

CABINET

18 October 2022

Title: Land at London Road / North Street, Barking – Extension of Development Loan	
Report of the Cabinet Member for Regeneration and Economic Development	
Open Report with Exempt Appendices (relevant legislation: paragraph 3 of Part I of Schedule 12A of the Local Government Act 1972)	For Decision
Wards Affected: Abbey	Key Decision: Yes
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Summary By Minute 33(viii) (20 October 2020), Cabinet has approved a development loan of £44m to Robyna Limited to facilitate the development of the former White Horse site and adjacent bus stand at London Road / North Street, Barking. This report provides an update on progress and seeks approval to extend the development loan being provided to the developer in light of the recent significant increases in building cost inflation, whilst remaining within the previously agreed loan criteria.	
Recommendation(s) Cabinet is recommended to: (i) Approve the extension of the development loan to Robyna Limited in respect of the London Road / North Street development from £44m to £52m on the terms set out in Appendix 1 to the report in light of the recent significant increase in building cost inflation; (ii) Delegate authority to the Strategic Director, Inclusive Growth, in consultation with the Cabinet Member for Regeneration and Economic Development, the Strategic Director, Finance and Investment and the Chief Legal Officer, to agree the documents to fully implement and effect the proposals set out in the report; and (iii) Authorise the Chief Legal Officer, or an authorised delegate on her behalf, to execute all the legal agreements, contracts and other documents on behalf of the Council.	

Reason(s)

To assist the Council in achieving its Inclusive Growth priorities including the delivery of a high-profile mixed-use development on a key gateway site to Barking Town Centre that would provide much needed affordable housing units.

1. Introduction and Background

1.1 On 20 April 2021, Cabinet re-confirmed and amended its various earlier resolutions of September 2018, March 2020 and October 2020, to enter into a residential-led joint development scheme with a developer (Robyna UK Ltd) on land separately owned by the Council and developer, whereby the Council would acquire the freehold ownership of the developer's site and, upon completion of the scheme, grant the developer a head lease on the combined sites for 250 years subject to the payment of a head rent. In addition, the Council would provide the developer with a construction loan of up to £44m. Cabinet also approved the acquisition of the Developer's land pursuant to section 227 of the Town and Country Planning Act 1990 and the appropriation of the Council's land for planning purposes pursuant to section 122 of the Local Government Act 1972.

1.2 The initial Cabinet report in September 2018 set out the rationale for the transaction and considered the following options before adopting Option 3:

Option 1 – Do Nothing.

Approximately one half of the site is outside the control of the Council. Should the decision be taken to 'do nothing', it is possible that Robyna Ltd will seek to bring forward a lesser scheme in isolation on their own land. It is unlikely that such a scheme would deliver the full planning potential of this key, landmark site and will not release any marriage value to be shared with the Council from the merging of the two parcels of land in a comprehensive, larger scheme. There would be a lower rate of new homes bonus, Council tax and business rates. This principle also relates in isolation to the Council's own portion of the site.

If agreement cannot be reached to work together with the Council, Robyna Ltd may delay or even abandon plans for redevelopment. This will result in the continuation of the 'eyesore', with the on-going potential for antisocial use.

The Council could continue to lease their own site to TfL as a bus lay-over yard but seek to negotiate a rent – although this may be challenging given the shared objective of supporting bus service provision.

Option 2 – Develop in isolation.

The Council could develop its portion of the site in isolation but, as noted above, it will fail to benefit from a larger, more efficient and ambitious scheme with the associated regeneration benefits.

The Council could try to acquire Robyna Ltd's land through compulsory purchase however this is unlikely to be successful given their desire to deliver development.

Option 3 (Favoured Option) – Enter into agreement with Robyna Ltd to acquire, fund the development (up to 80%) and hold long term

Through the proposed approach, whilst the Council will not be leading on the delivery of the scheme, control will be retained via the head lease arrangement

under which an annual head rent will be paid. The scheme also compliments and is integral to the overall regeneration vision of the wider Town Centre. The leasehold arrangement allows the Council to benefit from the regular income generated from the site although it exposes the Council to risk if the site is not developed or the Council has to step in.

To bring this key site forward for regeneration and maximise the site through an enlarged scheme across the two ownerships, the Council should engage and treat with the adjoining landowner, Robyna Ltd. Enhanced due diligence has not raised issues with Robyna Ltd but the Council will take steps to ensure that full measures are put in place to take early control of the land including contractual step in rights in the event of default. Robyna Ltd would fund the remaining 20% of costs from their own equity (ie no other lender). Development finance payments will be staged on periodic independently certified construction work to reduce risk, however it is acknowledged that stepping in may result in additional costs and delays to enable the building to be completed.

Option 4 – As Option 3 but without providing development funding.

The ability for the Council to fund the scheme, whether up to the agreed proportion in Option 3 or a lesser amount (Option 5), provides a further degree of control over the scheme being brought forward. In the event of developer default, the Council would have direct rights to step in and complete the development. Third party funders would typically require their own preferential step in rights to sell the scheme, potentially leading to significant 'stand still' periods on site. Lenders will also wish to have control over the land during construction by way of a first legal charge over the remainder. This would introduce issues of priority in the event of joint Council/lender funding situation.

The opportunity to generate a further income stream for the Council during construction would also be lost.

Option 5 – As Option 3 but with Council just providing 50% of Development finance.

A lower percentage of development finance would reduce the amount of Council borrowing required, however it would also result in lower returns and less control as set out for Option 4. This particular option would introduce issues of priority in the event of the Council and another lender both funding the scheme. Another funder would typically seek to rank first and such negotiations would delay progress alongside the control risks set out for option 4.

Option 6 – Sell Council land to Robyna Ltd or another party

The Council could sell its landholding to Robyna Ltd who would then be likely to progress the development proposal independently of the Council. A one-off capital receipt would be generated however it would fail to give the Council the ability to secure a long term rental income stream, the returns from development finance and a role in ensuring the development comes forward, together with the quality and content of the scheme. Selling the site to another party would similarly result in potential for the site to lie empty and not deliver the additional homes delivered by a combined scheme

- 1.3 The March 2020 Cabinet agreed to use its appropriation powers to help bring forward the scheme, and in October 2020 it was agreed to increase the loan up to £44m due to the increased size of the development. Finally in March 2021, Cabinet

agreed to amend the site area to reflect the planning consent and change the identity of the developer to a wholly owned UK subsidiary, Robyna UK Ltd.

- 1.4 The development secured planning consent in February 2021 and will provide 196 residential units, of which 35% will be affordable for the duration of the head lease (250 years) at no cost to the Council.
- 1.5 On 21 January 2022 the Development Agreement, Loan Agreement and other associated documents were exchanged between the Council and the developer. As anticipated by the agreement, the Council immediately took ownership of the developer's land (the site of the former White Horse Public House) at nil cost. The developer then commenced consultation with adjoining interests, as required before the Council could appropriate the site, and continued to finalise its development plans in order to satisfy the conditions precedent before work can commence.
- 1.6 The Council appropriated the site on 5 September 2022.
- 1.7 The Council has also now made good progress with securing vacant possession of the Transport for London (TfL) bus stand on part of the site by providing three alternative stands in close proximity. This work is expected to complete by end October 2022.

2. Proposal and Issues

- 2.1 In light of the recent significant increases in building cost inflation, construction costs for the development project have risen materially. Whilst this has been largely offset by an increase in the gross development value, the developer is seeking to extend the development loan being provided by the Council on the terms set out in the attached Part 1 of Appendix 1, 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.
- 2.2 This additional facility will be on the same loan criteria as originally agreed (notably the loan to value & loan to cost ratios) and over the same time period (30mths). It will also be subject to the same protection to take over the development should the developer default. These are detailed further in Part 1 of Appendix 1.
- 2.3 Most notably the additional funding will allow the developer to proceed with the development without seeking alternative additional sources of funding which may not be available on commercial terms, thereby allowing the scheme to proceed.
- 2.4 The developer has agreed to meet the Council's costs of amending the documentation to accommodate the extra lending and will additionally make a further contribution towards the cost of relocating the bus stand which the Council is committed to remove at its cost.
- 2.5 Additionally, in order to allow sufficient time for the documentation to be amended and the bus stand to be moved, it is proposed to extend by 6 months the deadlines in the existing loan and development agreements.

- 2.6 The additional lending increases the return the Council will receive from providing the loan as illustrated in the model at Appendix 2.
- 2.7 Updated valuation and loan reports have been commissioned (at the expense of the developer) in order to satisfy both the requirements of S123 of LGA 1972 and subsidy control (formerly state aid). The final lending will be subject to confirmation of satisfactory compliance.
- 2.8 Additionally, agreement to the additional loan facility will be subject to re-running enhanced due diligence on the developer.

3. Options Appraisal

- 3.1 **Do Nothing:** The Council is still committed to provide the development loan as previously agreed should the developer satisfy the conditions precedent in the Development Agreement. These include a requirement to demonstrate to the Council that it has sufficient funding to proceed with the development. If the loan extension is not provided, the developer will need to secure the additional funding from alternative sources or equity. As the Council are the principal lender for the development this may not be available at commercial terms to allow the development to proceed. This would result in the development agreement terminating and the development will not take place.
- 3.2 **Loan Proposal:** The recommended option is to provide the additional debt to the developer at the enhanced rate proposed. This will enable the development to proceed and deliver much needed affordable homes within the borough at this gateway to Barking town centre. The additional facility will be subject to the same loan covenants as before with the developer only securing a long interest in the property upon completion of the scheme.

4. Consultation

- 4.1 The proposals in this report were considered and endorsed by the Investment Panel at its meeting on 20 September 2022.

5. Financial Implications

Implications completed by: David Dickinson, Investment Fund Manager

- 5.1 The detailed assessment of the financial implications is set out in Part 2 of Appendix 1, 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. Below is a summary of other considerations.
- 5.2 **Subsidy control (formerly state aid)** - This is being carried out by Gowling. The loan should only be agreed if this has been satisfactorily signed off by Gowling prior to a report going to Cabinet.

- 5.3 **Due Diligence** - Be First have carried out some due diligence on Robyna and its parties that are associated with them. The Due Diligence completed has not raised any issues.

This due diligence was carried out a number of years ago and an update of this to take into account the financial viability of the various companies as well as the enhanced due diligence requirements, should be completed prior to a report going to Cabinet.

- 5.4 **Reputational Risk** - On-lending by a Council has additional reputational risks as, potentially, the borrower has been unable to obtain a loan from usual banking and private financing sources and has therefore approached the Council for financing.

It is important that comfort is obtained that the borrower is of sufficient quality and that any potential reputational risk has been minimised to fit within the risk parameters that the Council is willing to take prior to the report going to Cabinet in September 2019.

The source of both the initial funding from Robyna and the subsequent repayment of the loan to the Council is potentially an area where fraud and / or money laundering can occur. It will be essential for any final agreement to provide clarification of Robyna's source of funding.

6. Legal Implications

Implications completed by: Gowling WLG (external lawyers for the Council) and Ann Towndrow, Property Lawyer

- 6.1 Gowling WLG have reviewed the proposed variation to the loan terms and the extension of the ultimate conditions longstop date from a subsidy control (formerly state aid) and procurement perspective and have reported accordingly.
- 6.2 The increased loan should not constitute a subsidy as it is being provided on market terms. This is the basis on which the original loan was approved albeit the sign off on this will need to come from Avison Young (GVA's new owner) rather than Gowlings and we understand that a report from Avison Young is awaited. Paragraph 3.4 of the original report sets out the further details which Avison Young will need to consider.
- 6.3 There has been a change in the public subsidy regime (following Brexit) and we are currently in something of a limbo period pending the coming into effect of the Subsidy Control Act later this year. However, the terms of the new Act provide that "financial assistance is not to be treated as conferring an economic advantage on an enterprise unless the benefit to the enterprise is provided on terms that are more favourable to the enterprise than the terms that might reasonably have been expected to have been available on the market" (section 3(2)).
- 6.4. Regarding procurement, the development agreement is a public works contract which was exempt from procurement under Regulation 32 (see paragraph 4.5 of the original advice).

- 6.5. On that basis, it can only be varied in the circumstances permitted by Regulation 72. We anticipate that the variation to extend the ultimate conditions longstop date will fall within one or more of those circumstances.
- 6.6. For example, Regulation 72(1)(e) permits a variation where it is not considered substantial (meaning that the change does not: render the contract materially different; introduce conditions which may have resulted in a different conclusion to the procurement process (if any); change the economic balance of the contract in favour of the contractor; considerably extend the scope of the contract or replace the original contractor). We consider that the proposed variation would not be substantial and that the variation would be permitted under Regulation 72(1)(e). No notice would need to be published following the variation.
- 6.7 Full legal implications were included in the report to Cabinet in September 2018, including the Council's powers to participate in the transaction under section 1 of the Localism Act 2011 and the powers in s111 of the Local Government Act 1972 to do anything calculated to facilitate or conducive to the discharge of any of its functions including borrowing or lending money.
- 6.8 The exercise of powers is subject to use for a proper purpose and the usual reasonableness constraints. Investment decisions must also be made in compliance with all relevant statutory guidance relating to Local Government Investments, and with regard to the Council's fiduciary duty to taxpayers. An overall Investment Strategy should include consideration of total financial exposure, credit risk, credit controls and that the total loan book is within self-assessed limits

7. Commercial Implications

Implications completed by Hilary Morris, Commercial Director

- 7.1 This paper proposes to increase the loan to the developer to reflect increased construction costs whilst retain the existing loan criterion and security provisions approved by Cabinet in 2018.
- 7.2 Key security for the Council include a legal charge over the loan asset and full step-in rights in the event of borrower default which would enable the lender (the Council) to complete the scheme if needed.

8. Other Implications

- 8.1 **Property / Asset Issues** - The property transaction will not vary from that previously approved and contracted. The Council will retain the freehold of the site throughout and will only grant the developer a long leasehold interest upon satisfactory completion of the development.

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

List of Appendices:

- Appendix 1** - Revised Loan Proposals & Financial Implications (exempt document)
Appendix 2 - Revised Loan Model (exempt document)