

Gloucester City Council

Meeting:	Cabinet	Date:	15 June 2022
Subject:	Kings Quarter The Forum Phase 2 Approval		
Report Of:	Leader of the Council		
Wards Affected:	Westgate		
Key Decision:	Yes	Budget/Policy Framework:	No
Contact Officer:	Philip Ardley, Regeneration Consultant - Place		
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Appendices:	A. Hotel Operator Recommendation Report		
	B. Car Park Operator Recommendation Report		
	C. Phase 3, Plot 3c Recommendation Report		
	D. Business Plan January 2022		
	E. The Forum Site Plan		

EXEMPTIONS

The public are likely to be excluded from the meeting during consideration of appendices A to D of this report as they contain exempt information as defined in paragraph (3) of schedule 12A to the Local Government Act 1972 (as amended). All sections of these appendices A, B, C and D are considered confidential and commercially sensitive.

1.0 Purpose of Report

1.1 To secure approval for a recommendation to Cabinet that they authorise Officers to enter into a legally binding contract with the successfully tendered Hotel Operator and Car Park companies to deliver these elements of Phase 2 for the Kings Quarter The Forum mixed use development. Additionally, to enter into a building contract with E G Carter for the continued construction of the residential apartments on plot 3c in Market Parade in accordance with the planning permission granted and as envisaged by the Development Funding Agreement approved by Council on 28th January 2021.

2.0 Recommendations

2.1 Cabinet is asked to **RESOLVE** that:

- (1) the Head of Place in consultation with the Leader of the Council and Cabinet Member for Environment, the Director of Policy and Resources and the Council Solicitor is authorised to complete the acquisition of the remaining property interests in Market Parade, plot 3c, and enter into a JCT Building Contract with the successfully tendered construction company E G Carter to implement the second phase of the residential apartments forming part of Kings Quarter The Forum as set out in Appendix C of this report.

- (2) authority be delegated to the Head of Place in consultation with the Director of Policy and Resources and the Council Solicitor to take all necessary steps and undertake necessary procedures, including entering into any legal arrangements or other documentation as may be required to implement or facilitate Phase 2 Kings Quarter The Forum for the operation of the Hotel and Car Park together with the development of the residential apartments on plot 3c.

3.0 Background and Key Issues

- 3.1 This report seeks approval for the continuing delivery of Phase 2 Kings Quarter The Forum and directly relates to approvals and the previous updates submitted to Cabinet on the 11th March 2020, 17th June 2020, 13th January 2021 and 8th December 2021, and to Council on 28th January 2021.
- 3.2 It was reported in the last Cabinet paper that there was considerable occupier interest being generated in Kings Quarter. The officers and our development partner are pleased to be able to report that good progress has been achieved with negotiations resulting in two shortlisted high quality hotel chains and two national car park operators for the respective buildings on plot 2.
- 3.3 Appendix A from our Development Partner now sets out a recommendation for the preferred operator for the hotel and compares a summary financial return with the alternative shortlisted operator. Following detailed negotiations with Heads of Terms there has been a slight improvement in the financial return to the City Council, seeing the base fee reduced and a lower tiered incentive fee. There are two financial options available from the preferred operator and option 1 is favoured.
- 3.4 In the present hotel market conditions, leases are generally no longer on offer and hotels are effectively a franchise with the Owner taking the majority of the risk and reward.
- 3.5 It is proposed that the hotel operator will employ the General Manager direct, but all other staff will be employed by the Owner (City Council). It is recommended that the City Council set up a Company for all operational income, expenditure and staffing matters and that a rental is paid to the Council. Our solicitors will be consulted to advise on the proper management of all risks associated with the employment and company procedures.
- 3.6 Appendix B sets out a similar recommendation from our Development Partner for the operator of the multi-storey car park. This follows advice from specialist car park consultants, Town Centre Parking (TCP), and further recent visits to primary car parks in both Birmingham and Manchester city centres. Summary financial returns are compared from the two preferred operators together with more detailed analysis provided by TCP.
- 3.7 Both operators are nationally recognised as major specialist car park managers and we believe that either company could provide an excellent service for The Forum car park. The two companies were relatively close on the evaluation criteria but the recommended operator appears to be slightly ahead on quality of service and innovation which was evident during our recent inspection visits in Birmingham and Manchester. Additionally, we believe that the appearance and feel of the recommended operators car park will be more in keeping with the four star hotel.

There is very little difference in terms of financial return.

- 3.8 Appendix C sets out the latest financial position for completing the remainder of the residential apartments on Market Parade plot 3c, for which full planning consent was granted with plot 3b which is now under construction by E G Carter with completion due in October this year.
- 3.9 There are two options for acquiring the necessary property interests clearly set out in Appendix C either by using Compulsory Purchase powers, which has already approval in principle from Cabinet, or by private treaty with a summary of the benefits and disadvantages of each option. The present forecast construction cost inflation of 10.2% annually and the advantage of E G Carters continuing with their existing site set up immediately following completion of plot 3b has a significant influence in viability for the 24 apartments.
- 3.10 We have received solicitors advice regarding the procurement of the contract with E G Carters which is favourable as the contract is effectively an extension of the existing arrangement under the County Councils Framework Agreement and entered into between our Development Partner and the contractor direct.
- 3.11 Despite the advantages set out in the recommendation report and issues highlighted in 3.9 above, there is a substantial negative value realised from this development in the short term if the apartments were to be sold immediately. This possibly could be set off against the entire Kings Quarter development over say the first 10 years. Alternatively, open market letting of the apartments for a period of years may be the more attractive option. The total rental value should exceed borrowing costs by as much as 50% showing a healthy additional income for the City Council. This is the recommended option and legal advice should be sought for short term holding of the properties to mitigate the Right to Buy.
- 3.12 Appendix D consists of the latest version of the Kings Quarter The Forum Business Plan with updates following the completion of the building contract with Kier Construction in January 2022.
- 3.13 The viability of the whole scheme remains challenging especially in the early years as a result of the current unprecedented circumstances. However, viability has slightly improved as a result of anticipated increasing rental values and shorter rent free periods forecast by our letting agents following initial offers from potential occupiers.
- 3.14 Whilst this is an extremely significant investment it provides a massive opportunity to regenerate the city centre thereby benefitting the Kings Walk shopping centre including many surrounding properties. The enhanced railway station, modern Transport Hub, recently opened and refurbished Kings Square and the major investment by the University of Gloucestershire will result in an impressive gateway into the city centre as well as creating very significant employment opportunities both in the short and longer term. The success of the application for £3.98m grant monies for The Forge business centre from the Government's Levelling Up Fund considerably assists risk mitigation. Furthermore the £9.70m grant from the same source to assist in converting the presently vacant old Debenhams building is a tremendous confidence booster. The City Council will own the entire Kings Quarter The Forum development on completion and benefit

from all income.

4.0 Social Value Considerations

- 4.1 The social value of the Council's plans for Kings Quarter are considerable and the Officers and Development Partner have been working with the Council's Economic Development Team to maximise this impact with involvement from our specialist consultants the Social Value Portal.
- 4.2 The joint development proposals for Kings Quarter expect that over the next 3-4 years an additional 1,000 new job positions could be created in the city centre. Our Development Partner is putting in place a task force to ensure that a programme to help the local community upskill appropriately is created and the development is fully linked to the new digital access programmes at local Higher Education and Further Education institutions. This may also be part of The Forge offering. The construction tender process has included clear guidance and expectations for delivering these community benefits, all in accordance with our Social Value Policy.
- 4.3 Kier Construction are presently undertaking extensive refurbishment of NEM House in Clarence Street which will include a community learning hub on the ground floor. This was included in their detailing of Social Value proposals which have been assessed as part of the procurement process and forwarded to the Social Value Portal for measurement in due course.

5.0 Environmental Implications

- 5.1 The proposals emphasise how sustainable design has underpinned the redevelopment of Kings Quarter. All buildings will be constructed with a design life well beyond the 60-year industry standard, with layouts, utilities infrastructure and floor to ceiling heights future proofed for new technologies and uses. For instance, the design has incorporated a way in which the proposed multi-storey car park can be readily converted to alternative use should our current reliance on the car lessen. We have committed to incorporating features such as cycle storage, car sharing systems, electric charging points and have considered how solar panels and green walls and roofs are to be included.

6.0 Alternative Options Considered

- 6.1 The Council Officers did review alternative options to bring forward the redevelopment of Kings Quarter. The options included:
- Solely utilising Public Works Loan Board funding and managing the redevelopment of the site in house using procured contractors for each separate phase.
 - Advertising for a development partner and seeking expressions of interest.
 - Selling the site on a plot by plot basis with planning consent.
- 6.2 There are several disadvantages with each of the reviewed options such as: insufficient internal resources and experience, inability to maintain control over an important council regeneration asset, and significant delay in achieving activity on site at a time when action is required to commence building. They were all rejected.

- 6.3 The significant viability issue on plot 3c for residential use compounded by increasing inflation may be mitigated by considering alternative use of the ground floor with food and beverage being the most viable use at present, but this would be subject to a revised planning application and hence delay and costs.

7.0 Reasons for Recommendations

- 7.1 The proposals offered have the potential to provide a high quality and rapid opportunity for the Council to see its regeneration aspirations for Kings Quarter realised. It would potentially create employment space for over 1,000 new employees, which could equate to over £100m injected into the local economy each year. Being able to secure that number of new workers into the city centre would not only boost the local spend, but the provision of the 18-hour facilities proposed would extend that spending window from presently only working hours, into the evening and night-time economy.
- 7.2 Considerable recent negotiations have taken place both to improve the viability and reduce the risks for this scheme thereby strengthening the City Council's position with regard to defining the viability within the Development Agreement. Significant improvement in the viability has been enhanced by the success of the grant from the Levelling Up Fund as outlined in 3.14 above. At the same time the changes have underlined that the Development Partner arrangement accords with market sentiment and practice with expert experience for such a significant investment.
- 7.3 Extensive due diligence has been undertaken by our external consultants in conjunction with our Director of Policy and Resources, the Head of Place and our regeneration consultant to evaluate and negotiate the financial appraisals. Legal opinion has been provided by Trowers & Hamlins for procurement, state aid and to monitor the Development Agreement. The intention is to continue refining the viability and the financial returns and sign binding legal agreements for the continuing development of this project.

8.0 Future Work and Conclusions

- 8.1 The Council will continue to require the assistance of the property experts and external lawyers to scrutinise compliance with the Development Agreement and to negotiate the legal agreements and contracts required for operators and occupiers as this scheme progresses, and assist your officers as an expert client during the construction and letting phases.

9.0 Financial Implications

- 9.1 Cabinet approval is required to accept the recommendations in this report and the viability to enter into the building contract for plot 3c with E G Carter.
- 9.2 As part of the Development Funding Agreement our development partner has provided a Guarantee for the first five years of the hotel income. This is subject to operator incentives as set out in Appendix A and the cost plan. This ensures early income, avoids the room vacancy risk and results in this building being properly managed on behalf of the City Council. Our Development Partner has also funded the substantial architectural design costs resulting in the full planning consent determination received last year. These costs would only be recoverable, if for any reason, the city council

cancelled the Development Agreement, in which case they become payable on transfer of all necessary warranties and copyright of the proposals.

- 9.3 The current legal and due diligence costs were budgeted for within the original Kings Quarter approval and can be funded from existing arrangements.

(Financial Services have been consulted in the preparation of this report.)

10.0 Legal Implications

- 10.1 Specialist legal advice is continuing to be provided by Trowers & Hamblins. Our lawyers have also provided advice for the procurement and State Aid issues surrounding this development and a draft summary was previously provided to Cabinet. Following publication of the relevant notices including a VEAT notice under EU and UK rules at the appropriate times, Trowers & Hamblins, in consultation with One Legal, believe that any risk of challenge has been minimised, and that risk remains very low.

(One Legal are being consulted in the preparation of this report.)

11.0 Risk & Opportunity Management Implications

- 11.1 The main risks associated with this proposal are financial. The overall level of funding required to bring forward a development opportunity of this magnitude is considerable. Whilst all due diligence can be applied, investing in property can be particularly difficult to accurately predict. The present inflationary pressure on borrowing costs is likely to continue and hence rates will be locked in as appropriate.
- 11.2 We negotiated fixed cost pricing with Kier Construction but due to inflation pressures and difficulties with supply chains, only above ground construction cost can be fixed. Therefore, ground contamination and archaeological cost risk remains with the City Council.
- 11.3 It is a known fact that development in Gloucester can be financially challenging and whilst the latest independent financial appraisal completed on behalf of the city council for this development shows a significant improvement on previous assessments, there is still a potential gap between value that can be generated and total development cost in the early years. The development costs rarely sustain any initial land value. Therefore, we have explored mechanisms that utilise the potential income generating value of the development. When viewed over a longer-term period, the income generated can support the costs. Obviously, predicting the growth of revenue projections is difficult and there is a risk that they may not grow as predicted. Equally, there is also a possibility of greater returns than anticipated. The Council should take comfort in the fact that a private developer is sufficiently confident that they have signed the Development Funding Agreement with a commitment to take a lease and provide some guarantees for a 5 year income flow.
- 11.3 Council officers have sought independent advice to verify the financial appraisals underpinning this offer in order to mitigate future risk. Because of the significant technological survey work and planning consent process undertaken by the City Council directly, it is in a good position to verify the projected development costs. The risk of further abnormal costs and complications have already been minimised by competitively tendering the main construction costs.

11.4 Other significant risks which include fiduciary and compliance issues are being carefully monitored and managed with considerable input from our lawyers and consultants. The relevant notices are being issued at appropriate times.

12.0 People Impact Assessment (PIA) and Safeguarding:

12.1 At present there are no adverse impacts identified for any of the Protected Characteristic Groups. As the regeneration of Kings Quarter progresses, the design process has been carefully devised to ensure maximum community engagement with a focus on achieving engagement with disabled and other minority groups. Further Impact Assessments will be considered as part of the development process where relevant.

13.0 Community Safety Implications

13.1 There are believed to be limited community safety implications at this stage. The agreement to proceed with this proposal will involve construction taking place within a busy part of the city centre. During construction periods the contractors will be legally obliged to ensure the health and safety of not just their staff but also the local community.

13.2 Any changes in the final design of the development to accommodate occupiers will need to be agreed via the normal planning mechanisms and this is providing an opportunity for further scrutiny by key stakeholders such as police, counter terrorism teams, and the Fire Service.

14.0 Staffing & Trade Union Implications

14.1 There are no staffing and trade union implications at this stage.

Background Documents: None