

Item No. 29.	Classification: Open	Date: 13 March 2018	Meeting Name: Cabinet
Report title:		Proposed Acquisition of Freehold Interest in Office Accommodation 132 Queens Road London SE15 2HP	
Ward(s) or groups affected:		All wards	
Cabinet Member:		Councillor Fiona Colley, Finance, Modernisation and Performance	

FOREWORD – COUNCILLOR FIONA COLLEY CABINET MEMBER FOR FINANCE MODERNISATION AND PERFORMANCE

I'm delighted to be able to recommend to Cabinet the purchase of 132 Queens Road. Known within the council as Queens Road 1, the council has been renting the office since 2011. At that time the owners were unwilling to sell the premises and so we entered into a rental agreement. Since then the rent has increased by 75% to almost £700,000 per annum. It is clearly financially advantageous, particularly given low borrowing costs, that the council should take the opportunity to acquire the office with an estimated annual saving of approximately £330,000.

This proposal is in line with the recent recommendation of Overview & Scrutiny Committee in January and the budget agreed by Council Assembly in February.

RECOMMENDATIONS

1. That Cabinet shall:
 - 1) Note the circumstances leading to the proposed acquisition of the freehold interest in 132 Queens Road and actions and investment due diligence being undertaken by officers and their advisors;
 - 2) Approve the acquisition of the freehold interest in 132 Queens Road (identified edged black on the plan in Appendix 1) and related costs;
 - 3) Delegate to the Chief Executive, advised by and in consultation with the Strategic Director of Finance and Governance and Head of Property, authority to:
 - a. Complete the purchase of the freehold interest in the asset;
 - b. Agree detailed transactional terms pursuant to the Heads of Terms;
 - c. Agree the financing structure to be adopted to fund the acquisition of the assets.

BACKGROUND INFORMATION

2. At its meeting on 23 November 2010 Cabinet approved a Revised Office Accommodation Strategy and delegated approval to the Chief Executive to agree the detailed terms and complete a lease of the subject premises.
3. The council occupies the building as a tenant and is bound to comply with the terms of the lease, including negotiated rent review increases, how the building is used, maintained and dealt with.
4. The freeholder has indicated that they intend to sell the freehold. As a result the opportunity has arisen for the council to acquire this strategic part of its operational office estate.
5. The council's office accommodation requirement and presence in the vicinity of Queens Road is supported by the council's Modernisation Programme and Workplace Strategy endorsed by Cabinet at its meeting on 1 November 2016. The Workplace Strategy includes developing the council's office accommodation across a two centre model by increasing capacity at Queens Road.
6. At its meeting on 12 December 2017 cabinet approved a proposal to construct new office accommodation at 133-137 Queens Road and its procurement is being considered by the Strategic Director of Housing and Modernisation as a chief officer decision in March 2018.
7. Given that there is an established ongoing demand for office accommodation in the centre of the Borough the acquisition will give a number of advantages over the continued leasehold arrangement relating mainly to being able to achieve greater financial and estate management autonomy.
8. It should be noted that there is a small segment of land which falls within the freeholder's registered title but is not included within the lease extent. It is confirmed that the proposed acquisition will include the entirety of the freeholder's title i.e. including the small segment.

KEY ISSUES FOR CONSIDERATION

9. The council has the opportunity to acquire the freehold interest in advance of it being marketed. It is likely that the market will view the freehold investment, with the Council as the tenant, as attractive and bidding is therefore likely to be competitive. Therefore, subject to cabinet approval, the agreed exclusivity period gives the council the best opportunity to acquire on favourable terms.
10. Heads of terms have been agreed including an exclusivity period for the council.
11. External consultants have confirmed that the agreed consideration reflects the value of the freehold to the council and therefore supports the acquisition.
12. Legal and technical due diligence is being undertaken and it is confirmed that no issues have been identified that would prevent the acquisition.

13. It should be noted that this may represent the only opportunity for the council to acquire the freehold since, in the event of being acquired by an investment fund, they tend to hold assets for the long term and do not trade on with any frequency.
14. The financial rationale for an acquisition of the freehold by the council is considered in some depth in the closed version of this report. There will also be a series of asset-related benefits (soft benefits) which will arise directly from the change in tenure from leaseholder to freehold owner:
- 15.

No.	Factor	Leaseholder	Freehold Owner
1.	Business Operations	Restricted. The terms of the lease are geared towards protecting the value of the landlord's investment which may be at variance with the council's aspirations as an occupier. Changes such as modifications to the building need consent, which incur cost, take time to obtain, may result in additional rent, or may simply be refused.	Full flexibility subject only to legislative requirements affecting building owners e.g. planning, building control, health & safety, etc.
2.	Dealings	Onerous. Limited to assignment and limited subletting subject to landlord's approval and ongoing liabilities. For example, the council can assign the whole of the building but would need to find an assignee and would then have to guarantee against assignee default.	<p>The council would have total flexibility to treat with the building and parts of it as it saw fit. Examples:</p> <ul style="list-style-type: none"> • subletting part of the building to commercial concerns at a market rent ; • sale and leaseback should the financial context for holding the building change and there is a compelling business case to restructure holding arrangements. <p>Equally importantly the council would be better able to time any strategic exit from the property in the future should it wish to relocate.</p>
3.	Holding Costs	Significant risk. Exposed to periodic rent reviews. Also, contractually there is	Hedge against risk of rental growth. Would have a vested interest in the

No.	Factor	Leaseholder	Freehold Owner
		no option other than to maintain the building to the highest standard – irrespective of what might be deemed affordable.	value growth arising from the ongoing improvements and investment in the vicinity. As tenant, the affect of this would be reflected in the rent payable at review.
4.	Asset Value	Deteriorating. At the end of the lease the Council will be left with nil asset value, a dilapidations liability and would need to secure a further lease (in the same building or elsewhere, depending on its requirement at the time as an occupier)	There will be corresponding refurbishment costs. However, even at the end of the building's useful life the council would retain a site with a residual value in the site.

Community impact statement

16. In formulating the recommendations of this report the potential impact on the community has been taken into account, including people identified as having protected characteristics. No specific equality implications have been identified in relation to this report.

Policy implications

17. The proposed acquisition is in accordance with the council's Modernisation Programme and Workplace Strategy endorsed by Cabinet at its meeting on 1 November 2016. The Workplace Strategy includes developing the council's office accommodation across a two centre model by increasing capacity at Queens Road.

Financial Implications

18. The financial implications for the council arising from the proposed purchase are contained in the closed version of this report.

Consultation

19. In view of confidentiality requirements and commercial sensitivity in relation to this as yet uncompleted transaction, external consultation has not been undertaken. Internal consultation has taken place with all relevant departments, including the provision of advice from Director of Law and Democracy and Strategic Director of Finance and Governance.

SUPPLEMENTARY ADVICE FROM OTHER OFFICERS

Strategic Director of Law and Democracy

20. This property is already occupied by the Council under the terms of a commercial lease which runs from 20 years from 1 June 2011. The closed report explains the reasoning behind such a purchase and that external

valuation advice has been obtained which confirms that the proposed price represents the market value for the acquisition of the freehold interest.

21. Section 120 (1) of the Local Government Act 1972 (“the 1972 Act”) authorises the Council to acquire any land by agreement for the purposes of (a) any of its statutory functions or (b) for the benefit, improvement or development of its area. By virtue of Section 120 (2) of the 1972 Act the Council may acquire by agreement any land for any purpose for which they are authorised by the 1972 Act or any other Act to acquire land, notwithstanding that the land is not immediately required for the purpose; and until it is required for that purpose, it may be used for the purpose of any of the council’s functions.
22. In view of the urgency to progress with the acquisition in order to avoid the current owner placing the site on the open market, external legal advisers have been appointed to act on behalf of the Council.

Strategic Director of Finance and Governance

23. This acquisition would allow the council surety over the long term operational and strategic usage for the Queens Road site without exposure to market rent reviews, whilst providing immediate and ongoing revenue budget savings for the council.
24. The purchase will be funded by borrowing. The debt financing costs (MRP and interest) will be charged to revenue over the expected useful life of the asset. The additional borrowing associated with this acquisition will not have a detrimental impact upon the availability or cost of borrowing associated with the financing for existing capital projects.
25. The implication of this acquisition on the council revenue budget is set out in more detail in Appendix 4 of the closed report.

BACKGROUND DOCUMENTS

Background Papers	Held At	Contact
Lease, title reports, financial assessments valuation and professional advice; audit report and legal due diligence	Property Department 5 th Floor 160 Tooley Street	Peter Barter 020 7525 5327

APPENDICES

No.	Title
Appendix 1	Plan

AUDIT TRAIL

Cabinet Member	Councillor Fiona Colley, Finance, Modernisation and Performance	
Lead Officer	Eleanor Kelly, Chief Executive	
Report Authors	Peter Barter Principal Surveyor, Corporate Property	
Version	Final	
Dated	1 March 2018	
Key Decision?	Yes	
CONSULTATION WITH OTHER OFFICERS / DIRECTORATES		
Officer Title	Comments Sought	Comments included
Strategic Director of Law and Democracy	Yes	Yes
Strategic Director of Finance and Governance	Yes	Yes
Cabinet Member	Yes	Yes
Date final report sent to Constitutional Team	1 March 2018	