Open Agenda

Cabinet

Monday 26 July 2010
10.30 am
Ground Floor Meeting Room G02A - Tooley Street, London SE1

Supplemental Agenda No.1

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Date: 23 July 2010

Agenda Item 4

Item No.	Classification: Open	Date: 26 July 2010	Meeting Name: Cabinet
Report title:		Joint Venture Agreement (Development Agreement) between Southwark Council and Berkeley Homes plc in respect to the formation of the One Tower Bridge Partnership and the development of Land at Potters Fields London SE1	
Ward(s) or groups affected:		Riverside Ward	
From:		Cabinet Member for Regeneration and Corporate Strategy	

FOREWORD - COUNCILLOR FIONA COLLEY, CABINET MEMBER FOR REGENERATION AND CORPORATE STRATEGY

Potters Fields is a key development opportunity at a world class location and I am pleased to recommend that we enter into a development agreement with Berkeley Homes on the same terms as those agreed by the previous Executive on the 29 July 2009. This will bring forward this site which has remained vacant and derelict for many years for development providing new homes, commercial and retail opportunities and cultural accommodation. In addition, significant capital will be generated to assist the Council in meeting its core objectives through the capital programme for the benefit of all residents in Southwark. This will form an important funding stream in this uncertain economic climate.

I have fully considered the report from officers, which commences at paragraph 5, and am putting forward the recommendations below.

RECOMMENDATIONS

1. That Cabinet agrees to enter into a Joint Venture Agreement (Development Agreement) between Berkeley Homes (South East London) Ltd and the London Borough of Southwark (and other parties), relating to the formation of the One Tower Bridge Partnership and the development of land at Potters Fields London SE1.

2. That Cabinet approve the disposal of the Council's interest in land as highlighted in orange diagonal lines on the plan attached at appendix 1.

3. That Cabinet notes that the Development Agreement is in accordance with the Heads of Terms as agreed at Executive on 29th July 2009 and the Executive decision on Future Options Co-Operation Agreement dated 19th March 2008.

4. That Cabinet note the reasons in paragraph 13 for the delegation by the Chief Executive not being exercised.

BACKGROUND INFORMATION

5. On 29 July 2009, the Council's then Executive agreed to Heads of Terms with Berkeley Homes (BH) for the development of the land at Potters Fields. The Heads of Terms were agreed following a period of discussion and negotiation based on the objectives that were set out in the Cooperation Agreement between the Council and BH which the Council entered into following the decision by the then Executive on 31 March 2008.

6. Since the decision by the Executive at their meeting on 29 July 2009, the Council has been in discussions with BH to finalise a Development Agreement (DA) based on the agreed Heads of Terms.

7. BH have been working on delivering a planning application for the site, consistent with the parameters set out in the Cooperation Agreement and Heads of Terms. Following a public exhibition held in May 2010, BH submitted a planning application for the site for a mixed use residential led development. The planning application for the scheme, known as 'One Tower Bridge' is currently being validated by the Council's planning authority and will then follow the statutory planning process. Nothing in the DA can or will bind the Council as statutory planning authority.

KEY ISSUES FOR CONSIDERATION

Development Agreement

8. The Development Agreement (DA) sets out in detail the key principles of the Heads of Terms which were outlined fully in the closed report to Executive of 29 July 2009, the open version of the report is attached here at Appendix 2. The terms of the DA remain consistent with the agreed objectives set out in the Cooperation Agreement and in the Heads of Terms as confirmed by the Council's legal advisers, Field Fisher Waterhouse (FFW).

9. To facilitate the development, it will be necessary to vary the boundary with Potters Fields Park. The Council in its lease to the Potters Fields Park Management Trust has a legal right to vary the boundaries of the park in order to facilitate the development and a key principle of any land swap is that there will be no net loss of Open Space. The current plans propose giving back to the park additional land as MOL over and above that required for the development together with the associated landscaping improvements. The Trust has been fully consulted throughout the development of the scheme. The Council and BH have considered future options for the management of the park in consultation with the Trust and have agreed Terms in principle as to boundary changes as part of the detailed drafting of the DA. The Secretary of State's consent will be required in order to proceed with this change in designation and will be applied through the appropriate statutory process.

10. The plan attached at appendix 1 highlights the areas of MOL that will be affected by the boundary change and they are marked in hatching on the plan attached.

Delegated Powers for the Chief Executive

11. The report to Executive of 29 July 2009 delegated to the Chief Executive authority to enter into a DA in accordance with the terms recommended and approved within that report. If the DA was not substantially in accordance with the agreed Heads of Terms, the DA would have to be referred back to the Cabinet for decision. Examples of substantial variations which would mean that the decision would not be within the delegated authority of the Chief Executive would include:

    - Change in principal parties
    - Variations to the terms which have a substantial financial impact
    - Material changes to the scope of the project including site boundaries
    - Changes to the principal objectives.

12. This report together with the legal report and concurrent concludes that the terms agreed within the DA remain the same as the Heads of Terms (in all material respects) and consequently do not need to be referred to the Cabinet for decision.

13. In view of the change of administration the Chief Executive proposed that the new Cabinet consider the decision for entering into the Development Agreement. This is a major development in a prominent location and is a key decision and as such the terms are more appropriately considered by the Cabinet.

FINANCIAL CONSIDERATIONS

14. The factors affecting best consideration are dealt with in detail in the 29 July 2010 closed report on the Heads of Terms. The Head of Property confirms that this transaction complies with the Council's statutory duty to achieve best consideration for the sale of its property assets in accordance with Section 123 of the Local Government Act 1972. It should be noted that the Council's position is further protected in the eventuality of uplift in property values through its profit share arrangements with BH.

15. Following signing of the DA, the Council will continue to incur additional cost in terms of legal fees, external advisors and ongoing officer time and monitoring and auditing of the development. Until a satisfactory planning consent has been achieved, monitoring surveyor costs will be the responsibility of the Council; the other fees (previously approved) will be Development Costs. Once planning consent has been obtained all these costs will be treated as Development Costs.

POLICY IMPLICATIONS

16. This development will contribute a significant capital receipt towards the Council's capital programme which will be used in line with Council priorities.

Consultation

17. The proposed plans for the development at Potters Fields have been consulted on with a wide range of community interests such as the Potters Fields Park Trust, Shad Thames residents association, South Bank Cultural Quarter, the local MP and ward councillors amongst others. In addition, key statutory and non-statutory stakeholders have been consulted on the plans and designs such as GOL, GLA, the City of London, Tower Hamlets, Historic Royal Palaces, CABE and the Environment Agency among many others. The consultation culminated in a recent public exhibition in May 2010, following on from the public exhibition held in December 2008. In view of the commercial sensitivity of the project, there has been no community consultation on this report, however, statutory officers have been consulted and their advice is below.

Legal Advice from External Advisors Field Fisher Waterhouse

18. The Heads of Terms have been carried in to the DA and, in the process, have been refined and, in some respects, improved, with an increased likelihood of a deliverable scheme; the onerous conditions have been drafted so as to protect both parties from being committed to a non viable scheme. The DA is, accordingly, consistent with the principles set out in the Heads of Terms.

SUPPLEMENTARY ADVICE FROM OTHER OFFICERS

Supplementary advice of Strategic Director of Communities, Law & Governance

Property Comment

19. The Cabinet is recommended to approve the disposal of land at Potters Fields, London SE1 as shown highlighted in orange diagonal lines on the plan attached at appendix 1 to this report ("the Land") to One Tower Bridge Partnership (a 50/50 partnership between the Council and BH) for a consideration plus further payments as calculated in accordance with the Heads of Terms and upon the terms of the DA.

20. The Cabinet is advised that Section 123 of the Local Government Act 1972 provides that except with the consent of the Secretary of State, a Council shall not dispose of non housing land, otherwise than by way of a short tenancy, for a consideration less than the best that can reasonably be obtained.

21. The Head of Property at paragraph 14 of this report confirms that the consideration for the Land is the best that can reasonably be obtained. Provided that the Head of Property is satisfied that the consideration achieves the requirements of Section 123, the Cabinet may approve the recommendation to dispose of the Land.

Supplementary Advice of the Finance Director

22. This report recommends that the council enter into a Development Agreement with Berkeley Homes in respect of the development of land at Potters Fields London SE1. The Finance Director understands that the development agreement is substantially as agreed at Heads of Terms stage.

23. The Finance Director notes that the Head of Property has confirmed that this transaction complies with the Council's statutory duty to achieve best consideration for the sale of its property assets in accordance with Section 123 of the Local Government Act 1972. The Finance Director notes that the Council's position is further protected in the eventuality of uplift in property values through its profit share arrangements with Berkeley Homes.

24. The Council will also be responsible for its own legal and other fees which are to be met from this capital receipt, as outlined in paragraph 15.

REASONS FOR LATENESS

25. The discussions and negotiations on the DA have been ongoing between the Council and BH since the agreement of the Heads of Terms concluding only recently. The drafting of the DA and of this report required further technical and professional advice from the external consultancy team of legal, property and finance specialists. The final drafting of the report was, therefore, not concluded prior to the stage at which Cabinet papers would have been circulated under normal protocols.

REASONS FOR URGENCY

26. Under the signed Heads of Terms, both parties have committed to act in good faith. In recognition of this commitment and BH's submission of a planning application, it is essential that the Council shows reciprocal commitment to the partnership.

27. The next scheduled meeting of the Council's Cabinet is 21 September 2010 and as the planning application has now been submitted and the DA finalised, the programme for bringing forward development would be affected adversely if the decision was delayed until September 2010 as the Council and BH both require certainty that the DA has been agreed before the required resources can be committed to bring forward development.

BACKGROUND DOCUMENTS

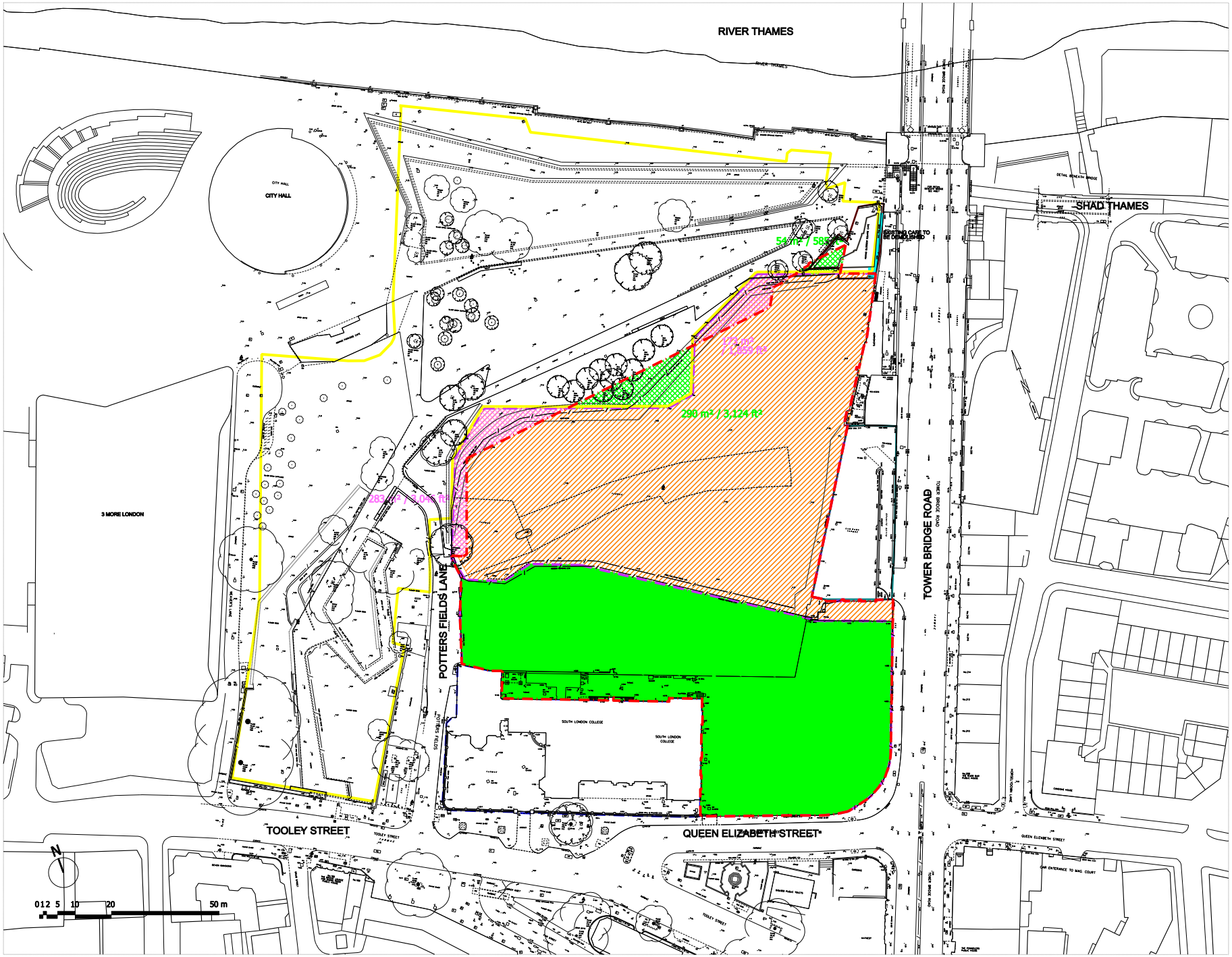
Background Papers	Held At	Contact
Overview and Scrutiny report – Update on Potters Fields	Property Dept	Tom Branton / Jeremy Pilgrim
Executive Report – Potters Fields Site – Decision on Future Options (19.03.09)	Property Dept	Tom Branton / Jeremy Pilgrim
Chief Executive Delegated Report – Agreement to Heads of Terms on Potters Fields Development – 23/10/09	Property Dept	Tom Branton / Jeremy Pilgrim

APPENDICES

Appendix 1	Council Land plan
Appendix 2	Open Executive Report: Potters Fields Heads of Terms, 29 July 2009

AUDIT TRAIL

Cabinet Member	Cabinet Member for Regeneration and Corporate Strategy		
Lead Officer	Chief Executive		
Report Author	Stephen Platts – Head of Property Jeremy Pilgrim - Property Development Manager		
Version	FINAL		
Dated	23.07.10		
Key Decision?	Yes		
CONSULTATION WITH OTHER OFFICERS / DIRECTORATES			
Officer Title		Comments Sought	Comments included
Strategic Director – Communities, Law & Governance		YES	YES
Finance Director		YES	YES
Date final report sent to Constitutional Support Services			23.07. 10



NOTES

DO NOT SCALE FROM THIS DRAWING.

ALL DIMENSIONS TO BE CHECKED ON SITE.

ALL OMISSIONS AND DISCREPANCIES TO BE REPORTED TO THE ARCHITECT IMMEDIATELY.

LAMBETH COLLEGE AND THE BRIDGEMASTER'S HOUSE ARE NOT THE SUBJECT OF THIS PLANNING APPLICATION: OUTLINES ARE INDICATED FOR THE PURPOSE OF CONTEXTUAL REFERNCE ONLY.

ALL INTERNAL LAYOUTS ARE INDICATIVE ONLY.

ALL LANDSCAPING LAYOUTS ARE INDICATIVE ONLY AND ARE SUBJECT TO CONDITION.

- London Metropolitan Open Land taken as part of the development 344 m² / 3,702 ft²
- Berkeley Homes land swap given back as open space 456 m² / 4,908 ft²
- Berkeley Homes Land
- London Borough of Southwark Land
- Revised Site Boundary
- Site boundary
- Berkeley Homes Land- Lambeth College
- Metropolitan Open Land MOL
- Corporation of London
- Perimeter of Cafe
- Demise- Cafe
- Bin Store

Revision description	Date	Check	Rev

Squire and Partners

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Project
Potters Fields,
Tower Bridge Road,
London SE1

Drawing
Land swap drawing

Drawn	Date	Scale
EA	20/07/2010	1: 500 @ A1 1: 1000 @ A3

Job number	Drawing number	Revision
08032	S+P P005	

08032_Z0_P_00_G200_005.DGN

Item No.	Classification: Open	Date: July 29 2009	Meeting Name: Executive
Report title:		Potters Fields – Heads of Terms	
Ward(s) or groups affected:		Riverside Ward	
From:		Chief Executive	

RECOMMENDATIONS

1. That Executive agree the terms in this report pertaining to the development of Potters Fields and eventual disposal of the Council's interest in land as outlined in the closed report.

2. That Executive delegate authority to the Chief Executive to enter into an agreement for the development of Potters Fields in accordance with the terms outlined in the closed report.

3. That if the proposed development agreement is not substantially in accordance with these terms, the matter will be referred back to the Executive for decision.

BACKGROUND INFORMATION

4. The history of Potters Fields is long and detailed and is subject to various reports to the Executive, the most recent and relevant being the 19th and 31st March 2008. At the meeting on 31st March 2008, the Executive agreed to enter into a Cooperation Agreement with Berkeley Homes (BH) with the aim of creating a joint venture/development agreement for the development of the site at Potters Fields. The decision was based on objectives agreed by the Executive at the meeting on 16th October 2007 to deliver:

    - *best consideration for the Council's assets*
    - *an iconic arts / cultural / entertainment facility*
    - *an architectural proposal consistent with the Council's aspirations*

5. It is important to note that these objectives form the basis of the Cooperation Agreement and underpin the principles of the Heads of Terms.

6. The report to Executive on 19th March 2008 addressed the key historical issues associated with Potters Fields which had been investigated thoroughly at that time. It is worth noting the background to the various issues briefly in this report as they affect the value of the site and have affected the Council's negotiating strength with BH.

7. Firstly, under the 1982 agreement, St Martins imposed a positive covenant on the land requiring the Council to use best endeavours to build a residential development on the land comprising of 450 – 456 habitable rooms. Secondly, in the 2003 transfer of the land to the Council, there is a restrictive covenant requiring that the land must not be used for any purpose other than residential. Thirdly, there is a restrictive covenant placed on the park land (which is adjacent to the Council's land) requiring that it may only be used as a park. The combined effects of: the stopping up of

Potters Field Road, the restrictive covenant on the park and the way that the boundaries were drawn when the land was transferred to the Council, means that the Council's land has been left land-locked to vehicular access. This complicated legal framework was created by the LDDC (London Docklands Development Corporation) and St Martins in 1982 to control development on the site once it had transferred over to the ownership of the Council as successor to the LDDC. BH are the beneficiaries of the various covenants relating to the site and the ransom strip following the acquisition of the site from St Martins.

8. The Executive report explained that all of the inter-relating complex issues were now more fully understood. The Council considered a number of options to bring forward a development on the site and following advice from Counsel, its legal and property consultancy teams it become clear that a joint venture arrangement with BH was the best way forward. It is also worth noting that the Mayor of London was threatening CPO action[1] in relation to the Council's land which was an additional factor in determining the decision of the Executive at that time. In considering this advice, the Executive agreed to enter into a Cooperation Agreement to work with BH on developing a joint venture.

The Cooperation Agreement

9. On 1st April 2008, the Cooperation Agreement was entered into and the Council and Berkeley Homes have been working together to develop plans for the site since then. A steering group between BH and the Council has coordinated the project's development and an internal management board was set up to advise the Chief Executive in her role at the steering group. The management board is chaired by the Deputy Chief Executive and involves all relevant departmental representatives as well as external advisors[2].

10. The Cooperation Agreement set out how both the Council and BH would work together towards creating a new planning application and what the quantum of the development should be, based on the existing planning consent. Operational matters were subsequently delegated to a working party involving the Deputy Chief Executive in order to bring the scheme forward. As matters progressed, a separate meeting group was convened to negotiate the Heads of Terms involving the Head of Property and the Deputy Chief Executive.

11. The Cooperation Agreement set out a list of key milestones that both parties would work towards in order to reach a planning application within a specific timeline. One of the principal milestones and the first step towards drafting a new planning application was to appoint a new architect. BH prepared a specification in consultation with the steering group in accordance with agreed parameters set within the Cooperation Agreement and requested three architectural firms to tender for the new scheme design. Make, Allies and Morrison, and Squire and Partners were the three firms who tendered and pitched for the job. The steering group members and a representative from the LDA attended the presentations and decided unanimously that Squire and Partners had met the key criteria in the brief most successfully.

12. BH instructed Squire and Partners to prepare more detailed plans for consultation in preparation for a planning application. At the same time, other issues relating to the

[1] However, with the change of Mayor, this has now been rescinded, as was evidenced in an answer to a question at Mayor's Question Time on 15th September 2008; The Mayor of London responded to a question asking whether the threat of CPO action would be lifted saying "I look forward to seeing the new scheme in due course, and in the meantime there is no threat of a CPO."

[2] The governance of the project team was reported to Overview and Scrutiny Committee in January 2009 – see Potters Fields Update Report to OSC – 12/01/09.

key milestones began to be resolved; this included the resolution of outstanding boundary issues and BH commencing the foundation and slab work on their site.

13. Soon after their appointment, Squire and Partners began to consult on the plans for the scheme involving a wide section of key stakeholder groups who were identified at an early stage. Stakeholders included ward councillors, the local MP, CABE, GLA, GOL, the Mayor of London, English Heritage, London Borough of Tower Hamlets, ICIMOS (representing UNESCO), Southwark Heritage Association, local religious leaders, the local school and the planning authority as well as the Potters Fields Park Trust and local residents and business groups.

14. Consultations took place in summer 2008 and then again in November 2008 at which updated and amended plans were fed back based on comments previously received. A public exhibition was then held at Lambeth College over three days in December to exhibit the plans and model for the proposed scheme which were showcased on the BBC and in the local and national press. Since then consultations have continued with the Local Planning Authority in pre-application discussions as well as further consultation with statutory stakeholders.

15. The cultural user is a key element to the scheme and a requirement of the local plan. It is an agreed objective of the Cooperation Agreement and the Heads of Terms. As far as the contractual arrangements are concerned, the objective is to secure “a full open market price for the arts/cultural facility”. The Council and BH have been working in partnership to progress the issue, going to the market to advertise the space, placing advertisements in the national and international press in September 2008 seeking expressions of interest.

16. A wide range of expressions of interest were received and potential bidders were requested to respond to a cultural brief outlining the key requirements of the site. At this point, specialist consultants from PwC were engaged to advise on the short listing process. PwC also provided a report contextualising each of the bids, offering a high level assessment of the validity of the financial assumptions from each of the shortlisted parties in order to inform the selection process.

17. Once a short list had been agreed on, bidders were invited to give a presentation to an evaluation panel including both BH and the Council, PwC, and an advisor from the Tate where bidders outlined the key aspects of their scheme and responded to a Q&A session. Following the presentations, the panel met again to consider the merits of each organisation and to receive reports from the architects and PwC and also to receive the advice from the Tate in order to inform deliberations. Unanimously, the panel decided that discussions should continue with two of the three short listed bidders and that one group should be removed from the process.

18. In agreeing to continue discussions further with only two bidders, the group felt that further clarity was required around the planning application and the final details of the scheme. It was agreed that once a planning application had been submitted, further referencing and due diligence of both organisations would be needed in order to inform decision making.

KEY ISSUES FOR CONSIDERATION

19. This section of the report will seek to highlight the key elements of the Heads of Terms and to explain the nature of the relationship we are proposing between the Council and Berkeley Homes.

THE PARTIES AND THE OBJECTIVE

20. The Council will be entering into Heads of Terms with Berkeley Homes (South East London) Ltd.

21. The Heads of Terms refer back to the objectives set out in the cooperation agreement and where they are expressed as being :

    The joint venture will comprise 'a high quality mixed use development which includes:

    - a minimum of 27,216 gross square metres of private residential space,
    - retail, commercial, A3; and,
    - leisure and an arts and/or cultural facility of a maximum size of 8,122 square metres (of London, national or international importance) capable of being used flexibly (its use not being limited to a specialist owner or occupier) and,
    - affordable housing'

    In addition, there are specific objectives to both the developer and the Council set out in the co-operation agreement:

    'The Council's Objective is to meet its requirement under the Local Government Act 1972 to secure the best consideration reasonably obtainable in the event that it sells the Council land and the Council is of the view that best consideration should be achieved by an agreement with its adjoining owner BH and securing a full open market price for the arts/Cultural facility to form part of the development.'

    'BH's objective is to maximise the development value and commercial viability of the BH land and is of the view that this should be achieved by agreement with its adjoining owner the Council'

22. These are the general objectives of the parties and will be reflected in the development agreement.

23. The Site includes the Council's land adjacent to and to the south of Potters Fields Park and BH's land to the north of Lambeth College these are marked on the site plan attached at Appendix 1.

Heads of Terms

24. The Heads of Terms address the key fundamental principles of the development agreement in relation to the value of the site, associated costs and receipt of funds and are set out below.

Profit Share Agreement

25. The value of the interests of both parties has been assessed externally (by Drivas Jonas) to take into consideration the ransom strip, covenants, location and size. The Council has received advice that the split of the development profit is reasonable and represents best consideration even when the performance payment paid to BH is taken into consideration.

Minimum Land Payment

26. Based on the valuation of the site by Drivers Jonas, the Council and BH have agreed a minimum land payment for the combined sites at Potters Fields to be split between both parties. This provides a Base Land Payment for the Council's asset. The Base Land Value will be paid out to both parties once the development has become cash positive and will be a priority payment after debt funding in accordance with the schedule of payments (42B) – the Council's payment being in priority to BH's payment. This will ensure that both parties benefit from reduced interest charges from earlier payment of costs which will in turn generate greater profit from the scheme.

27. In the event that the development does not become cash positive the minimum payment will still be due to the Council from BH and is in effect a guaranteed return (i.e. BH are required to pay this sum to the Council irrespective of whether the scheme makes a profit). This means that BH will be accepting the risk associated with the development on commencement, this payment is to be guaranteed by BH Group. Start on site however will not commence until a viability assessment is undertaken to ensure the profitability of the scheme which will demonstrate that the scheme can produce the minimum land payment. If this viability assessment is not met the scheme will not progress until such time as a payment of the minimum land payment can be forecast .

Funding the Works

28. BH have agreed to fund the development at Potters Fields in its entirety in order to ensure as swift a start on site as possible. The Council accepts that in the current economic climate, access to funding on this scale is challenging despite the fact that interest rates are currently set at 0.5%. In recognition of the difficult economic climate, the Council has sought advice from both Drivers Jonas (the Council's valuers) and PwC (consultancy support) on an appropriate fee for the funding of the works and both support the Council's negotiated position in reaching agreement with BH on a funding fee across the lifetime of the debt made up of arrangement fee, utilisation fee and a market rate over LIBOR.

29. It has also been agreed that interest will be charged on costs from the date of signing the Cooperation Agreement (1st April 2008). Interest will not be charged on costs incurred prior to this date nor on the costs already paid under the cooperation agreement as outlined in paragraph 57.

Management of Works

30. BH will manage the works on site directly and engage sub-contractors to carry out the development. The management of works will be subject to a fee based on the end sale value of each unit (both residential and commercial). The Council has sought advice again from both Drivers Jonas and PwC which supports its negotiated

position of a charge on end sale values. This fee is however capped on the residential element of the scheme on sales over an upper limit. The total fee (subject to the cap) is then charged to the Development Account. It is worth noting that as part of the Development Agreement BH are not seeking a developer's profit and an element of this management fee can be seen as being in effect a developer's return.

Pre-development Costs

31. The Executive report of 19th March 2008 outlined a number of scheme development and holding costs and how these costs would be shared between both parties in the event that a joint scheme did not proceed. Further details of these costs are highlighted in paragraph 57 and are excluded from the Development Agreement. It is however recognised that additional costs have been incurred by BH which are beneficial to the current scheme. These comprise of two main elements, construction costs and professional fees.

32. As advisors to the Council on the Potters Fields development PwC engaged a quantity surveyor and a cost consultant to audit the pre-development costs and assess them for reasonableness. PwC have now reported on those costs and given their signed off evaluation to the Council. This evaluation forms the basis of agreement with BH in which the Council have negotiated that relevant costs are to be charged to the development account and paid out in accordance with the schedule of payments as "development costs" (42D). For the avoidance of doubt these costs do not include abortive costs associated with the Ian Ritchie scheme.

Cultural Building

33. Both parties are committed to the aims of the Cooperation Agreement and the cultural building is a key objective of that agreement as well as an obligation required for planning consent. The full scope and design solution to meet this objective is currently subject to negotiation and options are being considered. A preferred solution will be agreed by both parties prior to a planning application being submitted. The current proposal is for a ground and lower ground facility under the main part of the site with access direct from the River Walkway. The detailed design work and due diligence is being undertaken to ensure that this proposal is deliverable. The final solution will be agreed prior to the submission of a planning application.

34. It has been agreed by both parties that the costs of the cultural building and any income derived from it will be dealt with in the same manner as any other costs/income associated with the scheme. It is still the intention of both parties to maximise potential revenues from the cultural element and paragraphs 15-18 summarise work to date on marketing the opportunity.

Affordable Housing/Section 106

35. The quantum of Section 106 payments and level of Affordable Housing is a planning matter and will be subject to the normal statutory planning process and viability assessments utilising the Three Dragons Model. It has however been agreed that the costs and any income derived from it will be dealt with in the same manner as any other costs/income.

Performance Payment

36. As previously stated it would be normal for a developer to seek an element of developers profit as part of any development agreement. BH have agreed to forego this in return for the Council agreeing to a performance payment to BH based on end sale values of the residential element. This will be taken as a priority payment from the development account based on sales values once the criteria has been met. Once this has been paid any additional profit will be split in accordance with the normal profit share arrangements.

Heads of Terms Summary

37. The Heads of Terms address each of the key principles as outlined in the rationale and also sets out the scheduling of payments and the responsibilities of each party. The first key aspect of the agreement is that the parties agree to assist each other in the deduction of title, removal of covenants and land assembly to ensure the development can proceed including any land swap associated with the adjoining Potters Field Park.

38. The Council in its lease to Potters Field Park Trust has a legal right to vary the boundaries of the park in order to facilitate the development therefore legal consent from the Trust will not be required. A key principle will however be that there is no net loss of Open Space. The current plans propose giving back to the park additional land over and above that required for the development together with landscaping. The Trust has been fully consulted throughout the development of the scheme. The Council and BH will consider further future options for the management of the park in consultation with the Trust as part of the detailed drafting of the development agreement and Section 106 strategy.

39. BH will prepare the planning application (working with the Council) so as to optimise the development value of the Site. There will be a cut-off date in the development agreement before which time planning consent has to have been obtained after which the parties will be able to rescind the development agreement. The Steering Group will approve any application prior to submission, with the Council acting in its role as development partner not statutory planning authority.

40. BH will provide such security as the Council reasonably require over land owned or controlled by BH so as to enable the Council to step into the scheme (or procure that a third party does so) in the event of default by BH.

41. Once planning consent has been obtained through the statutory planning process, the development proposal needs to be tested to ensure that it satisfies the viability test - The test being that the development (after repayment of finance) is likely to generate sufficient income to pay the minimum land payment. If the viability test is satisfied the development will commence in line with an agreed programme. It is anticipated that the development will be carried out in (previously agreed) phases; BH will manage the development process, procuring warranties (with step-in rights) on behalf of the Council, as well as the marketing and sales process. BH will also be responsible for procuring any development finance required in order to fund the development.

    Schedule of Payments

42. BH will set up a development account on an open book basis. Receipts will be paid into the development account and will be applied in the following order:

    A in payment of any debt and equity funding together with interest
    B in payment of the notional value of the site to the Council

C in payment of the notional value of the site to BH.
D in recovering development costs to include pre-development costs as outlined in paragraph 31 - 32;
E any positive sums in the development account will be shared between BH and the Council;
F performance payment to BH once the criteria has been reached; and
G any sums remaining will be shared between BH and the Council.

43. The Development Costs include:

- all the various costs incurred in developing the Site including pre-development costs; as well as,
- a management fee on sales revenue capped;
- an interest charge to finance the development funding over the lifetime of the debt (until repaid) to accrue on costs from the date of the cooperation agreement
- the cost of all Section 106 obligations, including the provision of cultural space
- Development/Construction Costs (insofar as not covered above).
- Professional fees
- Marketing

44. Income produced from the development will be credited to the development account with payments made in accordance with the schedule of payments as outlined in the Heads of Terms. Any revenue stream attributed to the scheme at the point of completion of the development agreement will be capitalised which will then be paid out as a receipt in accordance with the schedule of payments. Such income will include :-

- Residential sales
- Commercial rents/sales
- Ground rents
- Cultural Space
- Grants

DELEGATED POWERS FOR THE CHIEF EXECUTIVE

45. The Chief Executive will take a decision to enter into a Development Agreement on the basis of recommendations in a formal delegated report by the Head of Property to her as long as there are no substantial variations to the Heads of Terms outlined in this report. Examples of substantial variations which would mean that it would not be within the delegated authority of the Chief Executive to come to a decision would include.

- Change in principal parties
- Variations to the terms which have a substantial financial impact
- Changes to the scope of the project including site boundaries
- Changes to the principal objectives as outlined in paragraph 4.

FINANCIAL CONSIDERATIONS

46. The Council has appointed independent valuers, Drivers Jonas (DJ) to advise on the financial considerations and assist the Head of Property to ensure that the Council is meeting the requirements of Section 123 of the Local Government Act 1972 which is also one of the key objective's of the cooperation agreement.

47. The Head of Property is satisfied that the transaction proposed is likely to meet the requirements of section 123 when all factors pertaining to the site are taken into consideration. This issue will be kept under review during the further discussions of the Development Agreement; a final view will be taken on that issue at the point the Development Agreement is concluded and if best consideration is not achieved, then no Development Agreement will be entered into.

48. To assist in the negotiation process, a series of valuations were requested. The basis of valuation considered a number of scenarios:

    - The Council's site in isolation;
    - Berkeley Homes site in isolation;
    - Combined Council and Berkeley Homes sites; and,
    - The proposed Squire and Partners proposals.

49. In relation to the return for its asset, the authority is guaranteed to receive a minimum land payment. Further to this, a full financial model has been developed jointly with BH, which has been checked and will be continually monitored by DJ up to signing a development agreement. In BH's current financial model, the authority would receive the unconditional land receipt in three lump payments

50. Those payments are BH's estimates based on current market conditions, and the scheme will be subject to a viability test. The nature of the viability test has not yet been agreed by the parties. The timing and amount of these payments could therefore be subject to change.

51. In addition to the above payment, the authority is entitled to a share of the profit generated from the scheme. However, this is only after all costs have been repaid, including the minimum land payment. The exact timing of these payments is still to be agreed.

52. As with any joint venture arrangement, both parties are sharing the risk in relation to the future profits. As it is generally accepted that we are currently at the bottom of the property cycle, the Head of Property deems that these risks are acceptable. It is likely that both parties will benefit from an uplift in residential value which would have a significant impact on profits to be shared by both parties.

53. DJ have undertaken a sensitivity analysis of the financial model looking at the effects of:

    a. increase in value; and
    b. increase in build costs.

    Changes to the sales values and build costs are likely to have the most significant effects on the financial model, rather than other variables, such as programme.

54. The results of which are enclosed in the closed report.

55. In summary, in the current financial model, the Council could receive the minimum land payment with no profit subject to the development proceeding.

56. However, if the market increases according to current projections, the authority could expect to receive the minimum land payment of plus a potential profit.

Costs

57. As part of the cooperation agreement the Council agreed to share costs of developing the planning consent 50/50 with BH. These costs are excluded from the development agreement and have already been incurred. PWC have provided an audit of these cost to ensure they are fair and reasonable and to ensure there is no "double counting" in the development agreement. The Council has now received this reassurance.

58. Following signing of the development agreement, the Council will continue to incur additional cost in terms of legal fees, external advisors and ongoing officer time and monitoring and auditing of the development. These will be charged to the usual ongoing revenue budgets once the development agreement has been signed and top sliced from the capital receipts.

Next Steps

59. There are several key elements that will follow the agreement of the Heads of Terms, these are:

    a. Submission of a planning application
    b. Agreement of a programme
    c. Negotiation and completion of the development agreement
    d. Planning consent achieved
    e. Start on site 2010

TERMINATION

60. The Heads of Terms will be non-binding so either party will be able to pull out at any time; if this occurs then the termination provisions relating to the co-operation agreement will come into play.

POLICY IMPLICATIONS

61. This development will contribute a capital receipt towards the Council's capital programme which will be used in line with Council priorities.

RESOURCE IMPLICATIONS

62. Officer time and external advisors will continue to be a resource implication to the Council; however, all costs associated with the development going forward will be covered by either the existing arrangements under the Cooperation Agreement or top sliced from the capital receipt once the Development Agreement has been completed.

SUPPLEMENTARY ADVICE

Consultation

63. The proposed plans for the development at Potters Fields have been consulted on with a wide range of community interests such as the Potters Fields Park Trust, Shad Thames residents association, South Bank Cultural Quarter, the local MP and ward councillors. In addition, key and statutory and non-statutory stakeholders have been consulted on the plans and designs such as GOL, GLA, the City of London, Tower Hamlets, Historic Royal Palaces, CABE and the Environment Agency among many

others. In view of the commercial sensitivity of the project, there has been no community consultation on this report, however, statutory officers have been consulted and their advice is below.

Concurrent Report - Legal Issues (Field Fisher Waterhouse)

64. Attached at Appendix 2 is a legal report considering the main terms of the current form of the draft Heads of Terms in the context of the potential legal risks to the Council and its potential exposure as a result of those risks. It does not consider any financial or other risks.

65. Whilst the Heads of Terms, when agreed, will not be legally binding, they will form the basis of any development agreement that is entered into between the parties.

Concurrent Report - Legal Issues

66. The report sets out the legal and other risks in the proposal. This concurrent is restricted to comment on the EU procurement regulations position, and on the statutory requirements for obtaining best consideration.

67. Procurement issues: The report to the Executive of 19th March 2008 commented in relation to the cooperation agreement and procurement issues that "the co-operation agreement's primary objective is in our view a land transaction, even though it contains ancillary works objectives. Therefore the EU procurement regulations do not apply to it. It will be important as the later development agreement is negotiated to consider whether it too is a land agreement rather than a works agreement. This will depend upon the content of the agreement." This has been kept under review and advice has been obtained from our external legal advisors that the transaction as it currently stands could be seen either as a land agreement, or as a transaction within the scope of the EU procurement regulations but one which falls within the terms of Regulation 14(1)(a)(iii) and hence does not need to be advertised but can be negotiated directly with and awarded to a single supplier. Regulation 14(1)(a)(iii) applies where there is only one supplier which can meet the contracting authority's needs either because only that supplier possesses the necessary technical (or artistic) means or because that supplier has exclusive legal rights which mean that the authority must contract with them (for example the supplier might be the owner of intellectual property rights which were crucial to the contract). In this case, Berkeley Homes' possession of the benefit of restrictive covenants over the Council's land, and its ownership of the only means of physical access to the Council's land, mean that the Council has no other choice of developer. This argument is not completely risk-free. The European Commission is hostile to direct award by authorities on this ground and it is acknowledged that the provision in the Directive was not aimed at these kinds of circumstances. Nevertheless it does appear clear that the Council really does not have a choice and the plain words of the Regulations apply. Our external advisers have advised that they think that the balance of risk justifies applying that Regulation 14(1)(a)(iii), given that the alternative would appear to be not to proceed with any scheme on the land in question and risk being in breach of our covenant.

68. The position will continue to be kept under review during the remaining period of discussion and implementation of the Heads of Terms and a final view will be given in the report to the Chief Executive under her delegated authority. However, the position currently remains that while the position is not risk-free, the advice to the Executive is that the transaction is one which may legitimately be regarded as exempt from the EU procurement regulations; and further that even if the Regulations do have application, the transaction is covered by Regulation 14 and need not therefore be competitively advertised.

69. Best consideration issues: The report to the Executive of March 2008 commented that the cooperation agreement had "the potential through the release of "marriage value" to achieve best consideration for the Council". The comments in the report indicate that this remains the position and indeed that a position substantially in accordance with the Heads of Terms would achieve the statutory requirements of best consideration. This will be kept under review and any final decision to dispose (which would be made by the Chief Executive under the authority delegated to her by this report) would need to be satisfied that this requirement was met.

Concurrent Report - Finance Issues

70. This report seeks approval for the Chief Executive to enter into an agreement for the development of Potters Fields in accordance with the terms in this report.

71. Professional advice has been received from Drivers Jonas and PwC on the costs, market value of the site, and financial model, and this advice has been relied upon in the preparation of this report.

72. In the case that the the viability test (paragraph 41) is not satisfied and the development does not proceed the council retains its site, and is responsible for relevant costs arising from the co-operation agreement, and as incurred to date.

73. If the viability test is satisfied and the Development starts, then the council should receive a minimum guaranteed land payment. The report outlines circumstances in which the receipt may increase. Appendix 2 presents potential risks including the insolvency of the developer which could put this guaranteed land payment at risk. The council will also be responsibility for its own legal and other fees (as in paragraph 58) which are to be met from this receipt.

74. The Head of Property will keep the terms within the Development Agreement under review, and a final review will be completed immediately prior to the Development Agreement being entered into. The Head of Property will have to be satisfied at that point that the transaction proposed is likely to meet the "not less than best consideration" test of s.123 of the Local Government Act 1972.

75. If the Development Agreement is not concluded the council may be liable for abortive costs under the co-operation agreement.

BACKGROUND DOCUMENTS

Background Papers	Held At	Contact
Overview and Scrutiny report – Update on Potters Fields	Chief Executive's Office	Tom Branton
Executive Report – Potters Fields Site – Decision on Future Options (19.03.09)	Chief Executive's Office	Tom Branton
Executive Report – Potters Fields Site – Decision on Future Options – (31.03.09)	Chief Executive's Office	Tom Branton
Executive Report – Potters Fields site – Update on current position (16.10.07)	Chief Executive's Office	Tom Branton

Audit Trail

Lead Officer	Annie Shepperd – Chief Executive	
Report Author	Stephen Platts	
Version	Final	
Dated	20th July 2009	
Key Decision?	Yes	
CONSULTATION WITH OTHER OFFICERS / DIRECTORATES / EXECUTIVE MEMBER		
Officer Title	**Comments Sought**	**Comments included**
Director of Communities, Law and Governance	YES	YES
Finance Director	YES	YES
Executive Member	YES	YES
Date final report sent to Constitutional Support Services		

APPENDIX 1

SITE PLAN

APPENDIX 2

LEGAL RISKS

Event	Risks	Exposure	Commentary
Insolvency of the developer and/or the guarantor.	The effect would be to delay the development and add to the cost. Could be triggered by exposure due to other developments failing. Could also put at risk the guaranteed land price (and any other monies due) if the developer had insufficient monies to pay them. There would be a similar risk (at least as to part of the payment) if the development did not satisfy the Viability Test in the end – i.e. the finance costs took all the receipts and the developer/guarantor was unable to cover the guaranteed minimum payment	Solvency to be confirmed by PWC; the Council has have the operating company as the principal and the parent company as the guarantor (PWC to confirm).	The guarantee has yet to be agreed; the principal is an established company (not an off-the-shelf company); there is a commercial risk that either, or both, may become insolvent; there will be "step in rights" in the development agreement enabling the Council to take control in the event of insolvency – subject to any lender's prior interest. Developer's bank may step in, in any event. Bank bond could be provided to cover the guaranteed payment but this has not been agreed – Council could consider insuring against the risk.
Title matters such as covenants and easements.	Add to cost as these will need to be resolved to allow the development to progress.	Very unlikely in that the developer is unlikely to have bought its part of the site with title issues, but due diligence yet to be completed.	Not a major issue on the face of it and one to be resolved swiftly once the heads of terms have been signed. Many of the potential risks can be covered by insurance. Known issues on Council land will fall away once development agreement unconditional.

Park boundary not realigned	Smaller scheme on the site; reduced profitability. Delay as the plans will need to be adjusted.	No material issue anticipated with the Park Boundary, but no assumption that will be delivered.	Figures are based on the site as controlled by the parties, with the exception of the park land. If the park land is land not exchanged, a smaller scheme will be developed.
Planning not obtained in time or granted subject to onerous conditions.	Termination of the Development Agreement.	Abortive costs under the co-operation agreement – capped. The Council's own Professional fees and other costs for the project to that stage.	The indications are that an acceptable planning consent can be achieved.
Ground conditions and archaeological and other like issues.	Cost and delay	Unknown, but nothing material apparent so far.	Insurance could be considered to cover this risk to an extent. This point will be reviewed during detailed negotiations on the Development Agreement itself.
Judicial review of the planning decision.	Delay and possible termination – see termination above.	To be determined but as no challenge to the previous consent and the Council would be a party to the new consent, this is considered to be unlikely. The principle of development appears to be accepted.	To be kept under review; the Development Agreement will anticipate a challenge, within reason.

Dispute with the developer during development	Delay and cost – the development may not progress during the dispute.	Counter productive, but possible. To be dealt with by way of a dispute mechanism prescribed in the Development Agreement.	
Contractor insolvency	Delay and additional costs – this assumes that the contractor is a different party to the developer (if they are the same, see above).	To be kept under review.	Council has to approve the team and neither party will want to use insubstantial consultants. Due diligence on the team will reduce the chances of exposure.
Sales at undervalue and cost over runs and other financial manipulation	Cost and delay.	Possible but can be minimised through drafting and professional monitoring of the development accounts and process.	This can never be totally removed due to the fact that the developer ultimately leads on the expenditure and sales. The Development Agreement will address these issues and the developer will need to be actively managed – this will be done by regular audits, even if no obvious issues.
Financial and market issues	Could result in the development becoming uneconomic or part of it being mothballed.		These are covered elsewhere in the report to the executive, but may well have an effect on how some of these legal issues could play out. They could also fluctuate over time due to the fact that the market is likely to move during the course of the development.

The unknown	Various		Can be addressed to an extent by transparency, communication, constant monitoring and vigilance during the development process and ensuring that there is a sound relationship with the developer – within the parameters of the development agreement and given the fact that one party is a Council.
Development Agreement not being agreed/ development being aborted	Risks include: 1. Abortive costs under the co-operation agreement – capped. 2. The Council's own Professional fees and other costs for the project to that stage. 3. Losing the potential profit from the proposed scheme. 4. Losing the cultural/affordable housing benefits from the scheme. 5. Having an undeveloped site with access and covenant issues (see Report and previous reports).	The resulting costs and loss of benefits referred to in the 'risks' column.	The Development Agreement offers an opportunity to the Council to realise some value (both in financial and other) from its part of the site. However, the site could be 'mothballed', albeit that this would, technically, breach the positive covenant (see the Report) – however, practically, BH are unlikely to be able to require compliance. The possibility of a CPO of the site seems to have subsided for the time being.

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Dated: 30/06/10