Hinckley & Bosworth Borough Council

FORWARD TIMETABLE OF CONSULTATION AND DECISION MAKING

SCRUTINY COMMISSION 18 JULY 2019

WARDS AFFECTED: ALL WARDS (Hinckley)

RETENTION OF BLOCK C AND POTENTIAL IMPACT ON MTFS

Report of Head of Finance (S151 Officer)

1. PURPOSE OF REPORT

1.1 To inform members of the potential impact of the decision to retain block C at the Crescent site.

2. RECOMMENDATION

2.1 To note impact and potential savings or extra income needed

2.2 To consider the potential use of capital receipts and reserves use to off set the impact of the decision to retain Block C.

3. BACKGROUND TO THE REPORT

3.1 The Council in 2013 agreed to back an £80m regeneration scheme as part of its vision to redevelop the former bus station site. This included entering into a development agreement with Tin Hat Partnership to secure the completion of the whole scheme, including supermarket, shops, car park, bus station, cinema and family restaurants and public realm improvements. To ensure this development went ahead the Council invested £4.5m in the purchase of Block C, a multiple unit retail site. In addition, the business rate gain in ensuring development of the whole site was considered at the time as generating an additional £377,000 of business rate growth to the Council.

3.2 To this end the Council has achieved its primary aim of redevelopment and regeneration of this former rundown area of the town centre. The Crescent is a major shopping and leisure scheme that formed part of a comprehensive regeneration plan to transform the former rundown bus station site. Since its completion in October 2015 it has proved a major success transforming the town centre and introducing a range of family entertainment uses including a new cinema and family-orientated restaurants, new retail units including a major Sainsbury's superstore, over 500 car-parking spaces and a new bus station facility. Further information on the original purchase costs and current rental performance is given in appendix 3.

3.3 On the 21 May 2019, the decision to retain Block C was agreed at Council via a Member proposed motion. The key basis and rationale for retaining block C in Council ownership by the current Administration are as follows:

- The units in ‘Block C’ currently continue to bring an income in to the Council of over £336,000 per annum, with a net return before interest of £117,691

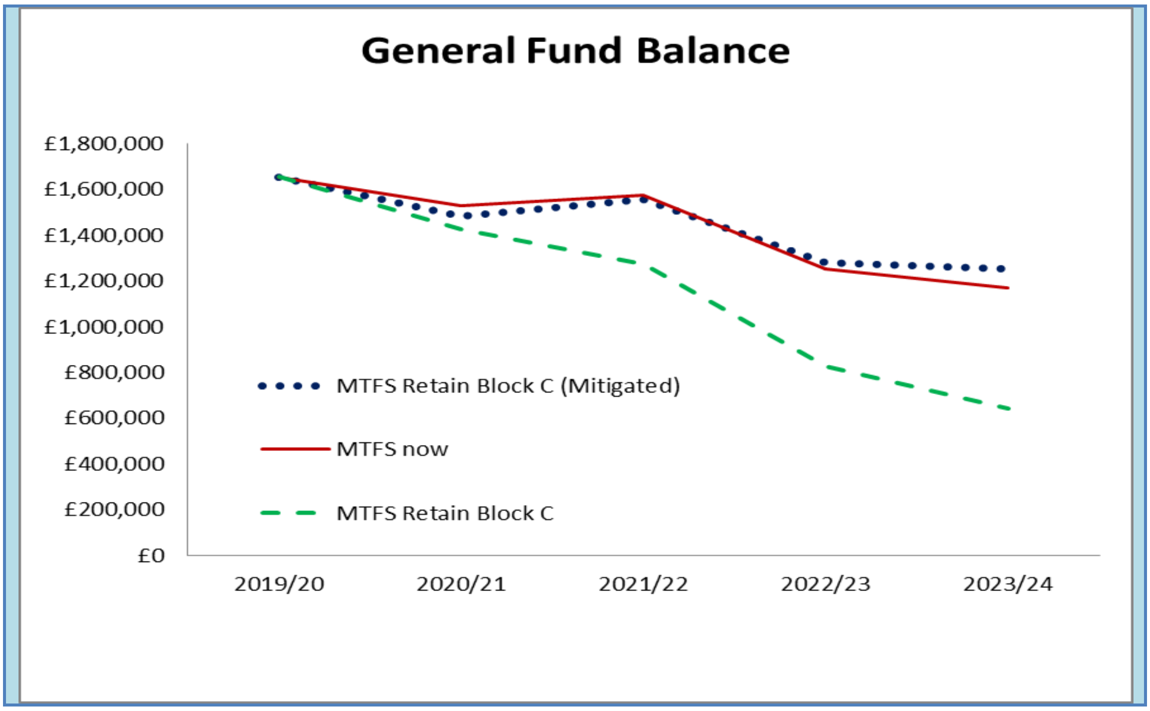
- This will signal the Council’s unequivocal commitment to Hinckley town centre as a key retail and leisure destination for local residents and visitors

3.4 It has been widely reported that since 2015 local authorities have spent an estimated £800m on acquiring shopping centres in a bid to safeguard and take control of prime commercial assets to underpin confidence in town centres. Therefore, HBBC is not alone in having such assets. As well as bringing benefits to these areas, there are also ongoing risks for councils associated with such investments. These are included in section 9 below.

3.5 This report considers the impact of that decision on the MTFS and the potential mitigating strategy to address that impact.

3.6 The affect on the General Fund Balance, before any mitigating actions are taken, over the life of the MTFS is noted in table 1 and accompanying graph below. The cause of the change is due to having to fund the crematorium project from a £4m loan as opposed to the capital receipt from the sale of Block C and the impact of slippage by 4 months on the delivery start time for the crematorium to become operational. As the sale is not happening, this slippage only makes about £20,000-£25,000 difference in 2020/21 post the decision to keep, but £125,000 difference on the previous MTFS agreed in February. Therefore £100,000 of pressure now faced is due to slippage on the operational start date and not the decision to retain Block C.

Table 1 GF balance	2019/20	2020/21	2021/22	2022/23	2023/24
MTFS now	1,651,887	1,529,004	1,575,073	1,249,475	1,167,841
MTFS Retain Block C	1,651,887	1,423,463	1,271,375	826,484	641,864
MTFS Retain Block C (Mitigated)	1,651,887	1,482,138	1,554,262	1,279,398	1,251,193
GF balance	**2019/20**	**2020/21**	**2021/22**	**2022/23**	**2023/24**
MTFS now	15.26%	15.06%	15.03%	11.47%	10.17%
MTFS Retain Block C	15.26%	14.02%	12.13%	7.59%	5.59%



3.7 In order to return the MTFS to a similar level of general fund performance as the original MTFS, two key areas can be used to address the pressure created in a full refresh MTFS. These include a review of:

- the assumptions for income generation from the crematorium
- the use of reserves and capital receipts

3.8 A full refresh of the MTFS would also consider opportunities for other commercial and income generation opportunities. These areas will be reviewed more fully when the MTFS refresh is completed and have not been modelled in this interim report which is limited to the issues surrounding the retention of Block C

Mitigation actions suggested

Number of Cremations

3.9 The Model used currently assumes through put will commence at 700 cremations in the first year, growing by 1% annually. This could be modelled at 800 cremations as opposed to 700 in year 1, which does not seem unreasonable based on local comparisons with other crematoria (appendix 2). This would be based on internal opinion and not based on independent external consultant advice, so may need to be confirmed as achievable. Under the current model 800 cremations will be achieved after 15 years. The maximum operating capacity of the cremator is 1,200 cremations a year, hence 800 cremations is within operational capacity. This changed assumption would increase forecast net returns by £442,000 over the 5 years of the MTFS.

Use of Capital Receipts and Reserves

3.10 It is the cost of servicing a loan of £4m that reduces the return from the crematorium project, therefore reducing this cost would increase the return generated. The cost of the loan could be reduced by using capital receipts and underspends, plus earmarked reserves to help fund the cost of purchase. There is £1.2m of capital receipts that could be used to offset the loan costs. This could be increased by further use of earmarked reserves of £850,000 noted in the table below.

Table 4: Reserve	£
Hub Future Rental Management Reserve	400,000
Uncommitted Hinckley Community Development Fund	200,000
Uncommitted Developing Communities Fund	200,000
Other reserves	50,000
Total	850,000

3.11 If this is agreed, the loan required based on current expectations, would be reduced to £2,000,000. A further £50,000 from other reserves will need to be released in 2020/21 to support the general fund balance. This brings the total use of capital receipts and reserve use to £2,050,000. This would generate a further £765,000 of net return of the 5 years of the MTFS.

3.12 This does mean of course that £2,050,000 from earmarked reserves and capital receipts will not be available for other areas and will be used prior to any indication of how we will be affected by the fair funded review. However, they are being used to generate future higher returns. This use of capital receipts and earmarked reserves should increase the net return from the crematorium by £153,000 per year, which represents a 7.7% rate of return. However, if used for this purpose, other areas of potential use will be foregone. In addition, other decisions that may reduce income significantly or increase costs will need to be delayed until it is clearly demonstrated they are affordable.

Combined increase in cremations and use of capital receipts and reserves

.3.13 In order to bring the MTFS performance to a similar slightly improved position, the increased cremations and use of capital receipts and reserves would have to be approved. If this were done, the profile would be as noted in the table below, which is at over 15% for three of the 5 years.

Table 6 GF balance	2019/20	2020/21	2021/22	2022/23	2023/24
MTFS now	1,651,887	1,529,004	1,575,073	1,249,475	1,167,841
MTFS Retain Block C	1,651,887	1,532,138	1,604,262	1,329,398	1,301,193
GF balance	**2019/20**	**2020/21**	**2021/22**	**2022/23**	**2023/24**
MTFS now	15.26%	15.06%	15.03%	11.47%	10.17%
MTFS Retain Block C	15.26%	15.09%	15.31%	12.21%	11.34%
Increase	0.00%	0.03%	0.28%	0.74%	1.17%

3.14 If cremations do commence at 700 in the first year and grow at 1% as modelled, then the pressure on reserves to bring the profile of the MTFS general fund balance onto a similar forecast to the current MTFS, would be an extra £190,000. This would bring the total use of capital receipts and reserves to £2,190,000. This could be done if a further £190,000 was used for this purpose. This risk could be covered from the Developing Communities Fund (DCF) reserve. This would mean that £390,000 had been taken out of the DCF reserve and would require a significant curtailment of phase 2 of the DCF scheme

Other considerations

3.15 There is a high risk that another unit will soon become empty, if we assume a loss of rental for one year, and that the council will become responsible for business rates, this would be a pressure of £30,000 of lost rent and £7,500 of business rates for the first year. The business rate charge would double if the unit were empty for longer than one year, as we would not get empty property relief in subsequent years. There would also be a service charge of £7,200 falling on the Council. This has not been included in the calculations in this report as it is anticipated that the unit may be re-let with only one-year's loss of rental, which would be absorbed by the asset management reserve. See Appendix 3, "Current Rental position and Analysis," for further risk analysis on rentals.

3.16 There is always a risk the Crematorium costs may be different to that currently planned due to changes, if needed, to the business plan, or the way in which the project is delivered. In this case, the return may be lower than expected. Therefore, forecast performance is not guaranteed, but what is currently planned using the current model of developed and run by the Council. Other factors could also reduce the return from the Crematorium. For example, if cremations numbers take longer to reach planned levels at the site, then this will mean the net return will be lower than budgeted in the forecasts used in this report.

3.17 There are other potential areas that could help address the MTFS pressure. These are:

- The negotiations with the LLEP in relation to the Business rates agreement, may lead to increased income.
- There is a £500,000 gain from being in the business rate pilot that may lead to savings once what it will be used for is decided, and.
- There is the potential to consider changes to our investment policy to see if higher returns can be obtained from longer term investment.

3.18 These will be considered as part of the MTFS refresh and have not been reflected in the considerations and calculations above.

4. EXEMPTIONS IN ACCORDANCE WITH THE ACCESS TO INFORMATION PROCEDURE RULES

4.1 None

5. FINANCIAL IMPLICATIONS [AW]

5.1 Contained within the body of the report.

6. LEGAL IMPLICATIONS [MR]

6.1 The MTFS provides the foundations to allow the Council to meet its statutory obligations in accordance with Section 32 of the Local Government Finance Act 1992 and section 25 of the Local Government Act 2003. The Council has a statutory requirement to set a budget for each financial year and approve the MTFS, including a three year capital programme.

7. CORPORATE PLAN IMPLICATIONS

7.1 The additional funding will help to deliver Corporate Plan priorities.

8. CONSULTATION

8.1 None needed

9. RISK IMPLICATIONS

9.1 It is the Council's policy to proactively identify and manage significant risks which may prevent delivery of business objectives.

9.2 It is not possible to eliminate or manage all risks all of the time and risks will remain which have not been identified. However, it is the officer's opinion based on the information available, that the significant risks associated with this decision / project have been identified, assessed and that controls are in place to manage them effectively.

9.3 The following significant risks associated with this report / decisions were identified from this assessment:

Management of significant (Net Red) Risks		
Risk Description	Mitigating actions	Owner
The Council's decision to purchase Block C was to ensure regeneration of the town centre, continued ownership does bring with it risks similar to having entered into commercial investment in retail units. These risks are a declining high street as the primary shopping experience, volatile and intermittent income stream and ongoing property owner costs.	Report at least annually, and by exception as needed, a review of the finances of Block C to the Executive, and the Finance and Performance Scrutiny Committee to ensure ongoing investment is monitored. There will also be an annual review of MTFS based on range of options to be considered by Scrutiny and Council to cover any potential pressures on the general fund and how they can be addressed.	A.Wilson

10. CORPORATE IMPLICATIONS

10.1 By submitting this report, the report author has taken the following into account:

- Community Safety implications
- Environmental implications
- ICT implications
- Asset Management implications
- Procurement implications
- Human Resources implications
- Planning implications
- Data Protection implications
- Voluntary Sector

Background papers: None

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Executive Member: Councillor Keith Lynch

Appendix :MTFS comparison

As per current MTFS					
	2019/20	2020/21	2021/22	2022/23	2023/24
	Forecast	Forecast	Forecast	Forecast	Forecast
Net Service Expenditure	11,384,598	11,082,610	11,406,989	11,344,541	11,664,975
Block C Rentals	28,570	100,810	0	0	0
Crematorium	0	-220,075	-174,304	-17,874	-18,676
All Other net.	-330,558	443,644	111,856	338,308	370,507
NET Borough Budget Requirement	11,082,610	11,406,989	11,344,541	11,664,975	12,016,806
Net reserve/grants unapplied movements	-411,109	-1,131,391	-909,710	-447,850	-456,595
Contribution to/(from) Balances	155,527	-122,882	46,069	-325,599	-81,633
NET BUDGET/FORECAST EXPENDITURE	10,827,029	10,152,715	10,480,901	10,891,526	11,478,578
General Fund balance	1,651,887	1,529,004	1,575,073	1,249,475	1,167,841
	15.26%	**15.06%**	**15.03%**	**11.47%**	**10.17%**
MTFS No sale of Block C					
	2019/20	2020/21	2021/22	2022/23	2023/24
	Forecast	Forecast	Forecast	Forecast	Forecast
Net Service Expenditure	11,384,598	11,082,610	11,512,530	11,542,698	11,784,268
Block C Rentals/Service charges	28,570	0	-10,417	-22,083	0
Crematorium	0	-13,724	-71,272	-74,655	-34,981
All Other net.	-330,558	443,644	111,856	338,308	370,507
NET Borough Budget Requirement	11,082,610	11,512,530	11,542,698	11,784,268	12,119,793
Net reserve/grants unapplied movements	-411,109	-1,131,391	-909,710	-447,850	-456,595
Contribution to/(from) Balances	155,527	-228,424	-152,088	-444,891	-184,620
NET BUDGET/FORECAST EXPENDITURE	10,827,029	10,152,715	10,480,901	10,891,526	11,478,578
General Fund balance	1,651,887	1,423,463	1,271,375	826,484	641,864
	15.26%	**14.02%**	**12.13%**	**7.59%**	**5.59%**
Difference	0.00%	-1.04%	-2.90%	-3.88%	-4.58%

Appendix 2: local cremation rates and fees

Crematoria	2016 Cremations	2017 Cremations	Jan 2017 fee	Jan 2018 fee	total cost
LEICESTERSHIRE					
Countesthorpe	1,462	1,387	£860.00	£900.00	£955.00
(South Leicester)					
Great Glen (Opened March '17)	0	505	£825.00	£845.00	£895.00
Leicester	2,364	2,119	£765.00	£799.00	£799.00
Loughborough	1,695	1,571	£969.00	£1,035.00	£1,035.00
WARWICKSHIRE					
Coleshill (Woodlands)	819	943	£710.00	£710.00	£755.00
Leamington Spa	1,711	1,880	£650.00	£685.00	£685.00
Nuneaton	1,928	1,988	£999.00	£1,070.00	£1,070.00
Rugby (Rainsbrook)	875	871	£775.00	£775.00	£775.00
DERBYSHIRE					
Alfreton (Amber Valley)	1,190	1,346	£770.00	£799.00	£843.00
Chesterfield	2,178	2,339	£690.00	£730.00	£773.00
Derby	2,591	2,652	£697.00	£671.00	£671.00

Appendix 3: Purchase and Rentals

<u>Original purchase decision</u>

A1.1 The table below gives a summary of the financial position of the council's ongoing investment in Block C, compared to that reported to Council in November 2013 when the scheme was approved, which was £487,250. The view reported to members in November 2013 was that a breakeven rental would be £309,250, excluding Business Rate considerations on the wider development.

Table 7: Comparison of original target/Budget to actual	
Original Target rental Income per year	£487,250
Actual (2018/19)	£331,143
Shortfall	**-£156,107**
Original Capital Budget approved	£4,500,000
Cost of Block C	£2,090,000
Incentives	£2,603,750
Sub-total	£4,693,750
Spend above original Budget	**-£193,750**

A1.2 There has also been a profit share receipt of £718,064 which has not included in the above calculations, as this was related to the sale of the rest of the Crescent site by the partner developer. In July 2013, this had been forecast to be £1,200,000, but the profit made by the developer on their share of the Crescent site was less than anticipated due to changing market conditions.

<u>Current Rental position and Analysis</u>

A1.3 There are two units that remain unlet, which contributes to the rental shortfall. In addition, overall market conditions have meant rents have been lower than forecast, which means that even when the remaining units are fully let, the maximum rental is now expected to be £396,143. This is £91,107 less than the original target rental of £487,250. Higher incentives have also had to be offered to attract tenants. All increases in budget have been approved by Council and supplementaries raised where needed.

A1.4 The most recent MTFS measurement of how the investment is performing assumes the current empty units will be let at half their floor area, as there has been problems in letting the whole of the unit space. The interest is the allocation of interest on a £5m loan taken out to contribute to the financing of both the Leisure Centre and Block C; it will not be paid off if the asset is sold, so this interest will continue to be a cost to the general fund. Therefore, it can be disregarded for the purpose of measuring the return from Block C as the keep or sell decision dos not change the interest cost to MTFS. These factors are noted in the table below.

Table 8	22018/19 (Actual)	2019/20 (Forecast)	2020/21 (Forecast)	Recurring (Forecast)
Rental	£331,123	£341,560	£363,643	£363,643
MRP	-£135,333	-£135,333	-£135,333	-£135,333
Business Rates empty Units	-£59,900	-£44,925	-£29,950	-£29,950
Service Costs	-£18,200	-£13,650	-£9,100	-£9,100
Return before interest	£117,691	£147,652	£189,260	£189,260
Interest (2.96%)	-£83,000	-£83,000	-£83,000	-£83,000
Return after interest	£34,691	£64,652	£106,260	£106,260

A1.5 The table below gives the position expected currently, due to a unit becoming vacant imminently. This has not been included in the current MTFS.

Table 8a	22018/19 (Actual)	2019/20 (Forecast)	2020/21 (Forecast)	Recurring (Forecast)
Rental	£331,123	£311,560	£363,643	£363,643
MRP	-£135,333	-£135,333	-£135,333	-£135,333
Business Rates empty Units	-£59,900	-£51,925	-£29,950	-£29,950
Service Costs	-£18,200	-£25,500	-£9,100	-£9,100
Return before interest	£117,691	£98,802	£189,260	£189,260
Interest (2.96%)	-£83,000	-£83,000	-£83,000	-£83,000
Return after interest	£34,691	£15,802	£106,260	£106,260

A1.6 The table below gives a best case scenario, with the units having the whole floor let, and all units fully let by 2020/21, and the unit currently becoming empty being re-let within 6 months.

Table 8b	22018/19 (Actual)	2019/20 (Forecast)	2020/21 (Forecast)	Recurring (Forecast)
Rental	£331,123	£326,560	£396,143	£396,143
MRP	-£135,333	-£135,333	-£135,333	-£135,333
Business Rates empty Units	-£59,900	-£51,925	£0	£0
Service Costs	-£18,200	-£25,500	£0	£0
Return before interest	£117,691	£113,802	£260,810	£260,810
Interest (2.96%)	-£83,000	-£83,000	-£83,000	-£83,000
Return after interest	£34,691	£30,802	£177,810	£177,810

A1.7 The Table below gives the worse case scenario and assume all empty units remain unlet, and Block C makes a recurring loss.

Table 8c	22018/19 (Actual)	2019/20 (Forecast)	2020/21 (Forecast)	Recurring (Forecast)
Rental	£331,123	£301,123	£301,123	£301,123
MRP	-£135,333	-£135,333	-£135,333	-£135,333
Business Rates empty Units	-£60,000	-£66,900	-£73,900	-£73,900
Service Costs	-£18,200	-£25,500	-£25,500	-£25,500
Return before interest	£117,691	£73,391	£66,391	£66,391
Interest (2.96%)	-£83,000	-£83,000	-£83,000	-£83,000
Return after interest	£34,691	-£9,610	-£16,610	-£16,610

A1.8 The interest is the allocation of interest on a £5m loan taken out to contribute to the financing of both the Leisure Centre and Block C; it will not be paid off if the asset is sold, so this interest will continue to be a cost to the general fund. Therefore, it can be disregarded for the purpose of measuring the return from Block C as the keep or sell decision dos not change the interest cost to MTFS.

A1.9 This calculation ignores inflation or the risk that there will be empty units between lets, or that businesses will fail and not be in place for the whole of their tenure. The information available for business failure rates on the high street is varied, but all indicates a significant pressure, and high failure rates for new start up businesses. This is a significant consideration in terms of considering the medium and longer-term reliability of the income from rents. In addition, it should be noted that many of the Block C units have agreements in place that are for less than 25 years or have break clauses before the expiry of 25 years, see table below. Note, C1 and C2 have not been let and the incentive not used, it currently sits in the Asset Management Reserve if needed.

Table 3 Unit	Terms	As at Nov 2015	Expected/ Current Rent	Incentive	Term	Break clause
C1	Marketing	£85,000	£30,000	£135,000	15yrs	
C2	Marketing	£86,400	£35,000	£150,000	15yrs	
C3/C4	Complete	£67,500	£67,500	£247,500	15yrs	15yrs
C5	Complete	£60,000	£58,543	£210,000	25yrs	15yrs
C6	Complete	£30,000	£30,000	£50,000	25yrs	10yr
C7	Complete	£13,000	£13,000		10yrs	
C8	Complete	£13,000	£13,000		12yrs	
C9	Complete	£17,500	£17,500	£26,250	15yrs	
C10	Complete	£131,600	£131,600	£2,050,000	25yrs	
		£504,000	£396,143	£2,868,750		