

APPENDIX B.2

WAVERLEY BOROUGH COUNCIL

EXECUTIVE – 3 NOVEMBER 2008

COUNCIL – 4 NOVEMBER 2008

Title:

EAST STREET REGENERATION – CONTRACTUAL MATTERS

**[Portfolio Holder: Cllr Richard Gates]
[Wards Affected: all Farnham]**

Note pursuant to Section 100B(5) of the Local Government Act 1972

An annexe to this report contains exempt information by virtue of which the public is likely to be excluded during the item to which the report relates, as specified in Paragraph 3 of Part 1 of Schedule 12A to the Local Government Act 1972, viz:-

Information relating to the financial or business affairs of any particular person (including the authority holding that information)

Summary and purpose:

This report recommends variations to the Council's contract with Crest Nicholson Sainsburys for the redevelopment and regeneration of the East Street site in Farnham.

How this report relates to the Council's Corporate Priorities:

The Council has a clear priority to regenerate the East Street area of Farnham by bringing forward a development proposal comprising housing, retail and commercial space, a cinema and a new town square. The current administration was successful in negotiating substantial amendments to the previous development proposals, and a revised scheme obtained a resolution to grant planning consent on 1 October 2008. Various contractual matters now need to be considered by the Executive and Council in order to facilitate the realisation of the Council's plans.

Equality and Diversity Implications:

None.

Resource/Value for Money implications:

The Council, as part of its development agreement, has negotiated both a capital receipt for its land at East Street through the development agreement (with the

safeguard of a "minimum land value"), and also an on-going revenue income stream from the commercial rents within the development.

A significant amount of financial investment has been undertaken to date in order to progress the scheme, and this is accounted for within the minimum land value calculations.

A detailed breakdown of the financial implications for Waverley arising from the development agreement is included in this report at [Exempt] Annexe 1.

Legal Implications:

The Council's solicitor has been consulted on this report and advises as follows:

The main intention of the proposed variations is to allow the term of the conditional contract to continue and to provide an opportunity for viability, given that the contract pre-conditions have not yet been fulfilled. In view of the Council's expressed continuing commitment to the redevelopment of East Street, and the fact that two of the four conditions will probably not be achieved before 2010 in any event, it would be appropriate for the Council to agree to the proposed extension until at least 31 December 2010. The proposed "rolling" viability test, the immediate withdrawal of the outstanding planning appeals, and the other variations proposed in this report would protect the Council's interests. It is for the Council to decide whether the longstop date, if extended, should be revised to the end of 2010 or 2011, having regard to its own priorities and the advice offered.

-
1. Waverley's development agreement with Crest Nicholson Regeneration Ltd and Sainsbury's Supermarkets Ltd (CNS), as currently constituted, is a conditional contract. These conditions bestow obligations on both parties to the contract. There are four conditions that must be achieved before the agreement becomes unconditional, and the development can proceed. These are as follows:

- Planning Consent.
- Land acquisition.
- Road and footpath closure.
- Financial viability test.

The contract requires that these four conditions be achieved by 31 December 2008. Thereafter, should any of the conditions not have been achieved, either party to the contract may (but is not required to) terminate it. The end date will automatically be extended in the event that either a planning inquiry is in process, or a Compulsory Purchase Order has been made, until the end point of that process has been reached. Councillors are reminded that there are two sets of previous planning applications (dating from 2006 and 2007) which are currently lodged with the Planning Inspectorate awaiting appeal against non-determination.

2. It is clear that the four conditions cannot be fulfilled by 31 December this year. While Waverley's Joint Planning Committee has recently resolved to grant planning consent, this is subject to a S106 agreement between Waverley, Surrey County Council and CNS. It is anticipated that this agreement will be concluded, and the planning decision notice issued by late December. The "road closure" condition (involving the making of a Traffic Regulation Order in respect of traffic on East Street and Brightwells Road, the diversion of existing footpaths and the creation of a cycleway) is estimated to take up to 12 months to complete, as the process involves public inquiries to hear objections to the various orders. It is only possible to commence these processes after a resolution to grant planning consent has been obtained.
3. The land acquisition condition concerns the purchase of the two plots of land within the development site that are not currently within Waverley's ownership. This matter is discussed in detail in another report on this Committee agenda, which recommends that Waverley commence compulsory purchase proceedings to acquire these two plots, as it has not proved possible to conclude an agreement for the voluntary purchase of either site, despite prolonged and detailed negotiations with both vendors. The estimated time-frame for concluding a CPO process is up to 24 months. Again, it is only possible to undertake a CPO in respect of a particular development proposal; therefore, this condition could not have been fulfilled prior to obtaining a planning resolution.
4. The viability test is the last of the contract conditions that is required to be fulfilled. This test is required by the contract to be undertaken after the other three pre-conditions have been met. Its purpose is to ascertain whether the development proposal is able to achieve both CNS's contractual conditions in terms of return on investment, and Waverley's required minimum land value. Currently, the contract allows for only one viability test on fulfilment of the planning, land and road closure conditions. Should the viability test fail, CNS has the option either to waive the test and pay the minimum land value to Waverley, or to terminate the contract.
5. Waverley has a clear policy objective to regenerate the East Street area of Farnham for the benefit of the town. Considerable time, effort and resource has been invested to date in seeking to bring forward this development proposal, which the Council, as landowner, has resolved is in the best interest of Farnham. Delivering a scheme of this type is, however, inevitably a lengthy and complex process. A very significant milestone was achieved this month when the revised development proposal achieved a resolution to grant planning consent. It is clear that, in order to succeed in realising the Council's ambitions, a number of key decisions concerning the development contract now need to be considered.
6. Two significant factors, outside this Council's control, serve as the backdrop to the consideration of the options available to Members. The first is the legislative timescale involved in concluding the processes to acquire the land and undertake the various road and footpath amendments, as outlined above. Officers advise that these processes could take two years to complete. The

second is the current economic situation. The severe financial crisis in the financial services industry, and the resultant catastrophic effects on share prices, housebuilding and business confidence, was not and could not have been predicted at the time when Waverley entered into the development agreement with CNS. The consequence of the credit crunch is that land values have fallen sharply, while the availability of credit finance has also reduced, and commercial borrowing rates have risen significantly. In current market conditions, housing and commercial renewal schemes are virtually unfundable.

7. Inevitably, it is the economic situation which is of greatest concern to CNS. The company's development director has written to the Chief Executive asking that Waverley consider making two significant variations to the contract: firstly, an extension of the "longstop" date by three years to 31 December 2011; and secondly, the insertion of a clause to allow a rolling viability test, to be repeated at intervals not greater than six months, between the time of conclusion of the three other pre-conditions and the end point of the contract, in order to allow the contract better to withstand the current economic uncertainty.

The options available to the Council:

8. The Executive and Council now need to consider whether to seek to negotiate any variations to the contract with CNS. The options available are:
 - Do nothing
 - Agree to the CNS requests
 - Seek alternative variations to the contract.

"Do nothing"

9. The main argument in favour of the "do nothing" option, is that this would give Waverley the opportunity to terminate the contract on or after 1 January 2009, because the four conditions would not have been achieved by that point. This would be the preferred option if the Council believed that it would have a better chance of achieving its objective of regenerating the East Street area through a different route (e.g. by entering into an alternative development contract with a different developer, or by seeking to dispose of the site).
10. This option, however, entails serious risks to the Council. Waverley does not yet control the totality of the development site, and this places a severe constraint on the Council's options for achieving the development. Moreover, as compulsory purchase can, in law, only be undertaken in favour of a particular development proposal, the absence of a development contract would detract significantly from the Council's ability to persuade the Secretary of State on the question of the public interest, as to terminate the contract would be seen as a clear indication that the Council did not, in fact, favour this particular development. Secondly, while the Council does not own the whole of the development site, this places a real constraint on its ability to offer the land for sale in order to achieve the development. Thirdly, terminating the

contract would mean, in effect, starting again at the beginning of the project, seeking an alternative development proposal, and new contract terms. This could entail several years of delay in meeting the Council's regeneration objectives, and would result in greater uncertainty for the people of Farnham.

11. The greatest risk, however, is financial. Waverley has already invested significant resources (see [Exempt] Annexe 1) into this development proposal. The minimum land value due to Waverley under the contract with CNS will see this investment returned. In addition, the contract secures significant revenue funding to Waverley from the commercial elements of the development. In the current market conditions, it is highly unlikely that in the current economic circumstances any alternative developer could be found who would match CNS's financial offer to Waverley.

"Do nothing" – alternative scenario

12. It is clear that it is in the best interests of Waverley to secure control over the whole of the development site, and that the continuation of the contract with CNS gives weight to the case for compulsory purchase. It is, theoretically, open to Waverley to allow the current contract end date to expire, but not to seek to terminate the agreement. Under this scenario, the process of fulfilment of the contract conditions would proceed as planned, culminating in the viability test.
13. The significant risk of this scenario is that the timing of the process would no longer be within Waverley's control. While CPO can take up to two years, the process can be halted at any time simply by the vendors agreeing to sell the land. Similarly, if no material or relevant objections arise to the road and footpath amendment proposals, the process can be concluded relatively quickly. This could, therefore, have the effect that the viability test needs to be undertaken at a time when the financial markets are still very volatile, which increases the risk that viability will not be achieved.
14. Moreover, the issue of the Council's policy intentions would arise. It is highly likely in this scenario that the council would be placed under considerable pressure by those parties who opposed the current scheme to change its mind and terminate the contract. This Council takes its community leadership role very seriously. As such, a clear statement of policy relating to the end date of the contract would give certainty and reassurance to the public of Farnham, and minimise the likelihood of constant and unhelpful debate on the subject in the local media and in questions to the Council.

Extending the contract

15. The alternative way forward is to set a new contract end date. CNS have requested an extension of three years, in order to allow the maximum possible time for the economic conditions to improve. It should be noted also that three years is the standard life-span of a planning consent – i.e. planning permission must be implemented within three years, or an extension specifically applied-for. The principal argument in favour of a three year

extension is economic. The principal argument against such a long extension is that it could serve unduly to delay the implementation of the development.

16. It must be considered, however, whether a contract extension of this length would be in the best interests of the Council. Previous contract extensions have been granted by Council, but never for such a long duration. The two previous extensions were for periods of 12 months and 9 months respectively.
17. As has been outlined above, the principal argument in favour of extension is in order to allow sufficient time for the processes involved in fulfilling the contract conditions to be concluded. Given that the CPO process, if taken to its conclusion without prior settlement, is estimated to take two years, it would seem appropriate to consider a contract extension of the same amount of time.
18. It should be noted that, should an extension be granted and the new end date be reached without the conditions having been achieved, it would again be open to the Council to decide whether at that point to terminate the contract, or to grant a further extension. At that point, however, the Council's options would be more numerous, as Waverley should have achieved control over the whole of the development site.

The rolling viability test

19. In addition to the contract extension, CNS have asked Waverley to agree to a rolling viability test, rather than this test being a one-off, all or nothing determinant of whether the development proceeds or fails. In the current market conditions, there is a very strong argument in favour of agreeing this request, provided that, as soon as a positive result is achieved, the contract becomes unconditional.

Other contractual requirements

20. If Waverley is minded to vary the current contract, then it is appropriate to consider whether there are additional amendments, from the Council's side, that should be included in the variation. It is recommended that Waverley seek to obtain the following concessions from CNS as part of the negotiations:
 - The immediate withdrawal of all planning appeals relating to previous applications. Currently this does not happen until a "clean" planning permission is achieved, which is not for up to 6 months, during which time the Inspectorate may require the appeal to be held.
 - The assignment of all plans, drawings, technical studies and other intellectual property relating to the planning application to Waverley, in the event of the contract being terminated in the future by either party. The copyright in the plans otherwise vests in the applicant, who would be entitled to withhold it or demand significant fees
 - An option to purchase the Marlborough Head pub site from CNS at cost, should the contract be terminated by either party.

- Confirmation from CNS that none of the planning conditions imposed by the Joint Planning Committee are "onerous".
- Safeguarding of the Council's position in all foreseeable circumstances.

Conclusion

Waverley's strong policy commitment to the regeneration of East Street is clear. The Council has invested considerable effort and resources over a long period of years in pursuit of this objective, and has recently achieved a significant milestone in the revised scheme being approved through the planning process. There is still considerable preparatory work to do before the contract conditions can be met and the scheme can be in a position to proceed. Moreover, the current critical economic conditions necessitate that a pragmatic approach be taken to testing the scheme's financial viability. It is clear that in the current economic climate, Waverley's development contract with CNS offers the best prospect to the Council of achieving the development and the required financial return. It reaffirms the Council's confidence in CNS at a time when the market is in considerable turmoil and community leadership is needed to stabilise it.

Recommendation

It is recommended that:

- 1) the development contract between Waverley and CNS be extended to 31 December 2010;
- 2) the contract be varied to allow a rolling viability test at intervals of no greater than six months, between the date of fulfilment of the site assembly and road closure conditions and the contract end date;
- 3) additional variations be negotiated, as set out in paragraph 20 of this report; and
- 4) authority to approve the final contract text be delegated to the Chief Executive in consultation with the portfolio holder for East Street.

Background Papers (CSP)

Relevant clauses of the East Street contract.

CONTACT OFFICER:

Name: Mary Orton, Chief Executive

Telephone: 01483 523 208

E-mail: mary.orton@waverley.gov.uk

comms\executive\2008-09\183 031108 E St Contractual final.doc

