

Item No.	Classification: Open	Date: 7 July 2010	Meeting Name: Cabinet
Report title:		Canada Water Retail Option	
Ward(s) or groups affected:		Rotherhithe Ward	
From:		Cabinet Member for Finance and Resources	

FOREWARD – RICHARD LIVINGSTONE, CABINET MEMBER FOR FINANCE AND RESOURCES

1. This report asks the Cabinet to approve the taking up of a 250 year lease of retail units at the new square adjacent to the Canada Water library (site B2) and note the option to take up a similar lease for further units next to Canada Water tube station (site A3). The recommendation would require the council to take up the advantageous option available to Southwark as part of the sale of the land to Barratt Homes.
2. The recommendation has three principal benefits to the local authority:
 - the preferential terms for retail space at what is likely to be near the bottom of the market in a strongly marketable location
 - the potential to generate a new revenue stream at a time when revenue funding from government is likely to contract
 - the tighter control of lessees of the units than planning regulations allow through ownership of the premises. This added assurance to the local community is important in a sensitive site such as this
3. I have also looked at the risks of the proposal and consider that the analysis in that section of the report gives sufficient assurance for the authority to proceed with the lease.
4. The option notice period on site B2 expires on 15 July 2010 and so it is important that the Cabinet consider the proposal at its 7 July meeting.
5. This proposal represents good value for money for the authority and I am therefore asking the Cabinet, after consideration of the officers' report set out from paragraph 8 onwards to approve the recommendation set out below.

RECOMMENDATIONS

The cabinet is asked to:

6. Give approval to the completion of a 250 year lease of the retail units in phase B2 of the Canada Water development, located as shown on the plan attached as plan 1, and to delegate to the Head of Property authority to negotiate the option price and final form of lease provided that they represent best consideration.
7. Note that in due course a further feasibility will be prepared to consider the option to purchase the long lease of the retail units in phase A3 of the Canada Water Development and that an appropriate allowance will be put into capital programme

for financial year 2012/13.

BACKGROUND INFORMATION

8. The council has the opportunity to underpin its investment in the new Canada Water library and plaza by exercising an option to buy from Barratt Homes a long lease in the retail space being built at sites A and B. Ownership of these assets will allow the council, through its letting policy, to enhance the setting for the new library, take advantage of the discounted purchase price for the shops and benefit from the anticipated rise in property values. Subsequently the council will have the option of selling the improved asset at any time to support the capital programme.
9. On 5th April 2005 a strategic development agreement was signed between the council and British Land Canada Quays Ltd (BLCQ) for the regeneration of the Canada Water area. The agreement required BLCQ to create a masterplan, which was approved by Executive on 11th October 2005.
10. After an initial period of public consultation and masterplanning the project is now in its delivery phase. This will see the area take full advantage of its central location and impressive public transport infrastructure (which is being further improved) to emerge as a renewed, vibrant and exciting residential quarter within inner London.
11. The philosophy behind the regeneration has been to follow a multifaceted approach in order to produce a sustainable community. One key element of this is the council's investment in the iconic Canada Water library, which along with the adjoining plaza will create a new civic heart for Rotherhithe.
12. This community building approach is echoed in the emerging Area Action Plan (AAP) for Canada Water. The AAP sets out a vision for the area as one that is family friendly, which has at its core the facilities of a commercial district that will be enlarged and re-energised as a more traditional town centre.
13. During the life of the AAP it is anticipated that the commercial core will expand with the construction of at least 2,500 new homes and up to 35,000 sq m of additional retail space. This activity will create a major retail destination made possible by the increased local population and the excellent public transport infrastructure. For example the Canada Water tube transport node (which sits directly underneath the new civic plaza and currently caters for something of the order of 31,000 exits and entries a day) will offer: direct access via the Jubilee line to the north of the borough; the second phase of the East London Line extension will open up the centre of the borough; and, a number of routes pass through the adjoining bus station.
14. The regeneration is at an exciting stage with significant activity on the ground:
 - a) The library and plaza are due to complete construction in the middle of 2011.
 - b) 232 new homes have been completed on site B (64 affordable)
 - c) 385 new homes are under construction on site A (113 affordable) with a further 283 homes to follow (57 affordable).
 - d) Site C has been granted planning consent for a mixed use scheme of approximately 11,000 sq m of commercial space and 430 homes (116 affordable).
 - e) Outline planning consent has been granted for a mixed use scheme on the Leisure Park site for around 16,000 sq m of commercial space, 509 homes (128 affordable) and 123 room student accommodation.
 - f) British Land has recently invested in the Surrey Quays Shopping Centre.

15. This level of investment will bring about a step change in commercial activity in Canada Water and it is anticipated will enhance the value of council property holdings.
16. The council sold sites A and B to BDW Trading, known as Barratt Homes, by way of an agreement dated 21 December 2007. Barratt are developing the two sites in five phases (phases B1, B2, A1, A2 and A3 in that order). The retail space is around 2,000 sq m and is located within phases B1, B2 and A3.
17. The agreement, which was authorised by Executive on 18 December 2007, includes an option for the council to take a 250 year lease of the retail space. The key terms of the option are; at the implementation of development of a phase Barratt serves on the council notice of the option to purchase the retail units in that phase. The council then has 18 months to confirm if it wants to exercise the option. The price is at a fixed rate per sq foot of gross external area.
18. The intention in negotiating the option was to ensure that the units are managed and operated in a way that supports the regeneration objectives and provides financial benefit for the council. The option price was fixed at a level that it was hoped would be financially advantageous to the council.
19. The first phase of the development, phase B1 has been completed. The option notice for the B1 retail expired on 28 February 2010 and for the reasons set out below was not taken up. Phase B2 is nearing completion and the retail option notice period expires on 15 July 2010. For the reasons set out below it is recommended this option be exercised. Phase A3 recently obtained planning consent but work has not started on site and no notice has been served. At the appropriate time a business case will be prepared to consider the benefit of exercising that option.
20. Since entering into the agreement to buy the land Barratt has appointed Peverel OM Ltd as managing agents for the development. If it is agreed to exercise the option and take a lease this will be by way of a tri-partite agreement involving the council, BDW Trading and Peverel.

KEY ISSUES FOR CONSIDERATION

Vision for the Canada Water Town Centre

21. Ownership of these assets will assist the council in furthering its regeneration plans for Canada Water. It will mean that we can create an appropriate setting for the new civic plaza and library and respond to local aspirations to expand the night time economy.
22. Once the area is established the council would have the option of disposing of its ownership with minimum risk to its regeneration objectives.

Valuation of the Retail Units and Business Case

23. The closed report on this cabinet agenda contains details of the valuation of the leasehold interest and the business case. It concludes that the option over the retail in site B2 should be exercised and that the option over the retail in site A3 should be considered in detail when it has been constructed.

Risk analysis

24. The risks identified with purchasing the units are summarised below:

- (a) That a suitable tenant can not be found – this will mean the expected rent roll will not be achieved and the payback period not met.

Canada Water is a fast developing area and it is expected that investment performance will improve as further regeneration materialises.

Canada Water is already attracting considerable investor interest. There is reason to believe that this will continue and that suitable occupants will be found. This view is backed up by consultants CBRE and this risk is not considered to be of high likelihood.

- (b) Liability for fit out – developers usually provide shell and core for new retail units with tenants responsible for the fit out. It is not unusual for tenants to negotiate a rent free period to cover some or all of the cost of the fit out.

Advice has been taken from retail letting agents at CBRE on the treatment of fit out costs and this is reflected in the business case.

- (c) That there is a delay in finding a suitable tenant – the considerable construction activity in the area may put off prospective tenants who may preferred to wait until the building work; which is also creating the homes for their customers, is finished.

It is undoubtedly true the area will be inconvenienced by building work for some time to come. However it must be kept in mind that the Canada Water tube station is the main driver of footfall in the area and that in 2008 it generated over 11 million exist and entries. So there is already a strong potential customer base for the units.

It is also clear that a number of investors are active in the area and it might be expected that tenants will view these new, good quality units as a chance to get in at the bottom of the market in an up and coming area. For these reasons this risk is not considered to be of high likelihoods.

Policy implications

25. This report flows directly from previous decisions made by the Council in December 2007 in respect of the sale of sites A and B at Canada Water and the option to take a lease of the retail space.

26. Taking a lease of the retail units would mean that the council has control of the letting policy. The units could then be managed in such a way as to support the council's wider regeneration aspiration for the area; for example by enhancing the new civic plaza being created at Canada Water and by creating an appropriate setting for the new Canada Water library.

Community Impact Statement

27. Should the council choose to exercise the option over the retail space at Canada Water it will afford the opportunity to enhance the new civic plaza being created in the vicinity. This will be to the benefit of all of the local community.

Resource Implications

28. Once the council buys the lease of the units, their day to day management as part

of the council's property investment assets will pass to the investment portfolio team within Property Services.

Financial Implications

29. The closed report on this cabinet agenda contains details of the financial implications of exercising the option to take the retail space and identifies appropriate funding sources from existing budgets.

Consultation

30. There has been internal consultation with officers in finance and property departments.

SUPPLEMENTARY ADVICE FROM OTHER OFFICERS

Strategic Director of Communities, Law & Governance

31. The cabinet is recommended to approve the exercise of the option to take a 250 year lease of the retail units in the completed Phase B2 of the Canada Water development. Section 120(1) of the Local Government Act 1972 (the "Act") enables a principal council to acquire by agreement any land, whether situated inside or outside their area, for the purposes of:

- a) any of their functions under that or other enactment, or
- b) the benefit, improvement or development of their area.

32. Section 120(2) of the Act enables a principal council to acquire any land for any purpose of which they are authorised by that or any other enactment to acquire land, notwithstanding the land is not immediately required for that purpose; and until it is required for the purpose for which it was acquired, the land acquired may be used for the purpose of any of the council's functions.

33. Paragraph 18 of this report notes the intention of council officers in negotiating this deal was to enhance the regeneration of Canada Water town centre. Paragraph 39 (of the closed report) notes that the exercise of the option will be for the benefit, improvement and development of the Canada Water area, and therefore the requirements of Section 120(1) of the Act are fulfilled.

34. The cabinet is therefore advised that there are adequate powers available to the Council to exercise the option and take the lease of the completed retail units at Phase B2.

35. We understand that the final form of lease has not yet been agreed and is subject to ongoing negotiation. Eversheds LLP are providing legal advice to the Council on this matter. The first recommendation of this report is that the Head of Property be authorised to agree any necessary amendments to the lease.

Finance Director / Departmental Finance Manager

36. This project will be funded via a revenue contribution to capital and be financed by a release from the regeneration and development reserve. The longer term business model is scheduled to deliver sustained revenue sources of income for the council from the retail units which can be used for a combination of reinvestment in regeneration across the borough and replenishment of the capital reserve. In the possible future event of asset disposal, this will generate a capital

receipt for the corporate resource pool.

Portfolio Business Manager, Property Services

37. The units will be held in the managed property holding account and managed as part of the commercial property portfolio. It is understood, if approval is given, the Council will buy long leases of the ground floor retail units which will let at open market value to prospective occupiers.
38. Barratt has provided a form of lease for the retail units. Further negotiations with Barratt and their legal advisers concerning the lease covenants are recommended. A critical area of negotiation is the Council's ability to underlet or assign the units without any restriction. The Barratt sale contract agreement of 21 December 2007, clause 12.1 states that there should be no restrictions on assignments or under lettings on the open market. The Property Portfolio Business Manager's team will lead further negotiations on the lease.
39. The acquisition of the 250-year leases by the Council will provide a substantial revenue stream which will increase over time and continue to improve the area.

BACKGROUND DOCUMENTS

Background Papers	Held At	Contact
Canada Water retail option case file and business case	Regeneration and Neighbourhood, Canada Water Team, 160 Tooley Street	Bunmi Olafare 020 7525 5422

APPENDICES

No.	Title
Appendix 1	Plan of sites A and B at Canada Water

AUDIT TRAIL

Cabinet Member	Cabinet member for Finance and Resources	
Lead Officer	Richard Rawes	
Report Authors	Tim Thompson/James Oates	
Version	Final	
Dated	29 June 2010	
Key Decision?	Yes	
CONSULTATION WITH OTHER OFFICERS / DIRECTORATES		
Officer Title	Comments Sought	Comments included
Strategic Director of Communities, Law & Governance	Yes	Yes
Finance Director	Yes	Yes
Portfolio Business Manager, Property Services	Yes	Yes
Date final report sent to Constitutional/Community Council/Scrutiny Team		June/29/2010