

Resources Overview and Scrutiny Panel

Agenda
Item:
A.8

Meeting Date: 20th October 2016
Portfolio: Finance, Governance and Resources
Key Decision: Yes: Recorded in the Notice Ref: KD
Within Policy and Budget Framework YES
Public / Private Public

Title: **Market Hall Roof Repair Works – Capital Contribution and Lease Extension**
Report of: **CORPORATE DIRECTOR OF GOVERNANCE & REGULATORY SERVICES**
Report Number: **GD.51/16**

Purpose / Summary:

The Panel has requested that the attached Executive Report (GD.51/16) be presented to them.

The attached report, which sets out the current position relating to the Market Hall roof repair works and the request by the tenant to extend their current lease, was considered by Executive at its meeting of 26th September where the recommendations given were agreed.

Members are also asked to note the financial information included within Part B of the attached report.

Recommendation:

The Panel note the Report.

Report to Executive

Agenda
Item:

Meeting Date: 26th September 2016
 Portfolio: Finance, Governance and Resources
 Key Decision: YES: Recorded in the Notice Ref: KD.
 Within Policy and Budget Framework YES
 Public / Private Public – Part A report
 Title: **Market Hall Roof Repair Works - Capital Contribution and Lease Extension**
 Report of: **Director of Governance**
 Report Number: **GD.51/16**

Purpose / Summary:

This report advises Members of the essential repair works to the Market Hall premises and of proposals to extend the head-lease and under-lease of the Market Hall premises. Approval to the release of a capital sum to meet the Council's funding liability for the works is requested (funding approved by Full Council at its meeting of 2nd February 2016, report ref. RD.47/15 refers) together with authority to extend the head-lease and sub-under-lease of the premises with the approval of detailed terms to be delegated to Heads of Service in consultation with the Director of Governance. Members are also asked to note the financial information included within Part B of this report.

Recommendation:

1. That Executive approves the release of capital monies earmarked in the Capital Programme to meet the Council's repair work funding liability.
2. That Executive delegates the agreement to the detailed terms of the proposed head-lease and under-lease extension to the Building & Estates Services Manager and the Asset & Investment Services Manager in consultation with the Director of Governance.

Tracking

Executive:	26th September 2016
Overview and Scrutiny:	20th October 2016
Executive:	n/a
Council:	n/a

1.0 BACKGROUND

1.1 Leasing arrangements and rental income

- 1.1.1 Carlisle City Council owns the freehold of the Market Hall which is let to BAE Pension Fund on a 99 year head-lease from March 1991 with an option to extend the term by 51 years. If the option is exercised the term would expire in 2141.
- 1.1.2 BAE is responsible for paying the Council a ground rent equal to 20% of the net rental income. Net rental income is calculated to represent the difference between gross rents (including any void rents) and permitted deductions.
- 1.1.3 The indoor market area is sub-let to the Council on an under-lease which is coterminous with the head-lease. The Council is responsible for paying over all rent and service charge monies received to BAE.
- 1.1.4 The service charge is payable on a monthly basis and recovers from the occupiers the anticipated annual spend, based on the previous year spend, for items such as building repairs and maintenance, cleaning, management fees and utility charges. Over the past few years BAE and the Council have agreed to cap the level of service charge to give costs certainty to the occupiers
- 1.1.5 There is a Market Hall Management Agreement in place which forms part of the head-lease. This agreement is now outdated and does not reflect modern estate management practices.

1.2 Repair liabilities and cost recovery

- 1.2.1 The Market Hall has, over the years, fallen into disrepair and BAE have commissioned a survey which highlighted the need for significant essential repairs, primarily relating to the roof.
- 1.2.2 Under the head-lease, BAE are responsible for undertaking the works, the cost of which either in part or whole is recoverable through the service charge.
- 1.2.3 Proper and reasonable repair costs which are not recovered through the service charge qualify as permitted deductions for the purposes of the ground rent calculations. This means that the City Council would bear 20% of the non-recoverable costs, with BAE shouldering the balance. There is thus a strong financial motive for BAE to recover as much as possible via the service charge whilst at the same time ensuring that the repair costs are kept to a reasonable level.
- 1.2.4 BAE has now commissioned the work to the roof which is due to start at the beginning of October with an anticipated completion date of mid November 2016.

1.3 Recovery through the service charge

- 1.3.1 All Market stall holders have, over the past few years, benefited from service charge cap arrangements and virtually all leases/licences are capable of determination by tenants/licensees on 1 months' notice.
- 1.3.2 There is significant risk that the recovery of the cost of the repair works through the service charge would deter traders from renewing leases, make re-letting difficult to achieve and indeed force some traders to give notice on their current agreements. The impact for both BAE and the Council could be similar as there would be a trade-off between higher service charge contributions on the one hand and lower rents/licence fees on the other.
- 1.3.3 If traders are deterred from occupancy there would be a loss of both rental/licence fee and service charge until such time as new occupiers are found. Voids and the costs associated with these could become prolonged, particularly if the market loses a critical mass of occupancy. All of these aspects would need to be carefully balanced in negotiating higher service charges and contributions from the tenants towards the cost of the works.
- 1.3.4 It is therefore highly unlikely that the full cost would be recovered by the service charge and that a substantial proportion would fall as permitted deductions.

1.4 Head-lease extension

- 1.4.1 BAE has put forward a proposal to extend their ground lease by a further 99 years, and the Council has engaged Cushman & Wakefield to advise and negotiate the detail of the lease extension to ensure best value is achieved for the Council.
- 1.4.2 It is considered that the extension of the head-lease is beneficial to the Council as it will not only secure an extended revenue stream but will also secure the ongoing maintenance liability for this Grade II listed building.
- 1.4.3 Negotiations to extend the head-lease will include proposals to consecutively extend the Council's under-lease of the stall holder area and will facilitate the opportunity to update the outdated Market Hall Management Agreement.

2.0 PROPOSALS

- 2.1 Subject to the agreement of detailed terms for the lease extension, it is likely that the majority of the costs of the repair works will fall as permitted deductions, affecting the Council's annual rental income. However, on the assumption that BAE was prepared to spread the recovery of the Council's costs liability through the rent it pays, it would be reasonable for BAE to include an interest charge on

the outstanding balance, therefore increasing the overall cost liability of the Council.

- 2.2 To protect and enhance its investment it is proposed that the Council make a one-off capital contribution to fully discharge its costs liability, with the payment being made from the capital sum earmarked as a contribution to the Market Hall repair works (approved by Full Council at its meeting of Tuesday 2nd February 2016 – report ref. RD.47/15 refers).
- 2.3 Discussions are taking place via the Market Hall Managing Agent to ensure that the stall holders are kept fully apprised of the works and any potential business disruption these may cause.
- 2.4 It is also proposed to agree the proposed head-lease extension, subject to the agreement of detailed terms, with the tenant.

3.0 CONSULTATION

- 3.1 Consultation has taken place with the Director of Governance, Officers, Portfolio Holder, Chair and Vice Chair of the Market Hall Management Committee, who support the proposals.

4.0 CONCLUSION AND REASONS FOR RECOMMENDATIONS

- 4.1 The recovery of the cost of the essential works through the service charge would have a detrimental effect on the tenants, the Council and BAE through potential loss of income and difficulties in the re-letting of vacant space.
- 4.2 BAE have put forward head-lease extension proposals. The Council has employed an external investment adviser to negotiate the detail of the head-lease extension, and to agree the best way of updating the outdated management agreement.
- 4.3 Discussions have commenced with BAE, in conjunction with negotiations relating to the head-lease extension, to agree the non-recovery of the repair costs from the stall holders through the service charge. It is anticipated therefore that the majority of the repair costs will therefore fall as permitted deductions which will affect the rent the Council receives.
- 4.4 The Council currently holds a capital sum in the Capital Programme earmarked as a contribution to the Market Hall repair works. The payment of a capital contribution will protect and enhance the Council's investment asset.

5.0 CONTRIBUTION TO THE CARLISLE PLAN PRIORITIES

- 5.1 The proper management of the Council's property resource makes an essential contribution the achievement of the Council's action plans and priorities.
- 5.2 Supports business growth by providing quality space and improves economic prospects for the people of Carlisle.

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Appendices None
attached to report:

Note: in compliance with section 100d of the Local Government (Access to Information) Act 1985 the report has been prepared in part from the following papers:

CORPORATE IMPLICATIONS/RISKS:

Chief Executive's – none

Community Engagement – none

Economic Development –

The grade 2 listed Market Hall is a key historic building within the City Centre and provides a key component of Carlisle's retail offer. The proposals will ensure that the fabric of the building is maintained and the retail opportunities maximised.

Governance –.

The financial and other liabilities connected with the Market Hall, and legal structures around the Market Hall lease and relationships between the parties to the lease and general management arrangements are set out within this report.

Local Environment – none

Resources –

The Council has set aside £460,000 in the capital programme for 2016/17 for cost of the roofing repair work attributable to the Council. This was subject to a further report to Executive for the release of this budget which is now satisfied by this report.

EXCERPT FROM THE MINUTES OF THE EXECUTIVE HELD ON 26 SEPTEMBER 2016

**EX.85/16 MARKET HALL ROOF REPAIR WORKS – CAPITAL CONTRIBUTION
AND LEASE EXTENSION**
(Key Decision – KD.19/16)

Portfolio Finance, Governance and Resources

Relevant Overview and Scrutiny Panel Resources

Subject Matter

The Deputy Leader, and Finance, Governance and Resources Portfolio Holder submitted report GD.51/16 detailing the need for essential repair works to the Market Hall premises, together with proposals to extend the head-lease and under-lease of the premises.

Speaking by way of background, the Deputy Leader indicated that the City Council owned the freehold of the Market Hall which was let to BAE Pension Fund on a 99 year head-lease from March 1991 with an option to extend the term by 51 years. The Market Hall had, over the years, fallen into disrepair. BAE had commissioned a survey which highlighted the need for significant essential repairs, primarily to the roof. They had further commissioned that work which was scheduled to start at the beginning of October 2016, with an anticipated completion date of mid-November 2016.

More detailed information on the leasing arrangements and rental income; repair liabilities and cost recovery; and recovery through the service charge was provided at Section 1 of the report.

For the avoidance of doubt, the Deputy Leader stated that scaffolding had been erected at the Market Hall due to the need to survey the extent of the damage to the roof. That did not mean that a decision on the repair work had already been taken.

The Deputy Leader highlighted, in particular, Section 1.4 which recorded that BAE had put forward a proposal to extend their ground lease by a further 99 years, and the Council had engaged Cushman & Wakefield to advise and negotiate the detail of the lease extension to ensure best value was achieved for the Council. The extension of the head-lease was considered to be beneficial to the Council as it would not only secure an extended revenue stream, but would also secure the ongoing maintenance liability for the Grade II listed building. Negotiations to extend the head-lease would include proposals to consecutively extend the Council's under-lease of the stall holder area and would facilitate the opportunity to update the outdated Market Hall Management Agreement.

In terms of the proposals before Members the Deputy Leader explained that, subject to the agreement of detailed terms of the lease extension, it was likely that the majority of the costs of the repair works would fall as permitted deductions affecting the Council's annual rental income. However, on the assumption that BAE was prepared to spread the recovery of the Council's costs liability through the rent it paid, it would be reasonable for BAE to include an interest charge on the outstanding balance, therefore increasing the overall cost liability of the Council.

In order to protect and enhance its investment, it was proposed that the Council make a one-off capital contribution to fully discharge its costs liability, with the payment being made from the capital sum earmarked as a contribution to the Market Hall repair works (approved by full Council on 2 February 2016).

He added that discussions were taking place via the Market Hall Managing Agent to ensure that the stall holders were kept fully apprised of the works and any potential business disruption those may cause. It was further proposed that the suggested head-lease extension, subject to the agreement of detailed terms, be agreed with the tenant.

In conclusion the Deputy Leader, and Finance, Governance and Resources Portfolio Holder moved the recommendations.

The Leader seconded the recommendations.

Summary of options rejected Not to approve the release of capital monies /
delegate the agreement of detailed terms

DECISION

That the Executive:

1. Approved the release of capital monies earmarked in the Capital Programme to meet the Council's repair work funding liability.
2. Delegated the agreement to the detailed terms of the proposed head-lease and under-lease extension to the Building and Estates Services Manager and the Asset and Investment Services Manager in consultation with the Director of Governance.

Reasons for Decision

The recovery of the cost of the essential works through the service charge would have a detrimental effect on the tenants, the Council and BAE through potential loss of income and difficulties in the re-letting of vacant space

BAE had put forward head-lease extension proposals. The Council had employed an external investment adviser to negotiate the detail of the head-lease extension, and to agree the best way of updating the outdated management agreement

Discussions had commenced with BAE, in conjunction with negotiations relating to the head-lease extension, to agree the non-recovery of the repair costs from the stall holders through the service charge. It was anticipated therefore that the majority of the repair costs would fall as permitted deductions which would affect the rent the Council received

The Council currently held a capital sum in the Capital Programme earmarked as a contribution to the Market Hall repair works. The payment of a capital contribution would protect and enhance the Council's investment asset