge workload.

2.0 Risks

A detailed summary of risks is contained in the previous Cabinet Paper and remain the same

Nature of risk	Consequence	Suggested Control Measures	Response (treat, tolerate, terminate or transfer)	Risk Rating (combination of severity and likelihood)
RPI increases	The capital payment made by the freeholder may be used up sooner than was anticipated	Closely monitor. An additional payment of £4m has been	Tolerate	8
Marketing	Rental levels decrease if vacancies increase	Monitor agents and change if necessary. Consider incentivising agents.	Treat	8
Asset & Property Management Performance	The income of the Park isn't optimised	Review and retender	Treat	6

3.0 Recommendations

- 3.1 To NOTE that the transaction to take a 40 year lease of Croxley Park and the option to buy the freehold at the end of the term for £10 has completed and that the payment of £92,000,000 has been made.
- 3.2 To NOTE the changes to the terms of the transaction as outlined in the report.
- 3.3 To NOTE the asset and management arrangements in place going forward.
- 3.4 To APPROVE the appointment of two new posts, one in the investment team to oversee the running of the Park for the council and the second in the legal team to undertake the day to day legal work generated by the Park.

4.0 Detailed proposal

- 4.1 The structure of this proposal is set out in the Cabinet and Council papers dated the 21 and 23 January 2019 respectively. In summary the deal structure is as follows. The council has acquired a 40 year head lease in Croxley Park (The Park). The

proposal has been structured as an “income strip” deal and the Council has the option to acquire the freehold of the Park at the end of the term for £10.

- 4.2 The Council will receive the full passing rental income from occupational tenants on the Park in return for paying a rent of £9.2m per annum to the freeholder which will be indexed linked to RPI with a cap and collar of 0-5%. The Council is, in addition to retaining the profit rent, responsible for rental risk and all planned and preventative maintenance (PPM).
- 4.3 On completion the freeholder made a payment to the Council of £92m to cover rent top up and Planned and Preventative Maintenance. This payment is broken down as follows, £20m of this sum represents a rent top up to cover any rent free periods on occupational leases whilst the balance £72m of the sum is set aside to off set risk and be used for planned and preventative maintenance over the term of the proposed lease which will become the Council’s responsibility going forward. This funding will be required in later years so will be invested to generate returns for the Council in the interim period.
- 4.4 The £92M has been temporarily invested within the Government’s Debt Management Account Deposit Facility (DMADF) to allow an investment strategy to be developed and procured working with the Council’s treasury advisers Link Asset Services.
- 4.5 Discussions with Link have identified a range of options for investing this money going forwards, but due to the current financial markets the advice is to retain the money within the DMADF for the short term. Going forwards we are working with Link to consider a range of options for the structure of investment, which may range from investing in an existing fund through to setting up our own fund. We will also need to consider the types of funds we would wish to invest in. Link are currently undertaking some soft market testing to understand the interest from the financial markets for our funds.
- 4.6 As this type of investment is new to the Council we will be setting up some training, for both officers and members, which will set out the risks and issues of each of the different investment structures available, and also to help with the consideration of the type of fund in which we wish to invest. Once this training has been completed, and we are confident that there is an understanding of the options available, we will be asking members to decide on the level of risk they wish to accept on the investment and the then confirm the investment route they would like to take.
- 4.7 CTi will additionally pay for and contract manage the construction of a new 85,000 sq ft office building which will commence construction in the third quarter of 2019 which will offer the Council an opportunity to generate further income. CTi have put £4m into escrow to cover the risk of cost overrun and also have secured a fixed

price building contract. LSH Building Management Services will monitor the construction of this project and provide regular monthly reports on progress.

- 4.8 Following approval by cabinet and Council in January there have been further negotiations with CTI relating to the transaction which has revolved around them selling on their freehold interests to an annuity fund vehicle which is headed up by Goldman Sachs which is now the council's freeholder. The new freeholder is Croxley 1 Limited and Croxley 2 Limited as nominee of Croxley Master Trustee Limited, Trustee of Croxley Master Property Unit Trust and as part of the deal other large Pension funds have bought shares in this arrangement.
- 4.9 In addition to paying rent to the new freeholder the council will from time to time require freeholders consent for alteration works, new lettings over 10 years etc. A protocol has been put in place with the freeholder to ensure the requests can be handled promptly in order not to cause delays or potentially lose prospective tenants.
- 4.10 This onward sale of the freehold resulted in significant delays to the original timetable as the proposed new freeholder had to undertake further due diligence which also resulted in a request to alter the terms of the transaction. The main change was to the Retail Price indices that applies to the rent that the council guarantees. This was originally agreed with a cap of 4% and collar of 2% and a request to change this to a cap of 5% and collar of 0% was made. The council's finance team instructed Grant Thornton (GT) to model the risk and it was deemed acceptable only in the event of a further payment being made to the council of £4m increasing the total contribution by the freeholder from £88m to £92m to reflect additional risk
- 4.11 The Property Management data will be held and controlled in two data bases, one run by Trowers and Hamlin LLP for legal documentation and another Bespoke property system called TRAMPS which contains property details and lease events including invoicing. This system is consistent with the council's outsourced Investment Property System run by LSHIM
- 4.12 Due to the increased size of the investment portfolio as a result of the completion of this transaction it is necessary to create 2 new posts. One in the property team to act as client officer to manage our external consultants and the second in the legal team to deal with the transactional landlord and tenant work arising from having 60 new under tenants. It is proposed that both posts be funded from the Park revenue and there is provision for this within the financial modelling. The legal post will be for an initial term of 1 year to gauge the actual amount of legal work generated. The property post will be permanent and is currently being filled on a day a week basis by a secondee from LSHIM, our property investment managers.

5.0 Implications

5.1 Financial

- 5.1.1 The financial model produced by Grant Thornton has been updated with the latest rental figures, inflation forecast and to reflect the final timings and is included in the Part B report. This will form the baseline for ongoing monitoring of performance both through PIB and as part of budget monitoring and will be updated on a quarterly basis.
- 5.1.2 The 2019/20 Budget included a full-year income contribution of £1.5M from the acquisition. This will be reduced as a result of the delay in completion and will be assessed as part of the Q2 budget monitoring in the light of the revised financial model and overall financial position of the Council.
- 5.1.3 Information in relation to the staffing costs are not yet known but it is anticipated that these can be covered from the Investment and Asset Management costs contained within the financial model.

5.2 Legal Issues (Monitoring Officer)

- 5.2.1 The Head of Democracy and Governance comments that the council employed external legal advisers to undertake the acquisition of the Park and cabinet and council received detailed legal advice on the council's legal powers and risks in entering into this transaction. Further legal advice was provided for the Managing Director and Mayor when exercising their delegated authority to agree to complete the acquisition. As noted in the report PIB will have the role of oversight of the management of the Park in the same way that it has oversight of the other investment properties in the council's portfolio. Once a detailed business plan for the Park has been prepared this will come to cabinet for approval and this will set out appropriate delegations to enable officers to manage the Park on a day to day basis.

5.3 Equalities, Human Rights and Data Protection

Not Applicable

5.4 Staffing

- 5.4.1 An additional staff member will be recruited with a strong commercial background to oversee the performance of our consultants on the Park. This position will be advertised shortly. Whilst a further position to deal with the legal work will also be created

5.5 **Accommodation**

5.5.1 Croxley Park's management suite provides a base for a small number of staff to work from on a hot desk basis on Croxley Park but this facility is paid for out of the service charge budget from the tenants so must only be used by people working on Croxley Park.

5.6 **Community Safety/Crime and Disorder**

5.6.1 Croxley Park has 24 hour security and the road is barriered off at night time with security patrols

5.7 **Sustainability**

5.7.1 Many initiatives are been taken forward to further the green agenda including photovoltaic installations, improved installation to buildings as refurbished and a high BREEAM standard to the new build office block. Transport initiatives such as the bespoke Croxley Park bus service connecting Watford Junction to the Park and a cycle hire scheme have been introduced. WBC will be exploring further options including linking in the Mayor's cycle hub scheme and developing an alternative transport solution in place of the MLX extension.

Appendices

None

Background papers

None