SCARBOROUGH BOROUGH COUNCIL	**REPORT TO THE PLACES AND FUTURES OVERVIEW AND SCRUTINY COMMITTEE** **TO BE HELD ON** **27 OCTOBER**
Corporate Aims People; Place; Prosperity; and Council.	**Cabinet Portfolio Holder** **Cllr Steve Siddons**

REPORT OF: DIRECTOR (NE) – 21/193

WARDS AFFECTED: ALL

SUBJECT: SCARBOROUGH TOWN CENTRE REGENERATION (STUDENT ACCOMMODATION SCHEME)

REASON(S) REPORT REQUESTED:

To implement the following motion:

Motion in respect of the project to redevelop the former Argos building

The Conservative Group on Scarborough Borough Council today call for residents of the Borough's financial interest in the project to be protected by a full review of the business case in light of cost pressures being experienced in the building industry at this current time.

PURPOSE OF REPORT:

To advise the Members of the Overview and Scrutiny Committee (Places and Futures) of the existing contractual provisions contained in the development agreement with Buccleuh Property (Scarborough) Limited.

RISK ISSUES:

- The Student Accommodation Scheme is unviable in light of the cost pressures currently being experienced in the building industry;
- Members are not aware of or assured by the protections contained in the legal agreements with the Developer.

1. INTRODUCTION

1.1. On 12 July 2019 (report ref: 19/151) Council approved the proposals for the redevelopment of the former Argos site on Newborough. The report set out that the redevelopment proposals involve Buccleuch Property (Scarborough) Limited (the Developer) demolishing the existing building on the site, constructing purpose built student and NHS key worker accommodation and ground floor retail space to take its place, and negotiating suitable pre-let agreements for the majority of the new-build space. The Council will then, subject to certain conditions, purchase the completed development with the benefit of satisfactory pre-let agreements.

1.2. Council approved a budget for the Council to purchase the site as well as an overall maximum development budget subject to certain conditions being met by the Developer.

1.3. On 16 June 2020 Cabinet approved entry into the conditional contract for sale and the funding agreement with the Developer to purchase and facilitate the development of the former Argos building (50-59 Newborough and 46-49 Queen Street and 18-20 Market Street, Scarborough) as student, NHS key worker accommodation and associated ground floor retail space.

1.4. On 8 July 2020 the decision was called into the Overview and Scrutiny Committee for scrutiny pursuant to Section 4.6 of the Constitution, Additional Overview and Scrutiny Committee Procedure Rules. The Committee reviewed the Cabinet decision dated 16 June 2020.

1.5. Following a debate of the issues and Member concerns the Overview and Scrutiny Committee resolved to uphold the Cabinet decision.

1.6. On 21 June 2021 the Council subsequently entered into the conditional contract for sale and conditional funding agreement with the Developer.

2. CORPORATE AIMS

2.1 The scheme contributes towards all four of the corporate aims: People; Place; Prosperity; and Council.

3. BACKGROUND AND ISSUES

3.1. There are two legal agreements between the Council and the Developer relating to this scheme: a conditional contract for sale and a conditional funding agreement. Both legal agreements contain a set of conditions which must be satisfied by the Developer before the Council is obliged to buy the

site and before the scheme proceeds and the Council is obliged to fund the development.

3.2. Since the Council and Cabinet decisions and the Council subsequently entering into the conditional contract for sale and funding agreement in June 2021, the Developer has been working to satisfy the various conditions attached to the legal agreements. In advance of the Council entering into the legal agreements the Developer was carrying out this work at risk.

3.3. On 6 October 2021 the Developer submitted a planning application for the scheme and the application was subsequently validated by the Local Planning Authority on 21 October 2021. It is anticipated that this planning application will be determined in November 2021.

3.4. Significant increases in construction costs have been reported in recent months and this may have an impact on the deliverability of this scheme.

3.5. On 2 September 2021 at a meeting of full Council the following motion was proposed by Councillors Phillips and Jeffels:

Motion in respect of the project to redevelop the former Argos building

The Conservative Group on Scarborough Borough Council today call for residents of the Borough's financial interest in the project to be protected by a full review of the business case in light of cost pressures being experienced in the building industry at this current time.

3.6. Whilst the motion was not passed at full Council in view of the closeness of the vote and the seriousness of the issues and concerns raised by Members at the Council meeting, the decision was made to implement the motion as proposed.

4. ASSESSMENT

4.1. As outlined above the legal agreements between the Council and the Developer contain various conditions which the Developer must satisfy before the Council becomes financially committed to the scheme.

4.2. Buccleuch currently owns the development site. The contract for sale sets out the terms and conditions relating to the Council's potential purchase of the site from the developer. The conditions attached to the conditional contract for sale include the requirement for the Developer to obtain satisfactory planning permission for the scheme; secure vacant possession of part of the site; provide various compliance certificates in respect of the building and enter into an agreement for lease with the future tenant of the development containing certain minimum terms including rent and lease duration. These conditions must be satisfied before the Council is obliged to buy the site from the Developer.

4.3. The funding agreement sets out the terms and conditions relating to the construction of the proposed student and NHS accommodation and

commercial space on the site and the Council's funding thereof. The conditions attached to the conditional funding agreement include the requirement for the Developer to have entered into certain contracts for the works on terms approved by the Council which must meet a minimum specification and programme. The final conditions to be satisfied before the scheme can proceed are the Viability and Maximum Price Conditions.

Viability and Maximum Price Conditions

4.4. The Viability Condition recognises that the costs of the scheme will not be known until sufficient planning and design works have been undertaken by the Developer. The Condition aims to provide financial flexibility within the project in light of this cost uncertainty, but more importantly protects the Council's financial interests by assessing the financial viability and projected returns at a future point in time when the estimated costs of the development have been finalised and can be fixed.

4.5. The Viability Condition will ensure that the Council's financial returns can be met through the development and that the overall development costs remain within a maximum price cap; thus providing the Council with a level of mitigation against cost increases such as those currently being experienced within the construction industry.

4.6. The Viability Condition requires the Developer to produce a financial viability appraisal as soon as possible following obtaining satisfactory planning permission. This appraisal will determine whether the Council and Developer's minimum financial criteria have been met and therefore whether the Viability Condition has been satisfied.

4.7. This assessment will be undertaken prior to the construction works commencing and will allow the Council or the Developer to walk away from the deal if the financial appraisal shows that minimum financial returns will not be realised or that the costs cannot be contained within the maximum price cap quoted within the funding agreement. The calculation methodology and level of the Council's minimum financial returns remain in line with those reported to Council in July 2019.

4.8. If the minimum financial returns have been met and the costs remain within the maximum price cap the scheme can proceed; with the Developer then bearing the risk of all cost overruns. The Council's budget for this scheme was set by Council on 12 July 2019 (ref 19/151) and the maximum price contained within the funding agreement aligns with that budget.

4.9. As part of the Viability Condition the Developer must provide evidence to support the figures included within the financial viability appraisal on an open book basis, to provide the Council with assurance that the maximum price is reasonable. The funding agreement includes provision for the scheme's costs to be independently verified by the Council using a third party cost consultant.

4.10 The viability appraisal will take into account the rental income achievable from the student and key worker accommodation, based on the Agreements for Lease in place, and the market rents achievable from the commercial units. These will be compared against the anticipated borrowing repayments and interest costs that the Council will incur, based on the scheme costs included within the appraisal.

4.11 The viability appraisal calculation will be modelled over a 10 year period to reflect the initial duration of the head lease. The borrowing rates included within the appraisal will be based on a 40 year repayment term, with the interest rates fixed at the time of preparing the viability assessment and the Council taking the risk on interest rate fluctuations that arise between that date and the time that the borrowing is taken out.

4.12 To meet the Council's minimum financial return the appraisal will need to demonstrate that the net annual surplus over the 10 year period will deliver a minimum 0.5% per annum average return on investment for the Council after allowing for financing costs and borrowing repayments.

4.13 If the scheme is viable for both parties the funding agreement between the Council and the Developer becomes unconditional and the Developer will commence the development works. The costs shown within the final viability appraisal are fixed from the Council's perspective and the risk of cost overruns lies with the Developer and its contractors. The Developer and the Council will agree a schedule of milestone payments for the funding of the scheme during the course of the works.

4.14 If the scheme is not viable then the scheme will not proceed. It should be noted however that if the Developer has satisfied the conditions attached to the Contract for Sale the Council will have been required to purchase the site and will be responsible for any on-going costs associated with the property.

5. IMPLICATIONS

5.1. Policy Implications

There are no direct policy implication arising from this report.

5.2. Legal Implications

This report contains detail of the conditions contained in the legal agreements between the Council and the Developer. The legal implications associated with the scheme itself including the risks are contained in the previous Council and Cabinet reports (refs 19/151; 20/114).

5.3. Financial Implications

This report contains details of the viability condition which is contained in the funding agreement between the Council and the Developer. The financial implications associated with the scheme itself including the risks are contained in the previous Council and Cabinet reports (refs 19/151; 20/114).

5.4. Equalities and Diversity Implications

There are no direct Equalities and Diversity Implications arising from this report.

5.5. Communications

Note that it is intended that a further report containing a full review of the construction costs associated with the scheme will be brought back to this Committee at the viability condition stage. Assuming the planning application is determined in November 2021, it is anticipated that this report will be brought to the Places and Futures Overview and Scrutiny Committee early in 2022.

5.6. Planning Implications

There are no direct Planning Implications arising from this report however it is noted that the Developer has submitted a planning application for the scheme which will be determined by the Local Planning Authority in due course.

5.7 I have considered whether Staffing Implications, Crime and Disorder Implications, Health and Safety implications, Environmental implications from this report and am satisfied that there is no identified implication that will arise from this decision.

Signature

Nick Edwards
Director

Background Papers:
Please give details of all publicly accessible (non private) background papers applicable to the report.

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IF YOU HAVE ANY QUERIES ABOUT THIS REPORT OR WISH TO INSPECT ANY OF THE BACKGROUND PAPERS, PLEASE CONTACT THE AUTHOR.