NORWICH
City Council

Committee Name: Cabinet

Committee Date: 07/07/2021

Report Title: NRL assurance and consideration of the Threescore phase 3 outline business case

Portfolio:	Resources
Report from:	Executive director of development and city services
Wards:	Bowthorpe
OPEN PUBLIC ITEM	

Purpose

To consider a report provided by Savills regarding assurance on the NRL business plan prior to the Council considering further investment in the company to deliver the plan. To consider the outline business case provided by NRL for the development of part of Three Score Phase 3 and agree to delegate authority to dispose of this land to NRL to facilitate the development subject to the business case.

Recommendation:

To, having regard to the independent assurance report provided by Savills and the NRL outline business case for Three Score Phase 3:

a) recommend to Council that provision for the necessary loan finance and share capital (currently estimated at up to £4.0m) be approved for inclusion in the capital programme £2m (2021/22) and £2m (2022/23);

Subject to council approval of a) above to;

b) delegate authority to the Executive Director of Development and City Services in consultation with the Portfolio Holder for Resources to dispose of land to NRL at the value set out in the exempt appendix (see para 6 of exempt appendix 3) to deliver the private housing element of the scheme;
c) delegate authority to the Executive Director of Development and City Services in consultation with the Portfolio Holder for Resources to appropriate land to the HRA to deliver the social housing element of the scheme (as set out in para 10 and 11 of exempt appendix 3); and

d) delegate authority to the Executive Director of Corporate and Commercial Services in consultation with the Portfolio Holder for Resources to enter into a new loan facility agreement with NRL to fund approved shareholder investment.

Policy Framework

The Council has three corporate priorities, which are:

- People living well
- Great neighbourhoods, housing and environment
- Inclusive economy

This report meets the *Great neighbourhoods, housing and environment corporate priority*

This report helps to meet the *Build and maintain a range of good quality affordable and social housing* adopted policy of the Council

This report helps to meet *Housing, regeneration and development* priority of the COVID-19 Recovery Plan

Report Details

Background

1. At its meeting on 10th March Cabinet considered the Norwich Regeneration Limited Business Plan 2021/22 that the company is required to produce under its articles of association. It agreed to welcome the Business Plan for Norwich Regeneration Limited for 2021/22 and, among other things, agreed that:

   - NRL should move forward to develop a detailed business case for the development of Three Score Phase 3 as described in the Business Plan to allow the shareholder to consider further investment in this scheme;
   - The Council as shareholder should support this activity so that robust business case can be established to enable the Council to make investment decisions; and
   - To instruct that officers to obtain expert independent advice, scrutiny and assurance in relation to the NRL business Plan and its underlying assumptions before agreeing to detailed business cases.

2. The business plan for the company for 2021/22 was contained in an exempt appendix to the March report. It sets out NRL's vision, mission, values, objectives and business principles, and outlined how financial performance and governance have been improved. It also described three schemes for further development during 2021/22 that may require further investment by the Council. The first of these schemes was an element of Three Score phase 3. Another site at Ber Street will be further considered later in the year.

Assurance on the NRL Business Plan

3. Following March cabinet Savills were appointed to undertake the due diligence work. Their report is commercially sensitive and is attached as exempt appendix 1. Overall the report offers a considerable level of assurance on the NRL Business Plan.

4. It concludes that “Whilst we report differences in approach compared to that presented by NRL in their business plan, our overall opinion is that there should be sufficient margin generated through both key projects to provide confidence for NCC to continue to invest in the vehicle as a means to generating both capital and revenue receipts. Clearly the historic debt position generates challenges for NRL (whilst at the same time enables NCC to generate additional revenue through interest charges against historic loans). However there does appear to be a positive direction of travel within the business, which can only continue if it is supported through the identification of sites which enables NRL to allocate its central costs against a larger number of projects.”

5. It goes on to further conclude that “The alternative to further investment into the NRL vehicle may be to essentially write-off the current debt position against the company. We are of the opinion that such a move would be premature at this stage, given our appraisal of both sites in question suggests opportunity to generate both revenue and capital receipts for the Council through the form of interest and capital debt repayments through future sales.”

6. With regard to the emerging business case for the proposed NRL scheme in relation to part of Three Score Phase 3 (which is considered further later in this report) it concludes that the project “should generate sufficient value through future sales to repay respective delivery costs, alongside allocated central costs made to each project reflecting a Service Level Agreement (SLA) between the Council and NRL, and interest incurred against historic debt held by NRL. Indeed sensitivity analysis has suggested that there is some degree of buffer in terms of worsening sales performance and/or increased costs which may provide some further assurance in the deliverability of proposals.”

NRL Business Case for Three Score

7. Subsequent to the decision of Cabinet in March 2021 NRL has continued to progress the development of the Business Case for development at Three Score phase 3. The latest version of this emerging business case is attached as exempt appendix 2. It should be noted that: a) this business case has developed since the Savills assurance report was produced so figures in the two separate appendices may not exactly correspond; b) the business case should still be considered as outline; c) the business case relates only to a part of the site at Three Score Phase 3 – most of the site is due to be developed by the HRA for social housing and Cabinet agreed the outline business case for this investment in July 2020 and authority to award contracts for the appointment of design and construction contractors in April 2021.

8. Until the scheme receives reserved matters planning consent (the site already has outline planning permission) and costs can be finalised through contract arrangements there can be no certainty regarding the design or cost figures presented. Nevertheless there is a high degree of confidence in these as the company continue to build on the adjacent site so if highly familiar with the conditions of the site and local market.

9. The outline business case is due for consideration by the NRL board on 1st July. A verbal update will be given to the meeting about whether the outline business case was endorsed or not.

10. The business case envisages that NRL construct 23 dwellings this comprises 4 x 2 bed homes, 11 x 3 bed homes and 8 x 4 bed homes. Construction is due to commence in October 2021 and the build programme is forecast to last for 20 months, completing in April 2023. Although the first properties are forecasted to be complete by August 2022 with sales revenues being realised between December 2022 and June 2023.

11. The business case notes that due to the success of Trinity Gardens it is anticipated that the company will repay a further £4m of the existing loan facility in 2021/22. This will enable NRL to reduce the interest payments that it owes but will require a new loan facility to be agreed in order to fund the Three Score Phase 3 development.

12. To deliver the Three Score Phase 3 development the business case identifies the need for a new loan facility from the Council as shareholder of £2m in March 2022 and a further £2m in 2022/23 to fund working capital for the scheme. The requested facility will comprise equity shares and loans to maintain a gearing ratio of not more than 75% debt. The loan interest rate is calculated as being 4.5% over base rate (currently 4.6%).

13. Whilst the details of the business case are commercially sensitive the total value of the homes built are expected to be around £7m. Anticipated profits arising from the development would be used to meet the operating costs of the company, pay down historic debt and contributing considerably to the overall financial stability of the company.

14. The business case is predicated on NRL's articles of association and delivering development that is an alignment with the 2040 Norwich Vision which puts sustainability at the centre of all development. Resultantly, these homes will be delivered to very high environmental standards taking a fabric first approach and informed by PassivHaus principles, in line with the delivery of the homes from earlier stages at Three Score. All development is also built in accordance with nationally described space standards.

15. The environmental housing performance standard is to target a low carbon approach that will drive for the energy certification of each dwelling. Energy performance certificates (EPCs) are a rating scheme to summarise the energy efficiency of each home. The home is given a rating between A (Very efficient) - G (Inefficient). The calculation of the energy rating on the EPC is based on the Standard Assessment Procedure (SAP). NRL's approach is to deliver the most efficient homes possible within the financial envelope and demonstrate best value. Highly performing home should therefore deliver the lowest fuel

bills for the home owner and band A is the target. The certificate uses the same scale to define the impact a home has on the environment. Better-rated homes should have less impact through carbon dioxide (CO_2) emissions. To note: the average property in the UK is in band D.

16. As NRL completes the design phase throughout the summer and concludes the planning strategy and RIBA Stage 4 detailed design, the residential viability appraisal will demonstrate key element cost categories that influence the overall construction cost of each dwelling and the company can take key decisions on achieving the target performance levels best on expenditure versus return.

17. The emerging scheme at Three Score Phase 3 is illustrated below. It should be noted that this may be subject to change through consultation and planning processes, and the delineation of land between NRL and the HRA is only approximate at this stage (HRA development shown greyed out).

Land Transfer and Disposal

18. The land at Three Score Phase 3 is an asset currently held by the Council's general fund. In order to undertake both the development envisaged in the NRL business plan for private sale and the HRA led development approved in July 2020 it will be necessary for land transfer to take place.

19. Prior to NRL undertaking the development of the private housing they will need to acquire the land from the Council. The value of the land is set out in the exempt appendix (appendix 3). It should be noted that this value is in accordance with a revised valuation from NPS property consultants, rather than a full independent red book valuation. However, it should be noted that the independent Savills report also considered the value of this land and concluded its value was very similar to this. Therefore, it is proposed to disposed of the land to NRL at this value.

20. The exact boundary of the land to be disposed of to NRL and appropriated to the HRA will be determined following the determination of detailed designs. Therefore, authority is requested to determine the exact areas and complete the transfers under delegated authority.

Implications

Financial and Resources

21. The city wholly owns NRL and provides all of its investment capital. City's investment in NRL at 18 June 2021 is £14.024m comprising £10.15m loan and £3.874m equity shares.

22. The company repaid £5.5m of loans in March and April 2021. A further £4.45m will be returned to the city in 2021/22.

23. To deliver the business case NRL will require further investment. The NRL board is expected to request the shareholder invests a further £2m in March 2022 and a further £2m in 2022/23 to fund working capital for this development scheme. The facility will comprise equity shares and loans to maintain a gearing ratio of not more than 75% debt. The loan interest rate will be 4.5% over base, currently 4.6%.

24. Officers are seeking the delegated authority to enter a new facility agreement with NRL to fund Threescore phase 3.

25. The overall equity investment in the company does not increase through this development. There remains a risk that the existing equity might not be recovered, this would have a subsequent effect on capital receipt available for other investments. The business case suggests that this scheme will provide a positive contribution to mitigation of this risk.

26. Due to retained losses in NRL the city has made a provision against the investment the company of £3.25m. This is a £0.75m improvement since March 2020 reflecting the enhanced financial performance. The level of impairment will continue to be reviewed annually to reflect financial performance.

27. The company and the city will continue to work closely together to monitor the cash position and reduce costs where appropriate, with the aim of reducing the peak loan and equity requirement. The managing director of the company continues to target overhead reduction within the company.

Legal and Governance

28. The detail of the loan agreement will be drawn up by the Council solicitor's at NPLaw.
29. Suitable security will be placed on the assets of the company including the land to be transferred.
30. Considerable improvements have been made to the governance and oversight of the company over the past year with the appointment of 2 independent non-executive directors. Recently further measures have been taken to reduce the potential for conflicts of interest between Council and Company with the Council's Portfolio Holder for Resources stepping down as a director of the company. Furthermore a shareholder panel has been set up to increase the overview and scrutiny of company performance.

Statutory Considerations

Consideration:	Details of any implications and proposed measures to address:
Equality and Diversity	N/a
Health, Social and Economic Impact	Delivery of new homes and building to enhanced space and environmental standards should have positive impacts on health and social considerations
Crime and Disorder	Scheme has been designed with a view to maximise surveillance of open spaces
Children and Adults Safeguarding	N/a
Environmental Impact	See paras 14 and 15 above. Ongoing environmental impact of houses likely to be considerably less than most other new homes currently being built in Norwich

Risk Management

Risk	Consequence	Controls Required
Not gaining planning permission for the development	Delay in being able to deliver the scheme and possible increase in costs.	Extensive pre-application engagement and consultation on the detail of design. Risk substantially mitigated by outline consent being in place
Financial risk	NRL not being able to repay or provide return on the investment.	See sensitivity testing in business plan assurance report (appendix 1)

		See risk management approach outlined within the business case (appendix 2).
Reputational risk	NRL not being able to deliver on the standards or timetable set out in the business plan or individual business cases	Improved governance measures put in place for the company (see paras 28-30)

Other Options Considered

31. Do nothing – this would fail to meet housing needs or make best use of the land asset held by the Council.

32. To build out the entirety of the site for social housing – this would be possible although it would create a problem for NRL as it would cast considerable doubt on its ability to deliver its business plan and put at risk council investment previously made in the company. Whilst meeting more of the acute housing needs development would lack social balance.

33. To sell the site on the open market – possible increased financial return to the Council in the short term. However, doesn't meet housing needs so well, is likely to result in homes built to a lower environmental standard and risks the development of houses being stalled by a third party.

Reasons for the decision/recommendation

34. It is considered that the Council's corporate objectives are best delivered by acceptance of the business plan and taking the appropriate steps to facilitate the development through taking the steps set out in the recommendations.

Background papers:

None

Appendices:

Exempt appendices supplied.

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