

CABINET

18 January 2022

Title: Amendments to the Funding Agreement for Be First Developments (Muller) Limited and Resolution to Dispose of the Muller Dairy Site on Shareholders Terms	
Report of the Cabinet Member for Finance, Performance and Core Services	
Open Report with Exempt Appendices 2 and 3 (relevant legislation: paragraphs 3 and 5 of Part I of Schedule 12A of the Local Government Act 1972)	For Decision
Wards Affected: Whalebone	Key Decision: Yes
Report Author: Jonathan Langham, Head of Commercial Development	Contact Details: Tel: 07812 965342 E-mail: jonathan.langham@befirst.london
Accountable Director: Ed Skeates, Director of Development, Be First	
Accountable Strategic Leadership Director: Claire Symonds, Acting Chief Executive and Managing Director	
Summary <p>This paper seeks agreement to sell the former Muller dairy site in Chadwell Heath shown on the plan in Appendix 1 following a marketing exercise that has generated a considerable level of interest.</p> <p>The Council has over the last 12 months received a number of unsolicited offers for the site and, as a result, a market testing exercise was undertaken to ascertain genuine market interest and the actual value of the site in the changing economic environment.</p> <p>This resulted in the receipt of several offers from major developers exceeding the Council's previous value expectations. As such, there is a strong justification for an early sale, particularly as changes in the housing market mean that the option to work up a mixed-use scheme and sell is now considerably higher risk.</p>	
Recommendation(s) <p>Cabinet is recommended to:</p> <ul style="list-style-type: none">(i) Agree that the Council, in its capacity as the Shareholder of Be First Developments (Muller) Limited, approves the disposal of the site shown edged red in Appendix 1 to the report to the preferred bidder on an unconditional basis, in accordance with the terms set out in Appendix 2 to the report;(ii) Agree that the Council authorises, as Shareholder of Be First Developments (Muller) and in conjunction with the Directors of the Company, the conversion of	

the zero percent element of the loan to equity by issuing new share capital in the event of the sale not being completed by 31 March 2022;

- (iii) Authorise the Managing Director, in consultation with the Strategic Director, Law and Governance, to repatriate any profits issued by Be First Developments (Muller) Ltd back to the Council;
- (iv) Authorise the Managing Director to undertake any action or execute any legal documents required to wind up/liquidate the company; and
- (v) Delegate authority to the Managing Director, in consultation with the Strategic Director, Law and Governance, to agree and enter into any legal agreements and contract documents to fully implement the above proposals.

Reason(s)

To comply with the original objectives of the Be First business plan and generate a revenue receipt to enable the Council to reinvest in other priorities including regeneration across the borough and assist in the longer term regeneration of the wider Chadwell Heath neighbourhood.

1 Introduction and Background

- 1.1 The former Muller dairy site lies within a designated area of locally significant industrial land in Chadwell Heath. The site was purchased in 2020 as it was competitively priced, appeared to have potential for value uplift and buying it would potentially enable the Council to influence the regeneration of the Chadwell Heath area. The site offers an opportunity to either provide space to consolidate and replace existing poor quality industrial space or to provide space for new residential development if a change of use could be secured. The Muller site is, however, at the edge of the Chadwell Heath industrial area and is some way from the new Cross Rail station which may be open by 2023.
- 1.2 The purchase was approved at Cabinet in February 2020 (minute 109) and completion took place in July 2020, after extensive renegotiation with the landowner on the price paid. The site was placed in a special purpose vehicle (SPV) company, Be First Developments (Muller) Limited. Since then, a masterplan for the Chadwell Heath area has been prepared by Be First on behalf of the Council and is subject to initial consultation at present. The strategy agreed at Cabinet envisioned the site would be sold by 2023 rather than being held for the long term.

Proposal to sell the site

- 1.3 To achieve the objectives of the Muller Business Plan the site will have to be sold to generate a receipt that can be repatriated to LBBD. The original Cabinet resolution for the purchase of the Muller site did not include a resolution to allow for the site to be sold, although the intention to do so is implicit in the Be First Business Plan. Directors of the SPV need consent from Cabinet as shareholder to sell the asset in order to discharge the objectives of the business plan.

- 1.4 Since the purchase in July 2020, the Council has received a number of un-solicited bids from a variety of parties including data centre, industrial and mixed use developers. At the moment, the site is designated for industrial use in both the London and Local plans and this is formally the desired planning use.
- 1.5 Be First undertook a marketing exercise to determine the actual demand and value for the site in the context of the unsolicited offers being made and some pessimistic valuations of the site received in early 2021. By running a formal process, this would provide the Council with a mechanism to evaluate competing bids and greater control over any subsequent sale. As a result of this process, a number of offers have been received from industrial/mixed use developers; no offers were received from residential developers, which is probably a reflection on the site's location in relation to the Cross Rail station and the recent decline in the London residential market, contrasted with the current strong demand for commercial space in this part of London.
- 1.6 To provide the Council with a rationale for the assessment of the bids the following criteria were set:
- Offer price, including any additional business rates income that might be generated (50%)
 - Site coverage ratio, any proposal must re provide at least 23,500 sqm (gross internal area) of commercial floorspace to ensure no net loss of employment floorspace and a site coverage ratio in excess of the previous use (10%)
 - Compliance with the objectives of the emerging master plan (including; active frontage, interfaces with adjacent uses, provision of east/ west pedestrian and cycle linkages, public open space) (22.5%)
 - Employment generation number of jobs, quality of jobs and training opportunities (7.5%)
 - Deliverability (Level of certainty LBBB has over achievement of the proposals/outcomes put forward by the bidder) (10%)
- 1.7 In assessing the deliverability of the scheme and its relationship with the wider masterplan consideration was also given to the following wider set of issues:
- Track record of bidder delivering multi-phase and/or mixed-use regeneration schemes
 - Appetite and interest of bidder in working with LBBB towards achieving LBBB vision beyond the Muller site
 - Level of certainty LBBB has over potential to achieve desired outcomes beyond the Muller site.
- 1.8 The offers have been assessed by officers from LBBB and Be First in an evaluation report and commentary provided by an external advisor to determine if this process has secured best consideration – this information is set out in Appendix 2, which is in

the exempt section of the agenda as it contains commercially confidential information (relevant legislation: paragraph 3 of Part I of Schedule 12A of the Local Government Act 1972) and the public interest in maintaining the exemption outweighs the public interest in disclosing the information. The preferred party represents the best price as well as the best scheme in terms of employment generated and design. The sale of the site to the preferred party would achieve a profit in excess of that estimated in the initial Muller Business Plan. The Directors of the Muller holding company recommended the sale of the site to the preferred party to the Shareholder Panel in a meeting on 9 December 2021.

The Loan

- 1.9 The purchase and planning budget was funded by borrowing from the Public Works Loan Board (PWLB). To comply with the requirements of public subsidy rules, the loan rate has to be at market rates and the advice from the Council's consultants confirmed that the loan should be split broadly 50-50 between a zero percent interest rate, and a premium loan charge at 8.14% reflecting the risks associated with the project. The Council has been advised that when the loan facility was initiated the zero percent element of the loan should have been converted from a loan to equity in the form of shares (in order to comply with the requirements of public subsidy that the overall loan is market facing). The Cabinet resolution that gave effect to the purchase and the creation of the loan only allowed for the creation of the loan and not the issuing of share capital. Therefore, a further resolution is needed to convert the loan to equity. The legal advice on which this is based is set out in Appendix 3, which is in the exempt section of the agenda as it contains legal professional privileged information (relevant legislation: paragraph 5 of Part I of Schedule 12A of the Local Government Act 1972) and the public interest in maintaining the exemption outweighs the public interest in disclosing the information.

2 Issues and Options

The Sale

- 2.1 The business plan envisages the Muller site being sold before July 2023. It is proposed that the sale proceeds at this stage in order to maximise the value that the Council can achieve.
- 2.2 There appears to be a significant bubble in the industrial land market at present caused by the combined effect of changes in shopping and working patterns as result of Covid accelerating existing trends, supply chain issues caused by Brexit, Covid and declining investor confidence in retail and residential development.
- 2.3 This bubble is unlikely to last as the market will stabilise and investors will drift back to residential and leisure, if not retail. The current valuation of the Muller site is therefore unlikely to continue to increase in the medium term. It is for these reasons that the recommendation is to sell the site at this point to achieve a surplus which can be reinvested in delivering other Council priorities.
- 2.4 The recommended bidder's proposal is compliant with the existing planning designation of the site and fits within one of the options proposed for the site in the emerging master plan, namely industrial intensification.

- 2.5 The Council will however want to ensure that the purchaser addresses both the traffic and transport implications of the scheme. In particular, the impact on Whalebone Lane and the A12 junction at Marks Gate to ensure that it delivers the aspirations around public realm and place contained in the emerging master plan and that it interfaces appropriately with the surrounding residential area given its peripheral position in the industrial area.

The Loan

- 2.6 In relation to the loan conversion this must take place before March 2022 otherwise there is a risk (albeit limited) that there may be a challenge that the zero percent element of the loan is contrary to the objectives of Public Subsidy. If the asset is sold before then there is no need to make the conversion as the loan would be repaid at the point of sale.

3 Options Appraisal

- 3.1 The recommended approach is to secure a resolution to sell the asset to the selected party and re-pay the loan at the time of sale provided this is before March 2022, otherwise the loan will have to be, in part, converted to share capital. The alternative options available to the Council are:

Alternative Options

- 3.2 **Option 1:** The Council could choose to retain the asset and seek to get planning permission for some form of mixed use development as proposed in the February 2020 Cabinet paper.

This means the Council would not only bear the holding cost of the site but also finance the design and planning process over the next two years. In the current market context this approach carries considerable risk. The pandemic has led to inflationary/ recessionary pressure in the wider economy, which means there is uncertainty over future land values. Coupled with this, there is a significant weakness in the residential sector, partly driven by the longer term impact of Covid on people's choices around where to live and population changes driven by Brexit. Alongside this, there remains the significant planning challenges of achieving a change of use for the site given the London wide need for employment space to be retained and the GLA's current strong policy position.

- 3.3 **Option 2:** To retain the site and seek to use it as part of a comprehensive redevelopment of the Chadwell Heath industrial area. Pursuing this course of action would be a major undertaking for the Council and require very significant land assembly, either through purchasing sites as they become available and/or the use of Compulsory Purchase Orders (CPOs). Not only would this take a long time, it would also require a significant ongoing capital commitment from the Council. This would need to be set against other priorities the Council has for its capital programme, not least the delivery of new homes and infrastructure across the borough.
- 3.4 **Option 3:** An alternative option would be for the council to select a private sector partner to bring forward the redevelopment of the whole Chadwell Heath industrial area, putting the Muller site into some form of joint venture with them. There is however some uncertainty as to whether or not a private sector partner of sufficient

scale could be found. The site, while important for the borough, is relatively peripheral in wider London terms and the current residential market and uncertainty around future demand for commuting into central London make it a risky investment prospect for residential development. In addition, there are only a very small number of active players in the London market able to take on a project of this scale. Therefore, choosing this route would potentially slow down the wider transformation of the area and make it harder to achieve the sale value assumed for the Muller site.

4 Consultation

- 4.1 The matter relates entirely to financial issues for the Council and no public consultation is required. Advice has been sought from relevant experts to ensure that the Council is complying with its statutory and regulatory obligations.
- 4.2 The proposals in the report were considered and endorsed by the Council's Investment Panel on 22 December 2021.

5 Commissioning implications

Implication completed by Darren Mackin, Head of Commissioning and Place, Inclusive Growth.

- 5.1 The sale of this site to the selected bidder will provide the council with a financial return that exceeds the target which is set in the Be First business plan. This return will support the delivery of the council's wider priorities.
- 5.2 The selected bidder is proposing to intensify the amount of employment use on the site. Achieving this aim will support the delivery of the Council's wider vision for Chadwell Heath. This is because it will enable other parts of the masterplan area, including those closer to the station, to be freed up for other uses. The Council and Be First will continue to work closely with landowners, including the proposed purchaser of the Muller site, to influence and shape the way the area develops.

6. Financial and Investment Implications

Implications completed by: David Dickinson, Investment Fund Manager

- 6.1 In February 2020 Cabinet agreed the purchase of the Muller dairy site to generate a revenue receipt that can be returned to the Council at the time of disposal to assist the Council with its long-term revenue funding requirements. To achieve this end, the asset was placed in a special purchased vehicle (SPV - Be First Developments (Muller) Limited) as this proposal would be a trading asset, i.e. it will be bought and sold within a relatively short period, as opposed to a long-term hold. Parts of the site were let out during the hold period and interest has accrued against a loan made to the SPV. This has provided the Council with an income stream and letting the site has helped reduce some of the hold costs for the SPV.
- 6.2 The site was to be held for three years while the masterplan and a planning permission application were completed, with interest charges calculated on a three-year hold. A review of the disposal options was proposed for after two years from the date of purchase.

- 6.3 As outlined in the report, there is an opportunity to sell the site earlier than envisaged at a value significantly higher than originally forecast. This is due to the increase in value of industrial land, which has recently seen a large uplift, and the preferred bidder's unconditional offer is seen as a good value. While land values may continue to increase in future, this sale will lock in the current market gain, as well as progress the development of the site, which is currently largely a vacant site.
- 6.4 The report covers most of the financial implications, the tendering process and the accounting requirements and there are no additional implications.
- 6.5 The report also seeks approval from Cabinet to convert the 0% element of the loan (£27m) to equity as share capital. This part of the loan is currently at 0% and is a soft loan. The loan conversion must take place before 31 March 2022 otherwise there is a risk that there may be a challenge that the 0% element of the loan is contrary to the objectives of Public Subsidy. If the asset is sold before this date, then there is no need to make the conversion as the loan would be repaid at the point of sale.
- 6.6 If the Muller site is sold, the loan and interest charges would be paid in full by the SPV to the Council. Any operating costs, fees and taxes would then be funded, with the net surplus paid back to the Council as dividends and accounted for as revenue income.

7 Legal Implications

Implications completed by: Dr Paul Feild Senior Governance and Standards Solicitor

- 7.1 The acquisition of the Muller site was considered and agreed by the Cabinet in February 2020. It was acquired via a Special Purpose Vehicle (SPV) a limited company being 100% of the shares Council owned. The purchase financed through a loan. As part of the corporate governance, some activities of the SPV were reserved to the Shareholder by a Shareholders Agreement and such decisions as set out in the Council's Constitution at Part 2, Chapter 6, paragraph 2.1(xx) are for the Cabinet to make.
- 7.2 The acquisition of the Muller site was in pursuit of the Council's Investment and Acquisition Policy. The Council has the power to acquire land by virtue of Section 120 of the Local Government Act 1972 and to carry out the proposed scheme by the General Power of Competence given by section 1 of the Localism Act 2011 (GPC for short). 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.
- 7.3 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. If there is an intention to trade the Localism Act 2011 at section 4 requires that it be facilitated by use of a company as has been done in this case with the SPV (Be First Developments (Muller) Limited).

- 7.4 If the land were to be disposed of after a minimal period of time, then the site may constitute a trading asset and such a transaction could be likely to be considered a trade.
- 7.5 The loan was lent to the holding company for the purpose of the land acquisition. The necessary loan agreement and was secured on the assets of the SPV. The proposal in this report is to convert that part of the loan which was set at 0% to equity by way of a subscription by the Council for share capital in the SPV. As the SPV owns the land it is reflected in the underlying value of the shares.
- 7.6 The reason that this transaction must come to Cabinet is under the SPV Shareholders Agreement the issuing of shares and financing are reserved matters for the shareholders and the 2020 Cabinet decision did not delegate the power to make financing changes to officers. The key points in the minutes being it decided to:
- (iv) Agree to the Council borrowing the sum set out in Appendix 3 to the report, to finance the acquisition of the Former Muller Site including site purchase planning promotion and ground investigations works subject to all necessary due diligence dependant on confirmation, or otherwise of the site being a Transfer of a Going Concern.
 - (v) Agree to the formation of a new development holding company 'Be First Development (Holdings) Ltd' on the terms set out in the report, to be owned by the Council and hold Be First Developments (Muller) Limited as its subsidiary and to authorise the Chief Operating Officer to take all necessary action in connection with the creation of the company as Shareholder and Chief Operating Officer, in consultation with the Director of Law and Governance, including agreeing an interim business plan, Shareholder Agreement, making any necessary resolutions and entering any other associated legal documents and contracts to give effect to this proposal;
 - (vii) Authorise the Chief Operating Officer, in consultation with the Director of Law and Governance, to agree the loan agreement and any associated guarantees and debentures referred to in the report and grant any indemnities subject to all necessary due diligence;
- 7.7 As following the successful disposal of the Muller site the SPV would effectively no longer have an interest in any 'Muller' entity or asset, it is proposed that the company is wound up.
- 7.8 In summary, this report seeks authority to address a concern regarding the current arrangement's robustness to the question of public subsidiary by virtue of the 0% content of the loan and sets out a proposed chart to go forward. Furthermore, it proposes the opportune disposal of the Muller site asset on terms that would broadly deliver the business plan and significant earnings for the Council. As the Council is the 100% shareholder and these matters are matters reserved for the shareholder and under the Shareholders Agreement, it is a Cabinet decision. It is proposed that the Council's Managing Director will act as the agent of the shareholder to ensure the shareholder decisions are executed.

8. Other Implications

8.1 Risk Management

Risk/Issue	Description/Mitigation
Risk (1)	Risk: No amendment is made to the loan and there is a challenge under public subsidy principles that the funding facility is not market facing. Mitigation: The 0% element of the loan is converted to share capital and confirmed as an equity investment.
Risk (2)	Risk: The offer is not accepted, and the financial objective of the Business Plan is not accepted. Mitigation: Delegated authority is given to the Managing Director to negotiate the best terms available with the selected party.
Risk (3)	Risk: The GIS reveals increased level of contamination. Mitigation: the findings of the original and revised GIS are contrasted to determine the significance of change to determine if it is material.

Public background papers used in the preparation of the report: None

List of appendices:

- **Appendix 1** – Site Plan
- **Appendix 2** – Offer Evaluation Report and Assessment of Best Consideration (exempt document)
- **Appendix 3** – Legal Advice on the Loan GWLG October 2021 (exempt document)