Cambridge City Council **Item**

To:	Leader of the Council
Report by:	Head of Strategic Housing and Head of Specialist Services
Relevant scrutiny committee:	Strategy and Resources
Wards affected:	All

Future of Park Street Car Park

Key Decision

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1. Executive summary

The Leader of the Council approved the requirements for the redevelopment of the Park Street Car Park at the Strategy and Resources Committee on 12 October 2015. This report addresses specific requests for further work made by the Leader of the Council at the last meeting in respect of preferred tenure mix; preferred development option; how the Council maximise the opportunities to provide housing that is affordable; and whether to build the Affordable Housing itself or to sell it to a Registered Provider. It also confirms that a Planning and Development Brief for the site will be developed and outlines how a final scheme will be brought forward for scrutiny.

2. Recommendations

The Leader of the Council is recommended to:

a. Note the impact of different tenure mixes on financial return for the Council and that a final scheme for the redevelopment of the Park Street Car Park will be brought back to the Strategy and Resources Committee recommending a tenure mix, budget and development option.
b. Note that the final scheme will be have been received prior scrutiny from the Council's Capital Programme Board and will be the subject of a Planning and Development Brief agreed with the Council's planning section.

3. Background

The Leader of the Council approved the requirements for the redevelopment of the Park Street Car Park at the Strategy and Resources Committee on 12 October 2015. These are as follows;

- A 250 space underground car park.
- Above ground a mixed development of market, intermediate and social housing, including the option for commercial rental on the ground floor, in conjunction with cycle parking.
- The same or greater number of cycle parking spaces.

In implementing the redevelopment the Council also require regular communications with the local businesses and neighbouring landowners and other local stakeholders and Members. There is a desire to re-open the car park for Christmas 2018 and to effect alternative car parking during the redevelopment period.

The Leader of the Council specifically requested a report to this Committee to further consider;

a) In addition to those above ground options described in the report to the Committee on 12 October 2015, to also evaluate a further option for a housing mix of 40% social and 60% intermediate housing (the latter funded from the council's general fund for investment return).

b) In order to establish a realistic assessment of the capacity of the site for above ground development, request the Urban Design Team to prepare a full planning brief, analysing its context and constraints in order to enable development value to be optimised within the planning guidance.

c) Explore the preferred mechanism to secure the redevelopment of the site to maximise the opportunities to provide affordable housing on the site within the constraints of financial viability.

d) Explore the preferred housing schemes, to enable the council to decide whether to build the social housing itself or to sell it to a registered provider, and to report back in the next committee cycle.

e) Explore the council developing the project itself, producing the social housing as outlined in the report but retaining and letting out the remaining housing.

This report addresses these specific requests in the context of the Council's requirements for the redevelopment.

First, for the sake of clarity the following is a glossary of terms used in this report in respect of tenure types;

AFFORDABLE HOUSING – Sub-market housing that is required within Planning Policy and can include social housing and some forms of intermediate housing (see definitions below).

SOCIAL HOUSING – Housing provided at rent levels that equate to Local Housing Allowance. (Note – Registered Providers are able to set Affordable Rents up to 80% of market rents if they receive grant on a scheme.)

INTERMEDIATE HOUSING;

- **Shared ownership** housing available within affordability guidelines set by the Homes and Communities Agency
- **Intermediate Rent** up to 80% of market rents.

STARTER HOMES – Homes for sale at up to 80% of market value

Note – If the Planning Policy requirement for 40% Affordable Housing is satisfied, the land owner/developer can choose the tenure mix of the other 60% of housing (provided the scheme is within the broader planning framework of sustaining a mixed and balance community).

The questions about what is the preferred tenure mix; what is the preferred mechanism to secure the redevelopment; how does the Council maximise the opportunities to provide housing that is affordable; and whether to build the Affordable Housing itself or to sell it to a registered provider are all inter-related. In order to guide a decision on these matters a 'Base-line Tenure Mix Option' is proposed with four variations. The preferred development routes are either through a Development Agreement with a partner building contractor or through a joint venture agreement. These alternatives are addressed in the procurement section of the report.

At this stage the need to address the capacity of the site (as outlined in b. above) is an important but secondary question. The work to produce a Planning and Development brief will proceed, but there is sufficient evidence based confidence in the current scale and property types used in financial viability analysis to-date for any subsequent changes not to make a material difference to the questions of tenure mix; maximising housing that is affordable; and development options. An up-date on progress with the production of the Planning and Development Brief is provided later in this report.

When considering the preferred route and alternative options the cost and income figures are those used in the October report except that more current rental data has been used consistent with that used in the business case for the Council's Housing Company. As a reminder, cost data was provided by Bidwells in liaison with Council officers to produce the October report. Also the analysis below excludes the cost of re-providing the car park which as a reminder has been assessed at £9,250,000 and the cost of providing cycle parking and any commercial premises to the ground floor . Other costs associated with alternative car parking while the car park is closed are also excluded. Appendix 1 summarises the cost and income assumptions used in the analysis below.

Base-line Tenure Mix Option

This route makes the following assumptions about the Council's preferred outcomes from the redevelopment;

- Tenure mix of 40% Affordable Housing (as required by Planning Policy) – assume 30% social housing and 10% shared ownership.
- Tenure mix of other housing that maximises the revenue return on the Council's investment as a capital receipt for the Council is currently secondary to a revenue return (a minimum 5% return has been set for use of the Investment for Income Fund).
- Tenure mix of other housing that maximises the provision of housing that is affordable.

The baseline route also assumes that the 40% Affordable Housing is sold to a Registered Provider on a long lease (125 years or more) at a typical market rate. As the Council requires a revenue return as opposed to a capital receipt, the baseline route is for all of the other housing to be made available for intermediate rent at 80% of market rents managed through the Council's new Housing Company.

Financial outcome for the Council;

Capital Receipt (from the sale of the Affordable Housing)
- £4,343,250

Revenue return on investment of £8,409,172 in the intermediate rent

- 3.3% year 1
- 4.7% over 30 years

- 5.1% over 35 years

A variation on the Base-line Tenure Mix Option would be to provide some housing at market rent levels and some at lower than 80% of market rent – say 60% market rent. The following table shows the resulting change in return.

	Baseline	Variant a.	Variant b.	Variant c.	Variant d.
% market rent					
100%	0	14 units	28 units	0	0
80%	28 units	14 units	0	14 units	0
60%	0	0	0	14 units	28 units
Return					
Year 1	3.3%	3.8%	4.3%	2.7%	2.3%
Year 30	4.7%	5.6%	6.4%	3.7%	2.9%
Year to achieve 5%	35	23	12	48	Over 50 years

<u>Planning and Development Brief</u>

The planning policy and urban design teams have been engaged to assist in the preparation of a Brief. The brief will be submitted to the Development Plan Scrutiny Sub-Committee for approval with a target date of March 2016. As well as access, the brief will set the framework for the redevelopment in terms its scale, mass and height and its design in relation to the historic environment.

4. Implications

(a) **Financial Implications**

Please see Background section of the report above.

(b) **Staffing Implications** (if not covered in Consultations Section)

The Council's Strategic Leadership Team has endorsed that the Housing Development Agency should project manage this scheme reporting to the the Head of Property Services as the Council's lead representative.

(c) **Equality and Poverty Implications**

These will be considered as part of the final scheme for the redevelopment of the Park Street Car Park will be brought back to the Strategy and Resources Committee recommending a tenure mix, budget and development option.

(d) **Environmental Implications**

The requirements of then Council in respect of the redevelopment offer to substantially improve the local environment in and around the car park site by reducing the number of car parking spaces but retaining safe and secure cycle parking.

Residential provision will be at least to the equivalent of Level 4 of the Code for Sustainable Homes.

(e) **Procurement**

Development Options

In general there are five main options to development a site such as Park Street Car Park, although there are potentially variations to each of these options.

1. Disposal (Sale) of the site
2. Traditional Route – Separate commission and funding of design and construction
3. Development Agreement
4. Joint Venture
5. Council as sole developer

Park Street Car Park is a confined site (48 units plus commercial and underground car park) in a high value part of the city (estimated construction cost – £20,000,000 including car park). There are some abnormal construction stage costs eg demolition and the underground car park. The preferred development option is dependent on the Council's view on the preferred tenure mix (including whether there is to be market housing); the extent that the Council has the appetite to cover all of the costs and risks; and whether it has the capacity and skills to manage the development itself or can procure the capacity and skills. In view of the high costs and risks associated with this redevelopment it is not recommended that the Council acts as developer. The site can be developed as an individual scheme under Option 3 or under Option 4.

In simply terms, the decision on which development option is chosen will depend on the degree of risk that the Council chooses to take in developing the scheme balanced by the potential reward (usually financial).

The following are the main risks associated with development (assuming the site is already in the Council's ownership);

A. Pre-planning

Legal constraints – eg existing rights of way; leaseholders; sitting tenants; utility wayleaves; boundary ownership etc.

Physical constraints – eg contamination; soil and sub-structure; topography; drainage; archaeology; ecology etc.

Location constraints – eg highway access; neighbouring land uses; airfield crash zones; flood zones etc.

B. Planning

Achieving planning approval

C. Construction stage

Design and construction – eg selection and performance of property consultants and contractors. Site clearance costs. Site servicing eg provision of gas; electric; water; sewers and site roads. Build cost inflation. Availability of skilled labour and materials.

D. Marketing, sales and lettings

Competition for properties for sale; fall in property values; lack of demand for rented houses etc.

Another key risk is whether the Council has the skills and capacity in its current staff establishment to manage particularly the marketing and sales stage if a development involves market housing. Consideration of tax; legislative and regulation change; and size and complexity of the scheme; who funds the construction period; and the time to develop the site are all important too in relation to the choice of development option.

The vast majority of these risks can be mitigated for a cost.

In terms of reward, planning and property law endorses the view that the more development risk (and potential cost) a developer of land is exposed to the greater their profit should be. Profit margins (often called developer profit) can range between 15% and 30% construction costs. As can be seen from above, there are risks at distinct stages in the development process and different organisations in the development sector make their business by speculating that they can mitigate the risks at the different stages. A developer will buy a site that does not have a planning approval; will mitigate the legal, physical and locations constraints; will secure a planning approval; will prepare a serviced site and will sell the site on to a house-builder. A fully serviced site with planning approval will have a higher value than when the developer bought the site. A house-builder will buy fully serviced sites and specialise in understanding the housing market and marketing and selling new homes to make their profit. A building contractor makes their business in constructing the houses. In practice some organisations act across the spectrum of developer; house-builder and contractor.

From the Council's point of view, as landowner, it can pass the development risks to a partner developer, house-builder or contractor to a greater or lesser extent under the options 1 to 5 above. However, the more development risk it passes to a partner the more reward the developer; house-builder and contractor sector will expect to receive with the reward being defined as profit margin and increased development value of the scheme. This relationship between risk and reward in the 1 to 5 development options is shown in the following diagram.

In respect of the Park Street Car Park site, as the Council is looking to achieve a 'double bottom line' of a long term revenue return on investment and meeting housing need, straightforward sale of any site can be discounted. The Council prefers revenue income to a capital receipt at this time. Option 2 – the traditional route can be discounted for higher cost higher value schemes as it entails significant up-front cost to procure a design and a building contractor. This route is more suited to schemes where there is not the opportunity to share these costs with a partner than can realise speculative market or commercial development as part of the scheme. Development of the Clay Farm Community Centre is a good example but this is not the case for the Park Street Car Park.

In a Development Agreement (Option 3) the Council can specify which risks it proposes to pass on and asks the market through a tender process to put a price on what it is prepared to pay to realise potential profit and up-lift in the schemes development value. This is a strong option if the Council wishes to de-risk the development of individual schemes and would prefer to fix its costs and return and to pass on development reward.

Under Option 4 – a joint venture – the Council would agree from the outset which risk it will share with a partner and will therefore share that some of the rewards will not be realised. (Note – Option 3 is applicable to individual schemes whereas a joint venture can cover more than one scheme)

Option 5 is not applicable if there is no market housing on the site as there will be no developer profit. If the Council chooses to require some market housing and develop the scheme itself, it will accept the cost of mitigating all of the risks and will retain the developer profit and will speculate on the up-lift in development value. This is not an option that the Council has any direct experience on relation to large, complex and high value sites.

To help quantify the cost of risk mitigation and the extent of the reward, the following table analyses this and compares Options 3 to 5 based on costs provided by Bidwells for the Park Street scheme.

	Option 3 – Development Agreement	**Option 4 – Joint Venture**	**Option 5 – Council as Developer**
COST RISK			
Pre-planning – estimate say £50,000 - £100,000	To de-risk completely the partner can be required to cover all of these costs.	The partner would usually be expected to cover all of these costs – but see impact on 'Reward' below.	The Council would need to fund these costs up-front.
Planning – estimate £500,000 including section 106 and public art costs	The partner can be required to cover all of these costs but it is usual for the 'market' to expect that some of the costs will be shared if a scheme does not achieve a planning approval.	The partner would usually be expected to cover all of these costs – but see impact on 'Reward' below.	The Council would need to fund these costs up-front.
Construction – estimate £9m to £10m.	The partner can be required to source and manage the construction and cover all of these costs. The partner may have a construction arm.	The partner would usually be expected to source and manage the construction and cover all of these costs. The partner may have a construction arm – but see	The Council would need to fund these costs up-front and would need to source and manage the construction. (Note – construction companies will

		impact on 'Reward' below.	typically apply a 6% profit on construction contracts depending on the complexity of the build.
Marketing and Sales. Estimate 1.5% of market value of any homes for sale.	The partner can be required to cover all of these costs.	The partner would usually be expected to cover all of these costs – but see impact on 'Reward' below.	The Council would need to fund these costs.
Development Finance – who funds the construction period costs – interest estimate £600,000	The partner can be required to cover all of these costs.	The partner would usually be expected to cover all of these costs – but see impact on 'Reward' below.	The Council would need to fund these costs.
REWARD			
Developer Profit – estimate £3,000,000 **(NOTE – ONLY APPLICABLE IF THERE IS MARKET HOUSING).**	If the Council is requiring the partner to cover all of the risks and costs as above, the 'market' would expect the partner to retain the Developer Profit although this can be 'capped' in a rising property market.	Depending on the extent that the joint venture agreement provides for the risks and costs to be shared, the Developer Profit can be shared eg 50:50 - £1,500,000.	The Council would retain the Developer Profit or in other words, does not have to pay the Developer Profit.
POTENTIAL REWARD TO COUNCIL	Land Value	Land Value plus £1,500,000	Land Value plus £3,000,000
POTENTIAL REWARD TO PARTNER	£3,000,000	£1,500,000	£0

While the rewards of development can be high, this reflects the inherent risks involved. The above example gives an indication of potential differences in reward between the various development options. The Council could achieve an additional profit of about £1.5m from acting as a developer assuming everything goes to plan. If the costs vary by 10-15%, however, this additional profit is soon reduced. Some aspects of the development appraisal are very sensitive to small changes with relatively large effect on values. For example, a change in yield (rate of return) from 5.5% to 6% can reduce capital value by about 8%.

Developers are experts in managing these risks and driving out profits from schemes. They decide which aspects of the development process they will undertake and which aspects they will pass to others where they perceive others can better manage risk. For more complex or higher value schemes, without development expertise or appropriate resource, as well as the cost risks set out above, there is also a risk that failure to manage the development process in a timely way or deal with unforeseen events as they arise can quickly increase costs.

Development partners bring expertise, resource and experience to schemes. They can also help with pace due to the relative size of their organisation and ability to call in resource when required.

There will be some direct costs incurred by the City Council whatever development option is chosen to, for example, cover any procurement costs and legal costs to set up a contract with the partner and project management through the Housing Development Agency.

(f) **Consultation and communication**

The Council has consulted with the public and businesses about the potential options for redeveloping the car park.

Informal consultation has taken place in advance of this report to consider how to mitigate the economic impact of the loss of public parking facilities in the immediate vicinity of the Park Street car park during the period of redevelopment.

A communications strategy will be prepared to publicise and consult on plans and proposals relating to this redevelopment, including potential planning application and mitigation arrangements

(g) **Community Safety**

This project is intended to have a neutral impact on Community Safety.

5. Background papers

None

6. Appendices

Appendix 1 summarises the cost and income assumptions used in the analysis below.

7. Inspection of papers

To inspect the background papers or if you have a query on the report please contact:

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Appendix 1 - Summary of Cost and Income Assumptions

1. **Property Mix (As per Bidwells report)**

   Affordable Housing

   - 10 one bedroom
   - 10 two bedroom

   Other Housing

   - 14 one bedroom
   - 14 two bedroom

2. **Market rents (Based on Home-track data at July 2015 using upper quartile)**

   One bedroom - £219 per week
   Two bedroom - £298 per week

3. **Cost of Residential (As per Bidwells report)**

   Build and On-costs - £12,687,648