

## CABINET

21 April 2020

<b>Title:</b> Purchase of the Heathway Shopping Centre Long Leasehold Interest	
<b>Report of the Cabinet Member for Finance, Performance and Core Services and Cabinet Member for Regeneration and Social Housing</b>	
<b>Open Report with Exempt Appendix 1</b> (relevant legislation: paragraph 3 of Part I of Schedule 12A of the Local Government Act 1972 as amended)	<b>For Decision</b>
<b>Wards Affected:</b> Village	<b>Key Decision:</b> Yes
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<b>Accountable Director:</b> Ed Skeates, Development Director, Be First	
<b>Accountable Strategic Director:</b> Claire Symonds, Chief Operating Officer	
<b>Summary</b> <p>The owners of the long leasehold interest (c 87 years remaining) of the Dagenham Heathway shopping centre, CIP Threadneedle UK Property, have approached the Council to purchase its interest.</p> <p>The purchase of the shopping centre will enable both its redevelopment as a high-quality retail destination but more importantly enable the redevelopment of Millard Terrace. Millard Terrace is in poor condition and suffers from recurrent repair problems including leaks which arise from the way the building was constructed. To date it has been impossible to economically redevelop it due to it sitting above the shopping centre which was not in the Council's ownership.</p> <p>Purchasing the shopping centre is a rare and strategically important opportunity to enable the redevelopment of both Millard Terrace and the existing shopping centre. In the very short term this help the Council manage its repairing obligations to both the shopping centre and the dated Millard Terrace that sits above it. In the period beyond this the redevelopment will provide a significant increase in the number and quality of homes and the creation of a high-quality shopping attraction for Dagenham.</p> <p>The shopping centre will generate income during the hold period and enable the Council and Be First to develop plans for the wholesale redevelopment of the shopping centre and Millard Terrace in future years. A redevelopment will provide new retail and residential accommodation more in line with market needs and achieve a significant increase in the number of residential units further increasing the footfall to the Heathway generally. An acceleration of the redevelopment will lessen the risk associated with retail income and maintenance liabilities arising from Millard Terrace. A purchase would put the Council in control of both areas of risk.</p>	

Cabinet are asked to delegate concluding agreements on the basis of satisfactory Due Diligence and that the final agreed purchase price does not exceed the purchase price figure set out in Appendix 1, which is in the exempt section of the agenda as it contains commercially confidential information (relevant legislation - paragraph 3 of Part 1 of Schedule 12A of the Local Government Act 1972 (as amended)) and the public interest in maintaining the exemption outweighs the public interest in disclosing the information. . A valuation by Strutt & Parker confirms this does not exceed the current market value.

Dagenham Heathway is the Borough's second largest centre after Barking Town Centre and is defined as a Major Centre. It serves as an important focal point in Dagenham being centred on the tube station with connections on the District line. Other than the recent redevelopment of the library site there has been little recent investment in the centre and both the shopping centre and Millard Terrace are physically unattractive and provide compromised accommodation.

The main retail area consists of commercial units on either side of the Heathway (a range of small units shops and the Iceland/ Lidl unit) plus the Heathway Shopping Centre (previously known as the Mall). The Heathway Shopping Centre, itself, is a 1.3 hectare site which consists of a covered shopping centre made of up around 32 internal units as well two units fronting the Heathway and some kiosks and totalling approximate 87,000 sqft. The wider site area including the shopping centre car park and a row of shops (units 218-234 - also owned by the council and including the Tesco convenience store and Lloyds bank together with AST residential properties above) extends to approximately 1.58 ha (4 acres).

The Council also owns the Millard Terrace made up of 156 homes of which around 135 are Council tenants. A total of 21 units have been sold under right to buy and as leaseholders they continue to have a maintenance liability for common parts which, given the scale of forecast major works, will exceed the current maintenance reserve fund.

The whole site including Millard Terrace, the Mall and the adjacent car park has been part of a recent study looking at medium to long term regeneration schemes for inclusion in the 2023 - 2033 Extended Estates Programme. It has been included in the 2020 Be First Business Plan for initial feasibility work. A potential purchase would enable an acceleration of the redevelopment timeline that will further mitigate the risks associated with the letting of unit shops and speed the delivery of area's regeneration. Indicative plans suggest the potential for the site to accommodate between 400 and 500 new residential units, as well as re-providing an element of retail provision at ground floor. Any redevelopment could include the adjacent Lidl block to allow phased delivery to enable continuity for retail trading across both sites, as well as proving opportunities for decant accommodation for the Council's own tenants. The proximity of the railway line and the scale of development will result in a complex construction programmes but one that could achieve a significant regeneration of the area.

The comprehensive redevelopment of Millard Terrace in the future will not be possible without the inclusion of the current long leasehold interest. Any proposals for its inclusion in the future Estate Renewal Programme would be subject to any statutory consultation requirements and be in line with any GLA funding guidance and policy following approval of the detailed proposals by Cabinet.

Cabinet are asked to approve the purchase and delegate to the Chief Operating Officer completion of the necessary due diligence for purchase and the preparation of a business

plan for the management of the shopping centre. A future report would set out comprehensive redevelopment opportunities based on more detailed costings, analysis and plans.

### **Recommendations**

The Cabinet is recommended to:

- (i) Agree to purchase the long leasehold interest in the Heathway Shopping Centre for an acceptable value subject to not exceeding the maximum purchase price set out in Appendix 1 to the report;
- (ii) Authorise the Chief Operating Officer to agree and approve an asset management strategy for the Shopping Centre;
- (iii) Note that the Transfer of Undertakings (Protection of Employment) Regulations (TUPE) shall apply with a transfer of the Shopping Centre manager to Be First; and
- (iv) Authorise the Chief Operating Officer, in consultation with the Director of Law and Governance and the Cabinet Member for Finance, Performance and Core Services, to agree and execute all the necessary legal agreements, contracts and other documents associated with the resolution subject to satisfactory due diligence.

### **Reason(s)**

- To generate an income source for the Council in line with the Council's Investment and Acquisitions strategy.
- To secure control of a high-profile strategic asset for short/medium asset management to deliver a range of socio-economic benefits and secure the long term potential for future redevelopment.
- To provide the Council with greater control over its maintenance budget for Millard Terrace and shopping centre in the short-term hold period.

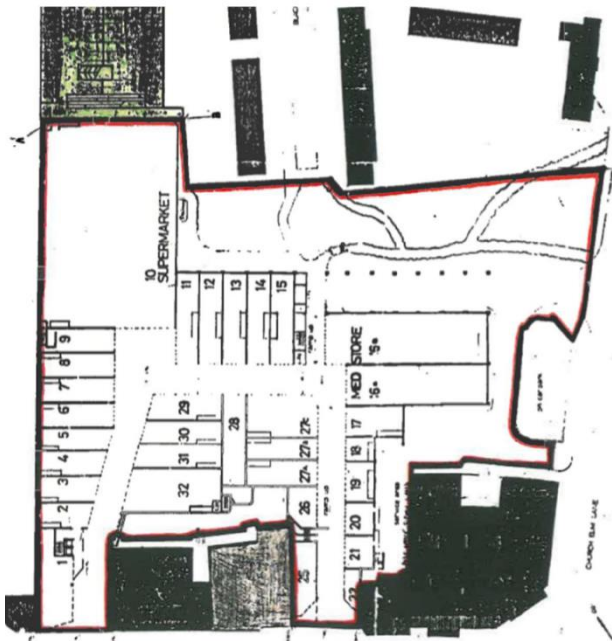
## **1. Introduction and Background**

- 1.1 Dagenham Heathway is a key focal point in the Borough with high footfall of 28,000 people a day. Vacancy rates at Dagenham Heathway are the highest in the Borough but well below UK averages. Originally the shopping centre was anchored by Sainsburys but this unit is now occupied by Wilkinsons (Wilko). Wilko no longer utilise their access to the car park. As a result, the car park has a low level of utilisation for shoppers and is only lightly used by residents of Millard Terrace. This contrasts with the utilisation of the car park for the Lidl store on the opposite side of the railway tracks which is congested at most times during the day. This car park is free for Lidl shoppers, in contrast to the Heathway car park that is subject to normal Council charges (Plan 1.1).

## Plan 1.1 - The Long Leasehold Interest



## Plan 1.2 - Demise plan from “Head Lease of The Mall Heathway – Nov 1988”



- 1.2 The shopping centre is shown on Plan 1.1 and the demise of the long leasehold interest is set out Plan 1.2 which excludes the car park and units 234-218 Heathway.
- 1.3 The shopping centre contains the Post Office, Boots, Specsavers, JD Sports, Shoe Zone, Savers, The Works (bookstore), Poundland and Timpson amongst other uses. In recent weeks a Starbucks Coffee store has opened in the prominent frontage unit. Officers have reviewed the full tenancy list and the length of leases. There are seven vacant units making up just 7% of floorspace (21% vacant by number). There are a further two units no longer being used but tenants are paying rent. There are two residential properties let on assured shorthold tenancies that have pedestrian access via the shopping centre’s operational service yard.

- 1.4 Units 234- 218 fall outside the long leasehold interest but are owned freehold by the council, which would enable a comprehensive redevelopment. These comprises a number of national multiple retailers including Tesco, Halifax and Lloyds. (Plan 2).

Plan 2 The Wider Site (Lidl site beyond)



## 2 Proposal and Issues

- 2.1 The shopping centre and Millard Terrace the residential housing estate on the upper deck was constructed in 1988. The centre was originally anchored by a large format Sainsbury's food store. There has been significant change in the retail market in terms of operator requirements. Whilst the centre still has a reasonable representation of national multiples the current unit sizes and internal arrangements will compromise future re-lettings and the overall attractiveness of the centre. Whilst the residential units in Millard Terrace still provide satisfactory accommodation the overall environment is hostile given its appearance dating from a 1970s design style which generates antisocial behaviour. This further underpins a lack of investment in the centre generally and a poor social and physical environment.
- 2.2 Whilst the shopping centre lease still has an 87-year unexpired term, the building will become obsolete in the very near future. Without significant reinvestment and combining the council's existing freehold interests in Millard Terrace, the adjacent car park and the frontage to Heathway (as well as the long leasehold interest currently owned by Threadneedle), it would not be possible to deliver a comprehensive redevelopment. A redevelopment would provide new retail (less floorspace overall but more regularly sized units) and residential accommodation fit for modern purposes as well as significantly increasing the number of residential units with flatted as opposed to terraced housing. In addition, there is an



opportunity to increase the level of private rented units that will provide diversity to the demographic profile of the area increasing levels of disposable income. The increased density of the development will maximise the site's overall accessibility given the adjacent District Line station and further bolster the patronage of both retail and community facilities within the Heathway.

- 2.3 The key issues that arise from the proposal relate to:
- the formulation of a viable redevelopment proposal;
  - immediate and long-term maintenance liabilities associated with Millard Terrace;
  - the operational management of the shopping centre.
- 2.4 These are considered below to formulate a suitable business plan to secure a comprehensive redevelopment aimed at minimising risk.

### **Comprehensive redevelopment proposals**

- 2.5 Prior to the formation of Be First, the Council's Regeneration Team held workshops with property and housing strategy teams to determine how to bring forward and appraise a programme of longer-term Estate Renewal projects including Millard Terrace. They concluded it would be difficult to implement any redevelopment scheme without the inclusion of the long leasehold interest that there was some concern that the condition of the deck and long-term maintenance requirement could not be satisfactorily addressed by the current capital improvements works budget. The workshop concluded that there was an opportunity to increase densities given the proximity of the district line station in a future redevelopment. In particular, it was noted that the site has the potential to accommodate taller buildings and has the potential to act as a catalyst for the regeneration of the wider area including land to the north of the district line including the Iceland and Lidl stores.
- 2.6 The proposals have the potential to create between 400 and 500 residential units as well as re-providing circa 6,000 m<sup>2</sup> of retail floor space (65,000 ft.<sup>2</sup>) with the provision of car parking spaces for residents.
- 2.7 A comprehensive redevelopment would secure a significant regeneration of the area by increasing the amount of residential accommodation and re-providing retail accommodation fit for purpose as well as boosting the income generation for the Council from retained units (both commercial and residential). The scale of development proposed would mean that a ballot of current residents would be required to access GLA grant funding. In any event a redevelopment of this scale would require extensive communication with both commercial and residential tenants as well as adjacent landowners including Network Rail.
- 2.8 It is clear that the council would not be able to progress a comprehensive redevelopment without buying in the existing long leasehold interest. There is advantage in securing this interest now. If the current landlord or an alternative landlord were to enforce the lease covenants the council may be forced into significant and disruptive capital expenditure in maintaining the roof to a proper standard. Whilst the council would be under the same obligation to maintain the shopping centre roof if it were to step into the long leasehold interest, it would be able to do so in a planned manner rather than being forced to undertake

maintenance on an unplanned basis. It would be able to compensate tenants for any disruption caused by delays in maintenance by providing softer rental terms on lease renewals for instance. By owning both the freehold of Millard Terrace and the shopping centre the council would be in the advantageous position of managing its ongoing maintenance liabilities.

- 2.9 Accordingly, it is considered that there is a significant advantage in securing the current leasehold interest at this stage, to implement short term asset management proposals to enhance the shopping centre income, as well as work towards a better planned maintenance schedule for the block with a view to formulating a longer term comprehensive redevelopment proposal.
- 2.10 A comprehensive development including the land to the north of the station occupied by Lidl would enable continuity of trade for a number of other retailers as well as providing the decant accommodation for the longer-term redevelopment of Millard Terrace. In overall terms the combined regeneration would significantly increase the volume of the housing stock and tenure mix which will result in increased levels of patronage for both commercial and civic facilities within the Heathway.
- 2.11 The 2020 Be First Business Plan proposes initial feasibility work to be undertaken with a potential start on site in 2026/2027. A redevelopment could take many forms from a direct development by LBBB to a JV with the private sector with LBBB simply buying completed units. At this stage there are too many variables to determine the optimum solution and the key objective is to secure the property interest to facilitate a future development as and when a credible plan is developed.
- 2.12 Subject to Cabinet approval it is proposed to prepare a business plan for the management of the shopping centre and formulate a strategy for the implementation of comprehensive redevelopment that will be subject to a further Cabinet Paper. The key initial stages to this programme would include:
- purchase of shopping centre;
  - scoping and implementing short term asset management proposals to enhance rental income and extend lease terms;
  - undertake detailed investigations for the short and medium term maintenance of the roof membrane to Millard Terrace and the car park deck;
  - develop an initial comprehensive redevelopment plan suitable for undertaking resident consultation with a view to holding a ballot;
  - undertake detailed costing proposals for the redevelopment proposal (with and without GLA funding and ballot arrangements);
  - undertake detailed valuation assessments of compensation due to existing commercial tenants and plans for phased construction to maintain continuity of trading;
  - preparation of a detailed phased construction plan to provide decant accommodation for displaced residential tenants;
  - determine the potential for external funding for the construction programme and use of joint venture partners to minimise construction risk to the Council.

## **The Maintenance and Management of Millard Terrace**

- 2.13 There are a total of 156 units in Millard Terrace comprising flats and two-storey terraced houses. A total of 21 units have been sold under right to buy and it is estimated that a budget of circa £6m would be required to buy back these interests to facilitate a comprehensive redevelopment.
- 2.14 As part of the council's Extended Estates Programme 2023-2030 an initial review of the planned maintenance programme for Millard Towers has been undertaken by an independent firm of cost consultants. The cost consultants estimate that cost of the maintenance of the residential elements in the next five-year period should be around to £4m but cannot provide detailed analysis without undertaking intrusive survey work. It is clear from the frequency of leaks to the roof that there is a significant problem.
- 2.15 The roof to the shopping centre is overlaid with the open space of Millard Terrace as well as the residential units themselves, in the form of the multi-story tower and the two-storey terraces. There is a network of drainage channels on the floor slab which is overlaid with a suspended paving finish. There is a history of blockages of these drainage channels resulting in multiple leaks to the roof in the shopping centre. Without a wholesale relaying of the roof membrane it is proving very difficult to provide a satisfactory remedy.
- 2.16 Moreover, the cost plan has no allowance for the maintenance of the adjacent car park. The council is under a lease obligation to provide 250 car parking spaces to be available to the shopping centre, even if a charge is made for their occupation. Anecdotal evidence suggests there are continued issues in maintaining the membrane to the car park as well as damage to the vehicle ramps due to their tight geometry. The resulting lack of planned maintenance is resulting in a decline in the attractiveness and usability of the car park. Nevertheless, there continues to be a lease obligation to the tenants of the shopping centre (and the long leaseholder in particular) to maintain the spaces.
- 2.17 Accordingly, there are a number of issues relating to the roof to Millard Terrace and the maintenance of the car park that have the potential to adversely affect the lease obligations that the council has to the owners of the shopping centre. If the shopping centre lease is purchased by a party that actively manages the asset the council may be forced into un-planned maintenance requiring significant and disruptive capital expenditure to the roof membrane on the terrace and the car park. The scale of this cost could easily exceed the annual income generated from the residential accommodation of Millard Terrace and the ground rent income generated from the shopping centre itself. In addition, difficulties are likely to be experienced in recovering significant maintenance contributions from the 21 long leaseholds that have been sold in Millard Terrace with the service of statutory notices. This will further complicate the council's maintenance budget.



## **The Operation and Management of the Shopping Centre**

- 2.18 The investment attractiveness of shopping centres has significantly deteriorated in recent years. The situation has worsened more recently. As a result there have been few transactions making it difficult to make an accurate assessment of the site's value. Comparable evidence for secondary and tertiary shopping centres range from a net initial yield of between 8 to 10%. Strutt and Parker have prepared a detailed assessment and conclude that a 10% yield is appropriate in this case. The maximum purchase price is set out in Appendix 1.
- 2.19 The centre includes a number of good quality national multiples such as Boots, Savers, Peacocks and JD sports. More recently Starbucks has taken one of the frontage units albeit via a franchise. In addition, the Wilko lease extends up until 2030. However, the majority of the units have lease terms that expire or have a potential break date within the next three years meaning that there is little security of income, up to 62% of the units have a lease event in the next 3 years. Accordingly, discussions have taken place with the centre's management team as well as the retained letting agents to determine short to medium term asset management proposals.
- 2.20 Through the service charge tenants are recharged the costs of maintaining the centre. This includes both the operation of the centre as well as the cost of management including rent collection and the centre manager itself. This generate a net income. As there are vacant units some of the service charge cannot be recovered there is a deduction to the gross income.
- 2.21 The Investment and Acquisitions Strategy requires a net return for retail investment after MRP (3.25%) of 4.13%. Due to the short lease terms on a number of units, that would have to be re let at expiry or the existing tenant renews the lease, there is a danger that the income might fall and the yield will drop below 4.13% in years 2023-2025 as a number of leases end.
- 2.22 Any approved redevelopment proposals will take time to secure planning permission and implement a suitable decant strategy for both commercial and residential tenants. Therefore, the scheme is unlikely to be redeveloped in a period less than three years and more likely between five and 10 years. Therefore, in the first instance it should be possible to extend the leases on a number of national multiple retailers even if slightly lower rents are offered to ensure continuity of income and remove lease breaks that would otherwise occur in the next three year period.
- 2.23 Stutt & Parker have undertaken a number of tenant re letting scenarios (Base Case assuming the re letting of units in line with lease terms and Active Management where a number of lease re gears take place on larger units and Wilko is re located to a terrace of vacant units). These demonstrates that there is a credible asset management strategy that could increase the overall rent roll in future years and remove lease breaks in the next three year period provided that incentives are offered to existing tenants to regear / renew their leases – this is exemplified in Appendix 1.
- 2.24 The Active Asset Management plan provides a more consistent cashflow over the hold period, which exceeds the IAS hurdle rate but incurs a cost in year 1 as capital

expenditure is incurred in relocating tenants/ offering incentives to regear/ renew leases. Accordingly, the year 1 return falls below the IAS hurdle. This suggests that a passive management strategy could achieve, on average, a return in excess of the IAS hurdle rate. Given the instability in the retail market it is difficult to determine the merit of either strategy and the sensible approach would be to undertake initial conversations with retailers to see if key tenants such as Boots, Savers, JD Sport can be encouraged to take extended lease terms.

- 2.25 The centre has a dedicated manager who coordinates with the various facilities management teams as well as with tenants. The centre manager is directly employed by Savills who manage the centre on behalf of Threadneedle, collecting rents and the service charge. If the purchase progresses the centre manager would have to be TUPE'd to the new owner. It is proposed that Be First would be responsible for the ongoing asset management of the centre and would take responsibility for the employment of the centre manager. The Savills contract could be renewed or terminated in future years. Savills do not provide an active asset management role but could do so and an allowance has been included in the cash flow model.
- 2.26 The centre manager could assist and form part of a wider town centre management team to following the model to be adopted for Barking Town Centre where a clear regeneration strategy is being produced setting out short, medium and long term actions. It is proposed that a commercial property agent would be retained to deal with all of the rent collection and service charge reconciliation with Be First acting as an intermediate client. The net rents received by the managing agent would then be paid directly to the council.
- 2.27 Appendix 1 illustrates the net cash flow after deductions for voids, ground rent and management fees. It is proposed that the Be First fee would be the margin of the net rents after the LBBB hold cost at 3.25%.
- 2.28 In discussions with the centre manager it appears that there is a long history of maintenance failures with the roof of Millard Terrace resulting in regular leaks into the shopping centre. The shopping centre has been let on a full repairing and insuring basis but this relates solely to the foundations and wall structure and not the roof. The council as freehold owner of Millard Terrace is responsible for the maintenance of the roof. The continued leaks present a risk that the current leaseholder may enforce its lease terms where the Council has to provide 'quiet enjoyment' and maintain the roof to a proper standard.
- 2.29 Based upon site inspections, the structure of the shopping centre (excluding the roof) is well maintained and a suitable service charge budget is raised and paid for by the current tenants to ensure the maintenance of common parts. There is an element of non-recovery of the service charge relating to vacant units, amounting to circa £120,000 per annum. This deficit can be reduced with new lettings.
- 2.30 Maintenance records confirm that there is little plant and machinery within the common parts of the shopping centre for which the landlord is responsible for maintaining. In particular all the lighting in the shopping malls has been upgraded to energy efficient LED and a rolling programme of replacement is currently underway in the service yard. Therefore, there are no significant capital items likely to come forward in the next 3 to 5 year period.

### **3 Options Appraisal**

- 3.1 Cabinet is asked to approve the purchase of the shopping centre and to delegate to the Chief operating Officer the preparation of a business plan for the short-term asset management of the shopping centre and the formulation of a business plan for the comprehensive redevelopment of Millard Terrace. At this stage the Council has the option to purchase or not to purchase. If it purchases, there are sub-options regarding the management approach it takes.
- 3.2 The 'Do Nothing' option would lose the opportunity to generate a rental stream, actively manage the centre and control future redevelopment opportunities of Millard Terrace. Potentially there could be an opportunity to purchase the site at a future date and proceed with development rather than holding now, however, there is no guarantee this will be possible and what maintenance liabilities will be incurred in the intervening period.
- 3.3 The recommended option to purchase the long leasehold interest is in line with the Investment and Acquisition Strategy and the emerging Inclusive Growth Strategy.
- 3.4 Should the Council purchase the site it is recommended a pro-active management strategy is adopted to maximise returns and deliver additional socio-economic benefits. This could be delivered through Be First acting as asset manager who would in turn appoint a commercial property agent to assist with new lettings rent collection and service charge reconciliation. This appointment would include the Transfer of Undertakings (Protection of Employment) Regulations 2006 for the existing shopping centre manager. The costs of this are included in the appraisal as they form part of the operational service charge as a deduction before arriving at the net rents received by the owner of the long leasehold interest.

### **4 Consultation**

- 4.1 Given the confidential nature of discussions between seller and purchaser there has been no consultation on this proposal. However, over the years various public consultation exercises seeking residents' views have identified a strong desire for improved facilities at Dagenham Heathway and the feeling that the full potential of the shopping centre was not being realised. If proposals are brought forward to Cabinet in due course for comprehensive redevelopment a full resident and wider community engagement strategy would be included and all statutory consultation and GLA guidelines followed in the preparation of this.

### **5 Equalities**

- 5.1 The Equality Act 2010 provides protection from discrimination in respect of certain protected characteristics namely: age, disability, gender reassignment, marriage and civil partnership, pregnancy and maternity, race, religion or belief, sex and sexual orientation. Section 149 of the Equality Act 2010 places the Council, as a public authority, under a legal duty ("the public sector equality duty"), in the exercise of all its functions, to have due regard to the need to:
- Eliminate discrimination, harassment, victimisation and any other conduct that is prohibited by or under the Equality Act;

- Advance equality of opportunity between persons who share a "relevant protected characteristic" (i.e. The characteristics referred to above other than marriage and civil partnership) and persons who do not share it; and
- Foster good relations between persons who share a relevant protected characteristic and persons who do not share it.

5.2 The Heathway Shopping Centre contains a number of facilities such as the Post Office and toilets which particularly serve the needs of certain protected characteristic groups. The recommendations set out in the report will not change this but future redevelopment plans would need to ensure a specific Equality Impact Assessment was carried out.

## **6 Financial Implications**

Implications completed by David Dickinson, Investment Fund Manager

- 6.1 This report proposes the purchase the long leasehold interest in Heathway Shopping Centre and outlines that the Council owns the freehold. The shopping centre is not mentioned in the Be First Business Plan as an investment but would fall under a commercial investment budget.
- 6.2 Shopping Centres, for several years, have proven to be a difficult investment, with higher than average vacancy levels and an increased use of company voluntary arrangements (CVAs) reducing the rental income received from commercial tenants. In addition, many property funds are also under pressure as investors move both out of shopping centres and out of the UK market due to the uncertainties around Brexit. As a result of these pressure, negotiations should seek to obtain a discount price when compared to the current valuation. This requirement is even more essential as several leases expire or are available for review in the next two years and these could result in reduced rental income.
- 6.3 While the report includes an outline of costs, there will be the potential for additional costs to be incurred as each lease is negotiated and the shopping centre is marketed. Any additional costs will reduce the net income, with the net income being allocated to the Be First return target. If the net income were to be negative due to a combination of additional costs and reduce rental income, then any net loss would be allocated to Be First. It is therefore essential that, if the lease is purchased, that it is actively and appropriately managed by Be First.
- 6.4 Financing costs will be based on interest costs of 3.25% and an MRP based on a 50-year annuity repayment profile. This will support the Investment and Acquisition Strategy as there is no build cost and interest from the lease will be available from the start.

## **7 Legal Implications**

Implications completed by: Dr Paul Feild, Senior Governance Solicitor

- 7.1 This report proposes the acquisition of a long head lease of 87 years from the current investor tenant. As the Council is the owner of the freehold title it will be able to merge the property interest and the freehold will no longer be subject to

restrictions of being subject to a lease and the landlord's obligations. Key legal considerations will be:

- the acquisition of the leases,
- the legal powers to enable the transaction,
- the need to minimise the Council's exposure to risk and unforeseen liabilities particularly with regard to the size of the site, its current and future investment value, planning, development and environmental risks, state aid and human rights.

## **Acquisition**

- 7.2 Due to the Council's existing freehold interest being subject to the lease, there is value to the Council beyond as it were, to that to a straightforward arm's length purchaser. The benefit of greater control and flexibility that the opportunity to acquire the lease presents delivers additional value to the Council's existing ownerships and interests at the site. In addition, future regenerative ambitions will require a full assembly of titles of which the lease is key. The purchase will be based on considered valuation advice. This will satisfy the Council's duty to achieve best value under the Local Government Act 1999.
- 7.3 The Council has the power to acquire land by virtue of Section 120 of the Local Government Act 1972, further it may by agreement do the same for the purposes of development by virtue of s. 227 of the Town and Country Planning Act 1990. This permits LBBD to acquire land for any purpose for which a local authority may be authorised to compulsorily acquire land under s. 226 of that Act. The Council further has the power to carry out the proposed scheme by the general power of competence given by section 1 of the Localism Act 2011 (GPC). Under the GPC power the Council can do anything that individuals generally may do provided that there is no prohibition against it elsewhere. Section 1(5) of the Localism Act provides that the general power of competence under section 1 is not limited by the existence of any other power of the authority which (to any extent) overlaps with the general power of competence. The use of the power in section 1 of the Localism Act 2011 is, akin to the use of any other powers, subject to Wednesbury reasonableness constraints and must be used for a proper purpose.
- 7.4 Whilst the general power of competence in section 1 of the Localism Act 2011 provides sufficient power for the Council to participate in the transaction and enter into the various proposed agreements, further support is available under Section 111 of the Local Government Act 1972 which enables the Council to do anything which is calculated to facilitate, or is conducive to or incidental to, the discharge of any of its functions, whether or not involving expenditure, borrowing or lending money, or the acquisition or disposal of any rights or property.
- 7.5 The purpose for which land is acquired is relevant to the powers to be relied upon. However in the current circumstances which includes the Council's ownership of the freehold, the multi-storey car park and the interests within the Housing Revenue Account, there are a number of good legal reasons for acquisition, firstly the enhancement of existing freehold interests that is without the incumbrance of being subject to a lease the value of the freehold is enhanced and as mentioned in this report the Heathway location has been identified as a regeneration and development opportunity and detailed feasibility assessments are being carried out

to determine the most suitable development strategy. Therefore, options are still being appraised and a preferred option has not emerged. However, the primary purpose of the acquisition appears to be the regeneration and wellbeing of the Council's area.

- 7.6 Investment Aspects - In exercising the power of general competence and in making any investment decisions (to the extent that any aspect of this transaction is considered to involve investment decisions), the Council must have regard to the functions for the purpose of which it is exercising the power, must act reasonably and also have regard to the following:
- 7.6.1 Compliance with the Statutory Guidance on Local Government Investments (the Statutory Guidance):
- i. Fulfilling its fiduciary duty to taxpayers;
  - ii. Obtaining best consideration for any disposal;
  - iii. Compliance with Section 24 of the Local Government Act 1988 in relation to giving financial assistance to any person (which either benefits from a general consent or requires express consent by the Secretary of State);
  - iv. Compliance with any other relevant considerations such as state aid and procurement;

### **Development/Land Risks and Considerations**

- 7.7 In normal circumstances there will be the imperative to ensure that all land, development and environmental risks are identified and managed. However, the Council is the freeholder owner and had an oversight of the site since the original development and is well-placed to understand the history and character of the site and its uses. The acquisition will be subject to the usual checks and diligence but it is not envisaged that there are any specific high risk elements to the proposed acquisition.
- 7.8 State Aid - As local government is an emanation of the state, the Council must comply with European Law regarding State Aid. This means that local authorities cannot subsidise commercial undertakings or confer upon them an unfair economic advantage. This report does not identify any specific aspect of the proposed acquisition, which is other than a commercial transaction, thus this arrangement satisfies the requirement it is on market terms. Furthermore, certain grants to remediate contaminated land are excluded from the State Aid Regime.
- 7.9 Human Rights – As the acquisition as described does not seek the use of compulsory purchase powers or displacement of any residents there does not appear to be critical risks associated with a Human Rights Act challenge, nevertheless, matters should be kept under review in case such considerations should arise.
- 7.10 The report indicates that an employee of the current leaseholder is responsible for the management of the leasehold interests. Given that the business of the leaseholder appears to be a going concern then it is likely that there will be a transfer of an undertaking and as a result the Council will be obliged to take the place of the previous employer on the same terms and conditions. As part of the due diligence it will be the responsibility for the acquiring party to establish the



current employment situation and whether there are any other workers potentially affected.

## **8 Commissioning Implications**

- 8.1 The proposal set out in this report would give the council a greater level of control, in the short to long term, over an important retail centre in the borough, and in a key regeneration area. The council currently owns the freehold of the site and there is a council owned housing estate as part of the development. The council purchasing the freehold would therefore simplify ownership and management of the whole site in the short term; and open up the potential for wider redevelopment as part of future regeneration plans for the borough, This would include the option to potentially look at redeveloping the existing housing through the estate renewal programme in future years, subject to appropriate approvals and financial viability.
- 8.2 In the short term the purchase of the site would provide the opportunity to improve management of the centre and encourage a diversification of uses within the existing centre, that will support the delivery of our wider ambitions for inclusive growth. This can be achieved by pursuing more active management of the centre, which would be achieved through Be First taking on responsibility for deciding the management arrangements for the centre.
- 8.3 Therefore, the purchase of this centre fits well with the council's wider ambitions for inclusive growth in Barking and Dagenham, providing short and long term opportunities to progress with the delivery our inclusive growth strategy, while providing a financial return to support the aims of the investment strategy.

## **9 Other Implications**

- 9.1 **Risk Management** - The recommendation involves the purchase of a long leasehold interest which would need to be funded from borrowing and therefore carry the risk in relation to the ability of the Council to service the debt as well as MRP. As appendix 1 shows this sum would be covered by the rental income however, there is a risk that tenants default/go out of business and/or new leases are not entered within 12 months of tenancies ending. The management strategy will be key to reducing the risk and ensuring vacant units are occupied as soon as possible but the financial model assumes a generous 12-month void and 12-month rent free.
- 9.2 **Staffing** - The Shopping Centre owners currently employ a centre manager who was TUPE'd over from the previous owners. Legally with the purchase this role would need to TUPE into Be First but would be fully funded from the rent roll and service charge budget. Cleaning, security, lettings etc are currently on the basis of contracts also funded from the service charge budget, which would continue unchanged.
- 9.3 **Corporate Policy and Customer Impact** – The proposal is a good example of the Council using its investment powers to both generate short term income as well as safeguard a future redevelopment opportunity which could deliver a number of Borough manifesto objectives.

- 9.4 **Safeguarding Children** – Future redevelopment proposals offer the chance to consider improvements which assist with improving safeguarding opportunities.
- 9.5 **Health Issues** – Future redevelopment offers the chance to address health and wellbeing issues which would be considered as part of the proposals.
- 9.6 **Crime and Disorder Issues** - Section 17 of the Crime and Disorder Act 1998 places a responsibility on councils to consider the crime and disorder implications of any proposals. As with many shopping centres, anti-social behaviour is a particular issue and as part of the management review the opportunities for making any improvements which address problems will be considered.
- 9.7 **Property / Asset Issues** - The proposals will generate a marriage value and add to the Council's existing land holdings.

**Public Background Papers Used in the Preparation of the Report:** None

**List of Appendices:**

Appendix 1: Financial proposals including cashflow (exempt document)