

To: City Executive Board

Date: 12 February 2015

Report of: Executive Director for City Regeneration and Housing

Title of Report: Acquisition of St Aldate's Chambers (SAC)

Summary and Recommendations

Purpose of report: To approve the acquisition of the long leasehold interest in St Aldate's Chambers, and simultaneously agree to vary the long leasehold interest at 5 Queen Street.

Key decision: Yes

Executive lead member: Councillor Ed Turner, Board member for Finance, Asset Management and Public Health

Policy Framework: Efficient and effective Council

Recommendations: That the City Executive Board

1) Grant approval for the acquisition of the long leasehold interest in St Aldate's Chambers for £7,539,230 (which comprises the purchase price of £7,200,000 plus acquisition costs of £339,230).

2) Agree the variations detailed in this report to the long lease of 5 Queen Street such that the City Council receives not less than £25,000 pa in rent until 2144.

3) Recommend to Council the increase of the budget in the Council's Capital Programme for the purchase of property in the sum of £539,230 to be financed from underspends in the Council's General Fund Revenue Budget in 2014-15.

Appendices

Appendix 1 –Risk Register

Background

1. In December 2013, British Airways Pension Trustees Limited (BA), with its development partner REEF, acquired the long leasehold interest in St Aldate's Chambers (SAC), and the adjacent 114-119 St Aldate's and 4-5 Queen Street. The City Council holds the freehold interest in SAC which delivers income of £5,000 per annum. The City Council also holds an occupational lease on SAC with a current rent liability of £300,091 per annum. The next, and final, rent review is in 2023; the lease expires in 2037. The City Council also holds the freehold interest in 5 Queen Street only i.e. not 4 Queen Street and nor 114-119 St Aldate's.
2. In July 2014, BA/REEF submitted a planning application for the redevelopment of 114-119 St Aldate's and 4-5 Queen Street for principally student accommodation (accessed from St Aldate's) and a new retail unit at 4-5 Queen Street. The application was conditionally approved by the West End Area Planning Committee on 12 November 2014. The Decision Notice is expected to be issued in February 2015, but BA/REEF cannot commence development until the City Council (as the freeholder of 5 Queen Street) agrees to several material amendments to the long lease. The long lease is geared to 12% of the rents received and it expires in 2144.
3. The City Council's acquisition of the long leasehold interest in St Aldate's Chambers is strategically driven by: the want to remove future rent review risk; to mitigate tenant dilapidations risk; and, make use of the City Council's competitive cost of capital. Separately, the amendment to the long lease on 5 Queen Street will enable development and increase the rental income to the Council from the property.

St Aldate's Chambers (SAC)

4. The City Council has sought valuation advice from Jones Lang LaSalle on the current Market Value of BA/REEF's long leasehold interest in SAC.
5. There has been a significant amount of negotiation with BA/REEF around the Estimated Rental Value (ERV) of SAC, net of a market incentive. An ERV of circa £450,000 per annum can be supported, which is predicated on £15.00 per ft² for the ground and upper floors which takes account of the age and size of the building. At the next rent review in 2023, the City Council's rent could therefore rise to £450,000+ per annum i.e. £150,000+ per annum more than the current rent.
6. We have now agreed in principle terms with BA/REEF, subject to due diligence and Board approval, to acquire the long leasehold interest for £7,200,000, added to which will be acquisition costs of £339,230 (being SDLT of £288,000 plus JLL valuation input and market advice (pursuant to both SAC and 5 Queen Street) of not more than £51,230). The total

purchase cost is £7,539,230. A purchase at this level equates to an adjusted Net Initial Yield of 3.91% which is supported by a formal valuation from Jones Lang LaSalle, which is a statutory requirement under Section 123 of the Local Government Act 1972 to demonstrate that the Council has acquired the property at a fair value.

5 Queen Street

7. 5 Queen Street currently comprises ground and basement retail with storage above, and the City Council as freeholder is entitled to 12% of the rents received, currently £13,200 per annum based on the letting to the current tenant, EAT. BA/REEF is proposing 4 storeys of student accommodation above the retail which might deliver another £6-7,000 per annum to the City Council based on 12% of the likely rents received for this use, but the majority of the value is in the new and improved retail to be provided on Queen Street.
8. We have agreed with BA/REEF that it will underwrite a minimum rent of £25,000 per annum on 5 Queen Street, which is £11,800 per annum more than the rent currently received by the City Council. This rent 'collar' is predicated on a fair assessment of the Estimated Rental Value of the new retail unit and the rent receivable on the student accommodation above. The new rent aside, it is proposed the City Council consents to (a) the proposed alterations to the Demised Premises (b) a variation to the Authorised Use to permit Class C3 residential use (c) a variation to the alienation provisions.

Legal Issues

9. By acquiring the long leasehold interest in SAC, it gives the City Council the ability to regularise any anomalies in the occupational lease (e.g. the lack of disregard for tenant's improvements and the abnormal 14 year review pattern) or indeed collapse the occupational lease. The City Council would also have the option of undertaking a sale and leaseback at some point in the future if corporate objectives were to change.

Financial Issues

10. The City Council's Capital Programme includes a budget for property acquisitions of £7,000,000 in 2014-15 which is £539,230 short of the overall acquisition costs for SAC.
11. In order for this transaction to be completed a recommendation will need to be made to Council to increase the Capital budget in 2014-15 by £539,230. This can be funded from forecast underspends in the General Fund Revenue Budget that are currently indicated for 2014-15.
12. Members should be aware that the savings in rental costs of St Aldate's Chambers has already been factored into the Medium Term Financial Plan that will be recommended to Council in February 2014.

13. The acquisition of the SAC lease and the varying of the lease on 5 Queen Street will have the following financial implications to the Council:-

Table 1 Financial Implications of Transactions	
	£
Capital cost of SAC (including acquisition costs)	7,539,230
Revenue	
Saving on existing rent for SAC	300,091
Increased rent on 5 Queen Street	11,800
Loss of income from BA/REEF	(5,000)
Total saving	306,891
Loss of interest on investment	110,000
Net annual Gain on transaction	196,891
Percentage return compared to investment	4.07%

14. Should the Council not undertake the transaction there is a potential for the rent to be increased to £450,000+per annum at the next rent review in 2023 which could produce a higher net gain for the Council against its capital investment.

Environmental Impact

15. There is no environmental impact.

Risk Register

16. The Risk Register is included as Appendix 1.

Equalities Impact

17. There is no equalities impact.

<p>Name and contact details of author:-</p> <p>Name: Jane Winfield Job title: Regeneration & Major Projects Service Manager Service Area / Department: Regeneration & Major Projects Tel: 01865 252551 e-mail: jwinfield@oxford.gov.uk</p>
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Background Papers

- (i) Jones Lang LaSalle's valuation.