

<b>25 March 2015</b>		<b>ITEM: 10</b>
<b>Council</b>		
<b>Gloriana Thurrock Ltd (“Gloriana”) – Proposed Development of St Chad’s site, Tilbury – Gateway 3 Report</b>		
<b>Wards and communities affected:</b> St Chad’s	<b>Key Decision:</b> Key	
<b>Report of:</b> Portfolio Holder for Finance and Education – Cllr John Kent		
<b>Accountable Head of Service:</b> Sean Clark, Head of Corporate Finance (S151 Officer)		
<b>Accountable Director:</b> Graham Farrant, Chief Executive		
<p><b>This report is public.</b> However appendices 1 and 2 are exempt <i>by reference to the descriptions in Schedule 12A of the Local Government Act 1972</i>, due to information relating to the financial or business affairs of any particular person (including the authority holding that information). <i>It is hereby marked as being not for publication and the press and public are likely to be excluded from the meeting during consideration of any confidential or exempt items of business to which the report relates.</i></p>		

### **Executive Summary**

This Gateway 3 report provides an update on Gloriana’s proposals, to develop St Chad’s Road site in Tilbury, in order that Council can give final approval to enable both the freehold land to be transferred to Gloriana and the Council to borrow and advance funding for the scheme to Gloriana.

This is the final Gateway stage in the pre-construction process. Since the last report to Cabinet in December 2014, the scheme proposed for St Chad’s site has received full planning approval. Gloriana is working towards a start on site with enabling works as soon as possible and a full start on site by the proposed contractor by 1<sup>st</sup> June 2015.

The Gloriana Partnering Board met on 3<sup>rd</sup> March 2015, in accordance with the agreed governance structures for this work, and noted that, following the full Council meeting of 25<sup>th</sup> February, the Gateway 3 position as set out in this report will now be considered by full Council on 25<sup>th</sup> March 2015. In summary, the Gateway 3 position is that the scheme’s financial parameters are less favourable than those estimated in previous reports due to rapidly rising construction costs. However, when Cabinet agreed the Final Business Case for Gloriana it was acknowledged that some schemes would show lower returns than others and St Chad’s has always been

recognised as a very difficult site to develop. Despite the increased cost of construction, the scheme still provides a healthy financial return to the Council.

The proposed contractor is currently obtaining sub-contractor tenders in order to offer a fixed price contract to Gloriana for the works and, when this is received, the financial modelling will be reviewed again.

However, this fixed price tender will not be received until April 2015 when purdah requirements will mean that a further Council report will not be possible without delaying start on site for the scheme – and potentially resulting in further increases in construction costs.

Officers have worked with the contractor to produce a best possible final estimate, including contingency, to allow for this and so this report proposes that delegated authority is given to the S151 Officer, in consultation with the Chief Executive and the Portfolio Holder for Finance and Group Leaders, to approve the land transfer and scheme funding to Gloriana and related amendment to the Council's prudential borrowing. This delegated authority will be subject to the scheme meeting key financial parameters.

## **1. Recommendation**

- 1.1 That it be approved that Gloriana develop the St Chad's site in Tilbury in accordance with the consented planning application.**
- 1.2 That authority be delegated to the S151 Officer, in consultation with the Chief Executive and Portfolio Holder for Finance and Group Leaders, to agree the land transfer to Gloriana and the final funding, including a form of guarantee as required, when the construction tender is submitted in April, and to enter into legal agreements as required, but subject to the financial parameters as set out in the report.**
- 1.3 That, with reference and subject to 1.2, it be approved that there be a variation to the Council's prudential borrowing limits and capital programme accordingly and that the Head of Corporate Finance be instructed to put in the necessary arrangements to secure the required funding.**

## **2. Introduction and Background**

- 2.1 The Final Business Case (FBC) to set up Gloriana was approved by Cabinet in March 2014 and the agreed governance arrangements for Gloriana provide for a series of Gateway approvals to each scheme.
- 2.2 In December 2014 Cabinet approved the Gateway 2 report for the St Chad's site and, subsequent to that, a full planning application for the scheme was submitted. This was approved on 5<sup>th</sup> February 2015.

- 2.3 This report provides the Gateway 3 report (including update to the FBC) and, assuming Council approval is forthcoming, the next step is that the Land Transfer, Management and Funding Agreements between the Council and Gloriana are entered into and Gloriana enters into a construction contract.

### **3. Issues, Options and Analysis of Options**

#### **Scheme Overview**

- 3.1 Since Gateway 2 approval, detailed design discussions have progressed with the proposed contractor with a view to finalising their fixed price tender for the scheme. As noted at FBC, the St Chad's site is difficult to develop because of the extent of piling necessary and the requirements for flood mitigation and sustainable urban drainage (SUDS). In addition the desire for a quality, exemplar scheme which can kick start the regeneration of Tilbury means that cost savings are less easy to achieve. Nevertheless value engineering has been, and is, forefront in the minds of both the design team and the proposed contractor.
- 3.2 The scheme mix and numbers remain unchanged since the last Gateway report in December with 128 terraced and courtyard houses in a grid pattern of avenues, streets and mews that echoes the mid-20<sup>th</sup> century street pattern. A sequence of public spaces and a linear park arranged diagonally connect with the surrounding countryside. There are eight 4bedroom houses but predominantly 2 and 3 bedroom houses.
- 3.3 The initial proposed tenure mix is 100% affordable rented housing. However, the sales market has shown good growth in Tilbury over recent months and, as construction progresses, the option to sell some properties outright or on a shared equity basis will be reviewed.
- 3.4 A final fixed price tender is expected in April 2015 and enabling works will start as soon as possible with a full start on site by the proposed contractor by 1<sup>st</sup> June 2015.

#### **Risk Assessment**

- 3.5 The risk register approved by Cabinet at FBC stage has been kept under review. All site related risks have now been dealt with, following receipt of planning approval. The key risks at this stage are financial viability and state aid compliance due to a worsened financial situation since Gateway 2.
- 3.6 The financial position is discussed in more detail below.
- 3.7 The state aid regulations are complex and intrinsically related to the financial viability. However, whilst the financial position is less favourable than that projected at Gateway 2 this does not preclude meeting state aid requirements. The Council's legal officers are taking expert advice and the scheme will not

proceed unless it is state aid compliant. Initial indications are that this should not be an issue.

### **Financial Projections**

- 3.8 As explained at FBC, the Council’s financial advisers have developed a financial model (“model”) to assess whether Gloriana can be established on a viable basis. This model considers the cashflow, tax and accounting implications of Gloriana’s proposed developments and also considers the cashflow and accounting entries impacting the General Fund. It can be used for each scheme on a stand-alone basis to examine whether the viability tests are met.
- 3.9 The model has been refined since the last Gateway report to reflect the fact that Gloriana is now moving towards live construction activity and major capital expenditure. As a result, Gloriana now has a robust model capable of being updated on a regular basis, with current data, as the St Chad’s site is developed out. This will enable up to date progress reports to be produced for Gloriana and the Council as required.
- 3.10 The inputs and assumptions for St Chad’s have been reviewed and will be subject to continuing review as construction progresses. Key changes are as follows:
- 1) Overall development costs by Gloriana have increased since the Gateway 2 stage reflecting continuing price increases in the construction sector.
  - 2) The land value has fallen reflecting the difficulties in developing the site.
  - 3) Total rental income over the period has fallen slightly, as has income from sales, reflecting more prudent assumptions regarding timing.
  - 4) Borrowing costs have fallen reflecting current interest rates and interest rate projections.
  - 5) As a wholly owned company the Council in effect stands behind Gloriana. However, depending on the final negotiations with the proposed contractor, it is expected that a formal Council guarantee will be required and an assumed cost for providing this has been included in the model.
- 3.11 A narrative summary of the current position is set out below and by way of update to the FBC. The detail of the latest inputs to the financial model and the resultant outputs are shown at Appendix 1.

<b>Input</b>	<b>Commentary</b>
Tenure Mix	All dwellings are let at affordable rents (80% of market rent). Sales either outright or on a shared equity basis are not precluded but will be dependent on demand and, as at FBC, no sales are assumed initially.

Construction Programme	1 <sup>st</sup> June 2015 to 1 <sup>st</sup> February 2017.
Land Cost	Independent valuation prior to land transfer.
Construction Costs	These are based on the proposed contractor's latest cost estimates and include planning and design costs. Costs have increased since the last Gateway report reflecting demand in the construction sector continuing to outstrip supply.
Sales Profile	Over time it is assumed that all affordable rent properties are sold either to the tenants or individual purchasers or to other providers. A prudent sales programme has been assumed.
Sales Values & Overall Sales Income	Sales values are based on recent market information and will be uplifted by house price inflation (see below) to the sale date. Overall income from sales of dwellings has been reduced slightly since Gateway 2.
Rental Income	Rents are based on recent market information. Rents are set at 80% of current market rents and are in all cases within current Local Housing Allowance figures. They will be uplifted by inflation (CPI – see below) plus 1%, in line with government policy for affordable rents, to the letting date. Overall rental income has fallen within the model since Gateway 2 as a result of more prudent assumptions regarding initial letting dates.
Operating Costs	Management and operating costs reflect the cost of the services provided by the Council to Gloriana on a full commercial basis. At this stage it is not considered that any additional management or operational staff will be required to deal with Gloriana's requirements. Therefore this arrangement should lead to efficiency savings within the HRA and a small net income within the General Fund resulting from the margin charged on top of direct costs to Gloriana. Maintenance and lifecycle costs reflect industry norms.
Bad Debts & Void Losses	This reflects a prudent allowance and is informed by the Council's experience of managing its own stock and experience of other providers.
Central running costs	An annual sum is included to cover accounting, insurance, IT and other central support costs which will be payable to third parties.
Inflation Factors	General inflation (CPI) and other inflation factors including house price inflation assumptions are based on relevant independent data.
Interest Rates	The interest rate which the Council is assumed to pay on its borrowing reflects PWLB rates. Funds on-lent to Gloriana will attract a margin which is based on current prescribed margins for state aid compliancy.

## Financial Parameters

3.12 In looking at the results of the financial modelling, the following underlying principles and parameters were agreed at FBC stage:

- 1) **Impact on General Fund.** Interest payable in the General Fund, as a result of the PWLB loans taken out to provide loans and equity finance to Gloriana, should be covered by interest receivable from the loans to Gloriana.
- 2) **Council equity return.** From a commercial perspective the Council needs to be satisfied that best value is generated by investing cash and land within Gloriana and that the return reflects a position that does not involve the provision of unlawful state aid.
- 3) **Gloriana financial viability.** Gloriana will be consolidated into the Council's group accounts and, therefore, the Council must be satisfied of Gloriana's overall financial position and ability to repay its loans.

3.13 At this Gateway stage the position is as follows, taking each parameter in turn:

- 1) The financial model shows that the interest payable by the Council, in respect of loans taken out to fund Gloriana, will be met from interest payable by Gloriana to the Council. In summary, this parameter is met.
- 2) As noted at FBC, the returns which the St Chad's site can be expected to generate are at the lower end of the acceptable range, reflecting the high cost of developing given the ground conditions. This position improved slightly at the last Gateway stage but has worsened since then. However, this is not out of line with market trends. The contractor's current estimate, with an element of contingency included, does meet this parameter. When Gloriana receives the final tender for the scheme the projected return must meet state aid requirements and this will be a key parameter in relation to approval to proceed.
- 3) The latest projections confirm Gloriana's financial viability and also that it will be able to operate as a going concern and repay its loan from the Council based on current known information and assumptions utilised within the model. The final parameter is therefore met.

3.14 In summary, when the final Gateway 3 position is known following receipt of the construction tender, the above three parameters will be re-assessed and all three will need to be satisfied for the scheme to proceed.

#### **4. Reasons for Recommendation**

4.1 Development of the St Chad's site will provide quality exemplar housing to meet housing needs and improve the lives of Thurrock residents as well as to counter current problems of stalled sites and low market confidence. Given the pending election and the fact that the final tender price for the construction contract will not be received until the Council is in purdah, the

recommendation in this report is designed to allow there to be no delay to the scheme start.

- 4.2 It is proposed that Council give delegated authority to the S151 Officer, in consultation with the Chief Executive and the Portfolio Holder for Finance and Group Leaders, to agree the final Gateway 3 position when the construction tender is submitted in April 2015 but subject to meeting the financial parameters set out in this report.
- 4.3 The estimated cost of construction and thus the level of borrowing that the Council will have to undertake are shown in the appendices and the final figures will be shared with the Portfolio Holder for Finance and the Group Leaders as part of the delegated authority process for approval. The Full costed Business Case has been made available in advance of this meeting.

## **5. Consultation (including Overview and Scrutiny, if applicable)**

- 5.1 The cross party Partnering Board, set up under the governance arrangements for Gloriana, has met and been kept informed of progress. Planning Committee has agreed the design of the scheme. Resident and community consultation has and taken place on the site proposals and the Housing Development Board which comprises Members and residents as well as Officers has been, and will be, kept updated as the scheme progresses.

## **6. Impact on corporate policies, priorities, performance and community impact**

- 6.1 Gloriana has been established to support the Council's growth agenda and will help deliver the Council's target of 1,000 new affordable homes in the Borough over the next five years. By enabling Gloriana to develop high quality housing on land that it owns the Council will provide an alternative route to private sector led regeneration which has been heavily constrained by the prevailing economic conditions. Such housing will contribute to improving wealth and increasing land values and to creating great places where community pride, good health and wellbeing and economic prosperity will thrive.

## **7. Implications**

### **7.1 Financial**

Implications verified by: **Sean Clark**  
**Head of Corporate Finance (S 151 Officer)**

The financial model within the FBC needs to demonstrate that any development is both viable for the Company and the Council.

St Chad's is the first scheme to reach Gateway 3 where material financial commitments will arise. It is critical that any authority delegated by Council requires the scheme to meet the financial parameters set out in this report. At its budget meeting in February 2014 the Council agreed that approval for any prudential borrowing for the purpose of providing funding for Gloriana should also be sought at the time of scheme approval and this recommendation has been included in this report.

## 7.2 Legal

Implications verified by: **Assaf Chaudry**  
**Major Projects Solicitor**

Gloriana's activities are within the Council's powers. Assuming Council approve the recommendations in this report, the final position will be checked with external legal advisers to confirm that state aid requirements are met. The legal agreements, including the formal Council guarantee, will be finalised, also with external legal advice, in preparation for signature between the Council and Gloriana. Approval will constitute a confirmation of the Council's approval of the FBC in the light of the updated circumstances.

## 7.3 Diversity and Equality

Implications verified by: **Rebecca Price**  
**Community Development Officer**

Development of the St Chad's site in Tilbury will have a positive impact on Tilbury and especially the availability of affordable housing. Gloriana's developments will follow Council policies in relation to diversity and equality and, in particular, will ensure that contractors bidding for work from the Company will follow the Council's Equality Codes of Practice on Procurement and will deliver social value through local labour initiatives, including training and apprenticeships.

## 7.4 Other implications (where significant) – i.e. Staff, Health, Sustainability, Crime and Disorder)

None

## 8. Background papers used in preparing the report (including their location on the Council's website or identification whether any are exempt or protected by copyright):

- Final Business Case for Commencement of Operations by Gloriana Thurrock Ltd, Cabinet Report, March 2014
- Cabinet Report - Progress on Gloriana, December 2014



## **9. Appendices to the report**

- Appendix 1 – Inputs to the Financial Model (Exempt)
- Appendix 2 – Outputs to the Financial Model (Exempt)

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