

DECISION RECORD

July 2018

Subject

Approval of the acquisition of 15 Church Street (Mama Mia's) and 16 Church Street (Shades) properties.

Type of decision (Key/Non Key)

Non key – Self funded business case and external grant funding spend.

Description**Council Commitment to Positive Intervention in Church Street**

The Council is committed to regenerating the Church Street Innovation and Skills Quarter (ISQ) area through public realm improvements, business/property assistance and active vacant and/or underused property acquisition on Church Street and Church Square.

With regard to public realm improvements the joint Finance & Policy and Regeneration Services Committee on 27th March 2017 agreed to:

- (i) The commencement of construction work on the Church Street Innovation and Skills Quarter (ISQ), subject to confirmation of planning approval and the formal award of grant funding from Tees Valley Combined Authority (TVCA) and the Heritage Lottery Fund.
- (ii) Allocate funding from the Regeneration Projects fund to support the overall cost of the scheme and approved the designs and funding for the Church Street redevelopment works

These public realm works were subsequently commenced and at July 2018 they were substantially complete.

Public realm improvements contribute to overall appearance and marketability of the ISQ area but it is crucial that individual private landlords and businesses are encouraged to improve the appearance of their property at the same time. In order to assist with this in October 2017 the Heritage Lottery Fund (HLF) gave HBC permission to start the Townscape Heritage Scheme (THS) in Church Street Conservation Area. The THS is primarily a grant funding scheme which covers 3 categories:

- (1) Priority Buildings. Pulse (12-26 Church Street) and Scarletts (22-23 Church Street) with an available funding package of £350,000.
- (2) Building Grants. A small building repair grant scheme with an available budget of £120,000.
- (3) Shop Front Grants. Grant scheme to fund repair and reinstatement of traditional shop fronts with an available budget of £75,000.

As the THS is delivered over the next 2 years to 2020 this will assist with the individual improvements of buildings where there is a willing land/business owner and where redevelopment is economically viable.

Church Street Property Intervention

There are several properties in the ISQ that are long term vacant, where the land/business owner has not progressed redevelopment and these buildings are having a significant detrimental impact (in terms of visual appearance, health & Safety, anti-social behaviour, enforcement responsibilities from the Council and deterring investment in adjacent properties) on the wider ISQ area. Where such instances occur and there is no likely prospect of the land/business owner bringing forward development the Council will seek to intervene and acquire and redevelop using Council and external public funding along with private investment from development partners and local organisations. Two such properties are:

- (1) 15 Church Street (Mama Mia's)
- (2) 16 Church Street (Shades)

Bearing in mind the significant detrimental impact they are having on the ISQ area the Council is seeking to acquire both properties from private ownership.

Church Street Land and Property Asset Market Research

The Council commissioned a strategic land and property review on the ISQ area in February 2018; carried out by independent property consultants Cushman & Wakefield (C&W). The C&W report provided an overview of the key land and property opportunities within the ISQ area and importantly the likely drivers of end user/market demand over the short-medium term. It goes further to provides a high level of assessment of a number of potential interventions/projects that could be delivered to achieve the desired degree of transformational change, with next steps to delivery set out. The C&W report is explicit in that it identified 15/16 Church Street as key assets within the ISQ area and goes further to identify Shades as a priority asset which requires intervention and investment. In summary the C&W report identified in the ISQ area:

- 1) New office potential. Opportunity for the provision of the right type of serviced/managed start-up (as per the emerging BIS scheme) and grow on space to meet expanding business needs. This could involve the development of additional small and flexible workspace/co-working space to support both start-up businesses.
- 2) New retail/leisure potential. Key to the future of the ISQ's retail/leisure market potential is establishing increased levels of footfall and dwell

time. Active redevelopment of Shades for a retail/leisure use will go some way to achieving this aim.

- 3) New residential potential. Identified need for smaller units, live/work units, affordable housing and student accommodation as the local colleges expand in the future.
- 4) Education potential. The ISQ is a growth area for local colleges and there will be potential to other flexible teaching, assembly, office and leisure staff to cater for the increased demand.

With specific regard to 15 and 16 Church Street the C&W report specifically highlights Shades as a priority building which requires intervention and suggests Mama Mia's could be acquired as a going business concern in the short term. The Shades building is recommended for acquisition by the Council and refurbished and brought back into use with the partnership support of key local businesses and colleges brought on board to be part of the development.

The Council is therefore following the specific recommendations of the independent report in terms of acquiring and bringing the buildings back into use and offering a proposed end use (retail, commercial, leisure and residential) post acquisition that is specifically highlighted as future ISQ growth potential sectors in the future.

The details of the properties are set out below:

15 Church Street (Mama Mia's)

The property comprises a 3 storey mid terraced building originally constructed in the second half of the 19th century located towards the lower end of Church Street in an area of mixed uses including licensed premises, restaurants, takeaways, office and residential.

It adjoins the Listed pub Shades, which is in the same ownership.

The property is constructed of rendered masonry, under a replacement pitched concrete tile main roof with flat mineral felt roofs to rear offshoots. The ground floor has a timber stall riser and plate glass display windows and a recessed timber shop door. A further ground floor entrance provides access to the first and second floor residential accommodation.

The property has been valued at £30,000 on the open market in its current condition and the Council has agreed an acquisition value of £140,000 with the private owner. The proposal is to acquire, undertake refurbishment and bring back to the market as:

- Ground floor: 1 x retail unit with potential uses of A1, A2, A3, A4, A5, B1a, D1, D2 and some Sui Generis.
- 1st floor: 1 x one bedroom flat which will be delivered as an affordable unit.
- 2nd floor: 1 x one bedroom flat which will be delivered as an affordable unit.

It is estimated that post completion of the repair works and occupation of the retail and residential elements the building could be valued at £100,000.

16 Church Street (Shades)

Shades Public House is a Grade II listed building situated on Church Street, which is a conservation area. The building is a mid-nineteenth century three storey end of terrace property in art nouveau style.

The ground and first floors have been altered to create open floor plates and incorporate bar areas. The second floor previously accommodated a residential flat.

The whole property internally and externally is in significant disrepair and is unsafe in places, with hoarding erected around the perimeter to protect the public. The property has been vacant for a number of years and has fallen into significant disrepair. Problems with the building include dry rot, wet rot, and evidence of water ingress throughout. Ceilings and floor are damaged and there are likely to be some structural issues.

The property has been valued at £40,000 on the open market and the Council has agreed an acquisition value of £300,000 with the private owner. The proposal is to acquire, undertake refurbishment and bring back to the market as a leisure/education/training/retail use with the support of significant external grant funding in partnership with local business and partners.

£308,000 grant funding has gone through due diligence and has been agreed with the Tees Valley Combined Authority (TVCA) to be used for the acquisition of the building from a private landowner. The Council has already physically received this money from the TVCA and there is no uncertainty around the award; the Council is just waiting to spend it on the acquisition. As part of the agreement with the TVCA the Council has agreed to a match funding arrangement where the Council is committing £140k (which is the funding being used for the Mama Mia's property acquisition). With regard to the subsequent redevelopment costs options and funding opportunities are currently being explored with local businesses and partners and will be progressed post acquisition. The Council is currently undertaking the relevant surveys but will not know the full situation until after it has acquired the property.

It is estimated that post completion of the repair works the building could be valued at £240,000 and post full redevelopment works and occupation by businesses approaching and aspirational value of £550,000.

The acquisition and subsequent redevelopment of the two properties will have a significant positive impact on the immediate area and wider ISQ; encouraging further investment in the adjoining private properties and removing the building from the Historic England "Heritage At Risk Register".

External Challenge

Prior to progressing the acquisitions, in order to get an independent audit opinion on the acquisition of the properties the Chief Executive and the Director of Finance and Policy met with the Council independent auditors (Mazars) and they raised no concerns with regard to the acquisition and the proposed purchase prices being above market value.

Alternative Options Considered

In addition to the proposed purchase by agreement detailed in the previous paragraphs there are 3 alternative options which can be considered by the Council.

(1) No Direct Intervention

The Church Street area has been in economic decline for a number of years which has resulted in many vacant and/or underused units throughout the street. These properties, particularly 15 and 16 Church Street, are not being developed due to an unwilling land/business owner or because private development is not deemed to be economically viable.

15 and 16 Church Street are both in the same ownership and the owner has historically failed to invest in the buildings and only takes action when prompted/threatened by the Council. With regard to Shades the Council has consistently requested that the owner undertake vital works to the fabric of the building bearing in mind its Listed status. The owner did not undertake these works voluntarily and as a result the Council unilaterally had to undertake the urgent works else the building would have been significantly damaged. If the Council did not seek to acquire the properties the situation would continue indefinitely (perhaps resulting in the loss of a heritage asset in the Listed Shades building) as the owners appear to have no desire to develop/invest. This option is not recommended as it would have a detrimental impact on the regeneration outcomes the Council is trying to achieve and continue to negatively impact on existing local businesses.

(2) Renegotiating an Acquisition Price Based on Market Value

The market value for 15 Church Street is £30,000 and 16 Church Street is £40,000 in their current state. The Council has consistently negotiated with the owners to acquire at the market value but the owner is not willing to dispose at that value and is comfortable with continuing the current status quo of them being vacant, underused and in the case of Shades approaching dereliction. The owner has a substantial portfolio of properties in Hartlepool and many are in a similar condition to the two on Church Street; including the Odeon on Raby Road and the Longscar Centre at Seaton Carew. The Council has sought to prompt development/investment at the other properties and discussions around acquisition at market value but these have been consistently rebuffed by the owners.

Through protracted negotiation the Council has agreed with the owner to dispose at the value of £140,000 for 15 Church Street and £300,000 for 16 Church Street. Whilst both acquisitions are above the expected market value it is the least value the owners would be willing to accept to dispose.

If the Council were to seek to re-negotiate the price, the owner would not engage and the buildings would remain vacant in the long term; this has also been the consistent approach of the owner on their wider property portfolio. Therefore, this option is not recommended as if the Council did not intervene and acquire then the significant detrimental impact they are having on the ISQ would continue.

(3) Compulsory Purchase Order

Whilst the principle of acquisition by agreement has been achieved at the value of £140,000 and £300,000 the Council could look to acquire the properties through a Compulsory Purchase Order (CPO). In 2016 the Council progressed with a CPO on the Longscar Centre at Seaton Carew (after discussions around acquisition by agreement failed), but was ultimately unsuccessful. There are established risks in progressing a CPO:

- (a) Costs. The Longscar CPO cost the Council approximately £222k to prepare the case (officer time) and pay for legal fees, professional fees, witness fees, Planning Inspectorate fees and background documents and evidence base reports. These costs did not include the actual acquisition of the building (at between £75-150k estimated value) and any potential legal/compensation costs to the owner even if the Council were successful in the CPO. The total estimated cost if successful could have been between £300-£500k, to acquire through the CPO process. It is expected that any CPOs on the 15 and 16 Church Street would be similar in terms of nature and cost to that of the Longscar CPO; although exact figures difficult to assume as each CPO is different depending on the nature of the CPO.
- (b) Losing. Notwithstanding the potential costs there is always the possibility of losing the CPO if the owner presents a compelling case to the independent Planning Inspectorate; as was the case with the recent Longscar CPO. In the event of the Council losing the CPO the following would be relevant:
 - Back to square one. The Council would have incurred significant time and costs in bring the CPO and these costs would have been abortive with no right of appeal. The money spent could have been used to acquire the properties by agreement.
 - Potential Costs. The Council may be subject to additional legal and compensatory costs depending upon the nature of the decision from the Planning Inspectorate.
 - Reputational Risk. Bearing in mind the recent Longscar CPO decision the Council would be associated with another failure; albeit at the hands of third party decision maker.
 - Relationship Risk. Another adversarial CPO would further strain relationships with the owners and potentially harm future development opportunities and/or acquisitions by agreement

discussions going forward; bearing in mind their existing property portfolio.

- (c) Time. CPO's traditionally take up significant staff resources and also time; time where no progress is being made on the development of the properties in question. Using the recent Longscar CPO as an example, from start to finish the CPO took approximately 24 months to complete. Even if the Council were successful through the CPO this would be nearly 2 years of "wasted" time where the Council could have legitimately started work to bring the empty properties to the market and drive regeneration forward.

In summary therefore the most appropriate course of action is to progress with the property acquisition by agreement.

Financial Considerations

Table 1 sets out the main costs and funding identified, including confirmed grant funding and external grants which the Council is actively pursuing but confirmation will not be given until after acquisition.

Table 1: Capital Costs and Funding Requirement

	Mamma Mias £000	Shades £000
Expenditure		
Purchase Cost	140	306
Renovation	228	2,020
	368	2,326
Funding		
TVCA Grant	(24)	(308)
HLF Conservation Deficit Grant (Note 1)		(1,490)
HE Grant (Note 2)	(70)	
THS Grant (Note 3)	(30)	
Section 106 (Note 4)	(101)	
	(225)	(1,798)
Net Capital Cost to be Financed	143	528
Decision Record Funding		
Prudential Borrowing Required	(143)	(510)
To be met from Departmental Outturn/reserves		(18)

Note 1: HLF Conservation Deficit Grant is being pursued by the Council. Whilst the Council is in positive dialogue with the HLF, prior to acquisition, the HLF will not make a decision on whether the funding bid is successful. See Development and Financial Risk Assessment Going Forward section for detail.

Note 2: The Homes England (HE) Grant (formerly HCA) is being pursued by the Council. An indicative amount of £35k per unit is being sought. The HE will not make a decision on whether the funding bid is successful prior to the acquisition being progressed; however the Council has historically been successful in securing grant on affordable housing schemes.

Note 3: The Townscape Heritage Scheme is managed by the Council. The Council will bid for the specific grant funding to contribute towards the cost of building and shop front works.

Note 4: The S106 funding is the amount required to balance the budget for the residential HRA component of the Mamma Mia's works after allowing for the borrowing that can be supported from net rent income. The S106 monies are available for affordable housing provision and legitimately fit with the proposed scheme.

Table 2 shows the amount of borrowing that can be supported based on the projected annual rental income for Mamma Mia's.

Table 2: Business Case for Prudential Borrowing – Mamma Mia's

	HRA	General Fund	Total
	£	£	£
Income			
Rent - Shop	0	(5,000)	(5,000)
Rent - Flats	(5,664)		
Voids and Bad Debt	566	0	566
Total Income	(5,098)	(5,000)	(10,098)
Expenditure			
Major Repairs Allowance	2,000		2,000
Reactive Repairs	1,000		1,000
Management	1,000		1,000
Insurance	250		250
Total Operating Expenditure	4,250	0	4,250
Surplus available to fund Borrowing Costs (A)	(848)	(5,000)	(5,848)
Borrowing Capacity Supported by Surplus (A)	29,228	118,000	147,228

As shown in the table above the borrowing capacity is £147,228 and this exceeds the funding requirement to balance the capital budget by £4,000. The HRA component includes the operating costs of letting the flats whereas the General Fund component relates to the shop for which the only expense to the Council will be the annuity loan repayments over a 40 year period.

Table 3 below shows the business case for Shades.

Table 3 : Business Case for Prudential Borrowing – Shades

	Total	Comments
Commercial Rent - Prudent Estimate	(25,000)	Between £25k to £50k
Borrowing Costs	22,000	Based on Borrowing of £510k
Surplus	(3,000)	

Note that based on a funding shortfall to be met from prudential borrowing of £510,000 the annual loan repayment will be £22,000 which is less than the most conservative estimate of future annual rent income between £25,000 and £50,000.

Sensitivity analysis of the impact of an increase in renovation costs above the £2m indicative estimate has shown that the cost of an additional £500,000 met from borrowing would result in an additional annual repayment cost of £22,000. However, as set out in section (ii) below there is a possibility that any increase in expenditure could be met from the HLF Conservation Deficit Grant and therefore additional borrowing may not be required.

Development and Financial Risk Assessment Going Forward

The business case shows that the acquisitions can progress however there are defined risks in terms of (i) capital expenditure, (ii) availability of external funding and (iii) ongoing operational budget and maintenance. These issues and mitigation measure are set out below:

- (i) **Capital Expenditure.** Key risks are that the renovation costs both in terms of contracts and fees are greater than the indicative costs reflected in the business case. The indicative estimates reflect work completed to date to assess the works required. However, there is potential for uncertainty and unforeseen costs which will only become apparent once the projects start post acquisition. In relation to Mamma Mia's any capital costs increase will need to be funded from section 106 funding to avoid an additional pressure on existing HBC budgets. The position in relation to Shades is potentially more risky (with it being a Listed Building) and the Council is currently undertaking design options analysis and this will not be completed prior to the building being acquired. An estimated figure of £2m is assumed for the refurbishment works; but until a comprehensive design scheme is developed exact refurbishment costs are not yet known. Whilst this is an identified risk it is anticipated that any potential increase in renovation costs would be covered by HLF Conservation Deficit Grant funding as the funding scheme specifically caters for such instances (see point (ii), as finalised costings will be reflected in HLF's funding approval).

(ii) Availability of External Funding. With specific regard to the Mama Mia's residential element, if the Council were unsuccessful with the HE Grant the Council could legitimately use S106 funding to fill the void so there is less of a risk going forward. With specific regard to the acquisition and development of Shades the HLF Conservation Deficit funding is a significant component of the redevelopment scheme funding. The Council is currently in advanced discussions with the HLF for such funding but as yet no decision has been made. In the future, if unsuccessful, the Council could be in a position whereby the Shades building is acquired but there is insufficient external funding to redevelop the building in the short term and the Council would be liable as the owner going forward. This would make the Council liable for the ongoing minor maintenance, major repairs and security costs along with Council Tax for the building and the specific costs are not yet known. Whilst this is an identified risk the Council has an excellent track record of securing HLF funding; the THS and Shades urgent works grant being prime examples. In order to mitigate the risk going forward the Council has appointed Cushman and Wakefield as an expert consultant to professionally draft the application and prepare the economic viability assessments. Council officers have consistently met with the HLF officers throughout 2017/18 and the HLF are keen for the Council to submit a bid; realising the current dire situation and the potential significant positive benefits of acquisition and renovation. The HLF bid will be submitted by 16th August 2018 with an anticipated answer most likely in December 2018. Should the Council be successful a second round application would be required and it is anticipated that this would be required by autumn 2019. If in the unlikely event that HLF funding was not successful then the Council could further mitigate the risk by looking to:

- a) The TVCA for additional capital funding; but there is no certainty around whether the development would meet TVCA funding criteria and expected outputs going forward.
- b) Finance the redevelopment (circa £2m) by using prudential borrowing (for which there is no identified budget or funding decision made). For reference, the indicative costs of prudentially borrowing £2m is an annual commitment of £85k.
- c) Dispose the building to a willing/appropriate 3rd party to take the development forward. It must be appreciated that (c) is unlikely bearing in mind the significant redevelopment costs and a 3rd party not willing to take a risk on the building without Council assistance/investment.

(iii) Ongoing Operational Budgets and Maintenance. The identified risks are:

- a) Loss of rental income through voids as the business unit may prove not commercially attractive to a tenant; and there is no legal agreement in place for a prospective tenant at this stage. Whilst this is a risk the Council is currently in positive discussions with the local business Cameron's and the

Cleveland College of Art and Design with regard to them taking a lease on the Shades post acquisition and renovation. These discussions are progressing in a positive manner and it is anticipated that lease arrangements will be agreed once acquisition has been completed.

- b) Loss of projected income as the £5k assumed annual rental income from the Mama Mia's commercial unit and the assumed £25k annual rental income from Shades may not be achieved due to general market conditions. Again as with (iii)(a) the Council is confident that there is sufficient business interest in the properties post renovation.
- c) Loss of rental income through bad debt "right offs" on the commercial and residential element of the developments.
- d) Higher than forecasted major and reactive repair costs.

Whilst there are defined risks attached to the acquisition and renovation/refurbishment the Council has identified mitigation where possible and the overall risk is assumed to be acceptable. The greater risk going forward, not only for the Council but also the wider ISQ area is if no direct action is taken to intervene. Intervention, acquisition and redevelopment, working with key business partners, will provide a significant improvement to the physical and economic performance of the Church Street area bringing vacant/underused key properties back into vibrant use. This will build upon the regeneration benefits achieved by securing the new college buildings at the bottom of Church Street and the environmental improvements to Church Street/Church Square.

Nature of Delegation being Exercised

This decision is made in accordance with The Constitution Part 4 Rules of Procedure Page 144 para 4.6 which states:

"The Council delivers a range of projects which do not require funding from the General Fund budget and are funded from either specific grant funding or specific income streams. It is necessary, to ensure good financial management and the making of timely business case decisions, where in the professional opinion of the Chief Executive, Director of Finance and Policy and Chief Solicitor, to delegate decision making where there is a robust and self funded business case to do so and which does not add a recurring financial commitment to the General Fund budget. Delegated authority shall be exercised by the Chief Executive, Director of Finance and Policy, and Chief Solicitor in consultation with the Chair of the Finance and Policy Committee. This delegation will also apply where revisions are needed to existing business cases but where such revisions still meet the objectives of the original business case and the tests above are satisfied. Details of business cases approved, or amendments to previously approved business cases, shall be reported to the next scheduled meeting of the Finance and Policy Committee for information."

Decision




- (1) To approve the purchase of 15 Church Street (Mama Mia's), which will be funded from grant funding and section 106 contributions;
- (2) To approve the purchase of 16 Church Street (Shades), which will be funded from grant funding.
- (3) To note that detailed business case reports on the development of 15 and 16 Church Street will be submitted to a future Finance and Policy Committee meeting outlining the strategy for completing these developments, including funding it is anticipated will be secured from HLF and potential prudential borrowing which may be required; which will be funded from rental agreements secured for the use of these properties. To also note that any required potential Prudential borrowing will need to be approved by full Council.

Reason for the Decision

The reason for the decision is to intervene and assist in the regeneration of the Church Street area by acquiring two key strategic vacant/underused buildings and bring them back into use.

Conflict of Interest(s)

None known

- (1) **NAME:** GILL ALEXANDER
POST: CHIEF EXECUTIVE
SIGNED: 
DATE: 3/7/2018
- (2) **NAME:** CHRIS LITTLE
POST: DIRECTOR OF FINANCE AND POLICY
SIGNED: 
DATE: 3/7/2018
- (3) **NAME:** DENISE OGDEN
POST: DIRECTOR REGENERATION & NEIGHBOURHOODS
SIGNED: 
DATE: 3/7/2018

(4) NAME: HAYLEY MARTIN
POST: ACTING CHIEF SOLICITOR

SIGNED: 

DATE: 4/7/18

In consultation with:

(5) NAME: CHRISTOPHER AKERS-BELCHER
POST: CHAIR OF THE FINANCE AND POLICY COMMITTEE

SIGNED: 

DATE: 3/7/18

(6) NAME: KEVIN CRANNEY
POST: CHAIR OF THE REGENERATION SERVICES COMMITTEE

SIGNED: 

DATE: 3/7/18

