

Public Report

Birmingham City Council

Report to Cabinet

Date 22nd January 2019



Subject: PARADISE DEVELOPMENT SCHEME

Report of: CORPORATE DIRECTOR, FINANCE AND GOVERNANCE
AND ASSISTANT DIRECTOR, ECONOMY

Relevant Cabinet Member: Councillor Ian Ward, Leader of the Council

Relevant O &S Chair(s): Councillor Tahir Ali, Economy and Skills

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Are specific wards affected?	<input checked="" type="checkbox"/> Yes	<input type="checkbox"/> No – All wards affected
If yes, name(s) of ward(s): Ladywood		
Is this a key decision?	<input checked="" type="checkbox"/> Yes	<input type="checkbox"/> No
If relevant, add Forward Plan Reference:		
Is the decision eligible for call-in?	<input checked="" type="checkbox"/> Yes	<input type="checkbox"/> No
Does the report contain confidential or exempt information?	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No
If relevant, provide exempt information paragraph number or reason if confidential : Paragraph 3 – report contains commercially sensitive information		

1 Executive Summary

- 1.1 The Paradise Circus development is one of the City's most important and complex regeneration projects that will deliver significant economic benefits. Located within the Greater Birmingham and Solihull Local Enterprise Partnership (GBSLEP) Enterprise Zone, the project has received significant

funding from the GBSLEP to deliver Phase 1 and further funding from the GBSLEP is now required for Phase 2.

- 1.2 This report seeks to ratify the decision of the GBSLEP to award additional funding to the project following the conclusion of the independent appraisal report commissioned by the GBSLEP and the Council (in its capacity as Accountable Body to GBSLEP).
- 1.3 The Paradise scheme is delivered by the Council and approval is now sought to borrow and subsequently defray the amount required for Phase 2 of the development. The presentation attached in Appendix 2 provides Cabinet with an update on progress of the scheme and the reasons for the increase in scheme costs.

2 Recommendations

That Cabinet:

- 2.1 Acting in its capacity as Accountable Body to the GBSLEP, ratifies the decision made by the GBSLEP Board at its meeting on 20th December 2019 to approve the award of up to £51,277,000 of Enterprise Zone (EZ) grant funding to Birmingham City Council for the delivery of Paradise project Phase 2.
- 2.2 Accepts the award of up to £51,277,000 from the GBSLEP for the delivery of the Paradise scheme Phase 2 and to approve the prudential borrowing of that sum as part of a larger EZ Investment Programme.
- 2.3 Notes and agrees to adhere to the GBSLEP conditions of funding set out in section 3.
- 2.4 Approves the expenditure of up to £51,277,000 for continued delivery of the Paradise project, and delegates to the Corporate Director Economy in conjunction with the Corporate Director Finance and Governance authority to defray these sums in line with the Council's and GBSLEP's approved governance arrangements.
- 2.5 Delegates authority to the Corporate Director, Finance and Governance, to enter into new or revised contracts with the developer and PCLP to reflect the additional funding and all terms and conditions attached to it.
- 2.6 Authorises the City Solicitor to prepare, negotiate, execute and complete all relevant legal documentation to give effect to the above recommendations.
- 2.7 Approves the co-commissioning of an independent audit into the Paradise project by the Council acting in its capacity as Accountable Body jointly with the GBSLEP.
- 2.8 Notes progress with the delivery of the Paradise Circus development.
- 2.9 Notes that the project's revised Full Business Case (FBC) is predicated upon a further EZ funding request to the GBSLEP for delivery of Phase 3. This report does not seek approval to Phase 3 expenditure which will be the subject of a

further Green Book compliant FBC to be submitted once the designs and costs are appropriately developed.

- 2.10 Notes that the FBC has been reviewed separately by the Department for Business, Energy and Industrial Strategy and that the revised agreement addresses their concerns.

3 Background

- 3.1 The redevelopment of Paradise Circus is one of the City's key regeneration projects. Once complete it will constitute a landmark development within Birmingham supporting the transformation of this part of the City Centre with the delivery of high quality office, retail and leisure space alongside a world class urban realm. It will expand the City's central business district, connecting Colmore with the Westside area, further strengthening Birmingham's offer and competitiveness as a premier UK business destination.

- 3.2 The scheme will deliver up to 2 million sq ft (Net Internal Area), containing:

- Grade A Offices, in up to ten new buildings (BREEAM Excellent as minimum standard with the opportunity to achieve BREEAM Outstanding)
- 4* hotel with up to 250 bedrooms
- Lower level shops, bars, cafes, and restaurants
- Up to 550 car parking spaces
- Buildings from 70,000 sqft to 400,000 sqft
- Floor plates from 12,000 sqft to 40,000 sqft.
- Business rates of £527,000,000

- 3.3 In March 2013 the Greater Birmingham and Solihull LEP (GBSLEP) approved an investment into the project of £61.3m, subsequently increased to £87.79m in line with scope changes in July 2014 with an indicative allocation across 3 phases as follows:

- Phase 1 - £37.685m
- Phase 2 - £28.007m (inc £21.000m BCU relocation costs)
- Phase 3 - £22.098m

- 3.4 The funding is for major infrastructure improvements including:

- Remodelling of the highway network
- Demolition of the former library building and site wide reconfiguration
- Significant improvements to the public realm

- 3.5 Paradise Circus Limited Partnership (PCLP) was established as a joint venture between BCC and the British Telecom Pension Scheme (managed by Hermes) to deliver the project. Argent are the development manager, BCC act as funding applicant and recipient for the EZ funds.

- 3.6 Progress to date has been significant with major alterations to the inner city ring road, demolition of the Central Library, Birmingham City University

Conservatoire and Chamberlain House. These works have contributed to the delivery of all three phases of the scheme.

3.7 Phase 1 will complete in 2019 and comprises;

- One Chamberlain Square – 172,000 sq ft office building including retail/restaurants on the ground floor, which will be occupied by PWC.
- Two Chamberlain Square – 183,000 sq ft office building including retail/restaurants on the ground floor.
- The two buildings yield £168m in new business rates by 2045/46.

Phase 1 - Delivery Challenges

3.8 The delivery of Phase 1 has been affected by a number of challenges which have impacted on costs;

- Grade A Office rents have not increased since 2010.
- Construction cost inflation has been double market forecasts.
- Substantially more infrastructure investment is required than was anticipated due to increased scope of works, demolition and remediation costs and part Carillion liquidation costs

Phase 2 – Additional Funding request

3.9 In addition to the increased costs for Phase 1, the updated development appraisal for delivering Phase 2 has indicated that additional funding of £51.277m is required for a number of reasons including;

- Former contractor (Carillion) liquidation costs
- Compulsory Purchase costs of the Copthorne hotel
- Additional unforeseen infrastructure works

3.10 In March 2018, as a consequence of these issues a change request was submitted to the GBSLEP by BCC to cover variations on both Phases 1 and 2 that would subsume the funds made available for Phase 3 and require an additional £51.277m to complete the project to Phase 2 stage.

3.11 A fuller breakdown of the project variance is set out in Appendix 2. There is no specific funding request for Phase 3 nor a commitment to deliver this phase and a future FBC will be submitted.

3.12 The revised FBC for the additional funding has been shared with BEIS following a request from them in September 2018. The findings have been reported to the GBSLEP and concluded that the FBC demonstrates value for money and that there may also be wider strategic reasons for supporting the project.

Key points from the independent appraisal report:

3.13 The main conclusions from the independent appraisal report on the five cases of the FBC are as follows:

- 3.14 Strategic case - the scheme is a critical component of the regeneration of Birmingham City Centre and has a strong fit with GBSLEP's wider strategic and economic objectives. There is expected to be market demand for the proposed office accommodation. A rationale for public sector investment is identified in terms of externalities and the provision of public goods.
- 3.15 Economic case - the economic costs and benefits of the scheme have been assessed. The FBC identifies that the preferred option demonstrates an overall positive Benefit-Cost Ratio (BCR) of 4.06 and is estimated to perform more strongly than each of the other three intervention options considered and the 'do nothing alternative'. However, value for money based on the assessed BCR is substantially less than the original appraisal due mainly to the substantially higher public support required. For Phase 2 specifically, the additional funding request will result in the creation of 410,000 sq. ft. and a 250 bedroom hotel that will need to be delivered by the developer.
- 3.16 Commercial case - PCLP remains the delivery vehicle for the scheme as a 50/50 joint venture between BCC and the British Telecom Pension Fund. The delivery arrangements are governed by a complex commercial legal structure which controls financial contributions and returns as assessed during consideration of the original business case. For Phase 2, Argent Services LLP will continue as overall delivery manager with the additional support of Quantem Consulting as project manager and Sir Robert McAlpine as the main contractor. The contractor appointment is designed to incorporate appropriate competition.
- 3.17 Financial case - PCLP is seeking additional public sector funding of £51.277 million for Phases 1 and 2 of the scheme and has also indicated that a further request for funds will be made in the future for Phase 3 based on a Green Book compliant business case. However, no funding is sought for Phase 3 at this stage. The cost increases and reduced receipts have been reviewed by Gardiner & Theobald (G&T) and Cushman and Wakefield. Further detail is contained in the private report.
- 3.18 Management case - the overall governance arrangements remain consistent with the original appraised proposals - with corporate governance fulfilled by the Joint Venture partners, the Joint Venture company responsible for overall success of the scheme, and Argent Services LLP responsible for overall delivery supported by project management, legal, and fund management advisers. Management arrangements for Phase 2 have been strengthened with the appointment of Quantem as project manager (with professional support to include architect, structural engineers, and construction) and Sir Robert McAlpine as main contractor.
- 3.19 The inadequate management and control exercised in Phase 1 is recognised by all parties and proposals to adopt revised procedures have been identified in the updated business plan. Further specific monitoring and reporting arrangements are part of the GBSLEP conditions on funding, which are set out below and within the private report where commercially sensitive:

- the development of a detailed Funding Agreement which includes amongst other things:
- a clear schedule of works, fees and other costs against which progress and expenditure can be monitored; and
- a clear basis in the form of a proposed schedule upon which grant is paid against progress made in relation to outputs and costs incurred.
- the inclusion of a GBSLEP representative as an observer on the PCLP Board, together with 2 BCC senior officers;
- the establishment of an officer group comprising PCLP, BCC and GBSLEP representatives that would meet ahead of the PCLP Board meetings to review issues and progress
- monthly reporting of financial and works progress to GBSLEP against targets, along with detailed quarterly reports on financial and physical progress, together with risk management. The monthly reporting should include a joint GBSLEP / BCC meeting held immediately following the monthly PCLP Board meeting;
- the appointment of an independent advisor to review costs, financial and physical progress and to validate interim claims for EZ payment; and
- an audit on final completion of Phase 2 and interim evaluation of performance.

4 Options considered and Recommended Proposal

- 4.1 The Paradise development remains a strategically important project for the city and the wider GBSLEP area. Both BCC and the GBSLEP have reviewed a number of options concerning the scheme, including curtailment of the scope. The independent business case review, however, shows a clear benefit to the City in taking this forward and financially it will deliver income receipts for use on the wider GBSLEP investment programme.

5 Consultation

Internal

- 5.1 The Leader of Birmingham City Council has been consulted on the contents of the report and both the leader and deputy leader have been fully briefed as part of their GBSLEP Board duties. Members of Audit Committee have been fully briefed on the development progress. Officers from Corporate Procurement, City Finance and Legal Services have been involved in the preparation of this report.

External

- 5.2 Members of the GBSLEP Board and have been instrumental in bringing forward the content of this report.

6 Risk Management

- 6.1 Updated risk registers have been provided as part of the full business case and a number of measures are in the process of being implemented to improve and ensure that there is increased monitoring of the project and its funding.

7 Compliance Issues:

7.1 How are the recommended decisions consistent with the City Council's priorities, plans and strategies?

- 7.1.1 The Paradise development supports the Council's Business Plan and Budget 2018+, specifically the priority for making Birmingham a great city to live in. In addition it promotes transformational change in the City Centre in line with the Big City Plan and Birmingham Development Plan.
- 7.1.2 The development of Paradise forms part of the GBSLEP (Greater Birmingham and Solihull Local Enterprise Partnership) EZ Investment Plan 2014 and supports the Birmingham Connected five core objectives.

7.2 Legal Implications

- 7.2.1 Investment in economic development is made pursuant to the general power of competence contained in Section 1 of the Localism Act 2011. External legal advice has been sought and received as part of this review that as proposed the development will not breach European State Aid rules. Sufficient assurances have been received in this respect.
- 7.2.2 This is in part based on the financial case and the sharing of excess developer profits over the normal hurdle rate and in part by the fact that the funding relates to infrastructure and does not benefit any commercial enterprise. There is no effective subsidisation from the infrastructure payments that could, potentially, distort competition by favouring a private enterprise. No public body will be subsidised relative to private enterprise in the provision of services.

7.3 Financial Implications

- 7.3.1 The City Council is the delivery agent for the Paradise project. The Council undertakes prudential borrowing to cover the costs of the development and receives a grant from the GBSLEP to cover all borrowing costs. During the demolition and construction phases the Council no longer receives NNDR (national non-domestic rates) from the empty properties, but receives a payment of circa £0.468m in recompense from the developer during this period of risk. This de-risks the initial stages for the Council and provides comfort that there will be no additional call on the Council Tax payer as a result of the development phase.
- 7.3.2 Under Enterprise Zone legislation, all uplift in NNDR, over and above that level that existed prior to the development, is retained by the Local Enterprise

Partnership, GBSLEP and funds, in the first instance, the costs of the development and thereafter to fund their broader EZ Investment Programme.

- 7.3.3 The independent audit into the Paradise project to be commissioned by the Council acting in its capacity as Accountable Body jointly with the GBSLEP will be funded within the Enterprise Zone Investment Plan.

7.3.4 Paradise EZ Cost & Funding Statement

	Total £m	Phase 1 £m	Phase 2 £m	Phase 3 £m
Original EZ Award	87.790	37.685	28.007	22.098
Cost Movements	51.277	50.105	23.270	(22.098)
Revised EZ Award	139.067	87.790	51.277	0.000
Capitalised interest	21.742	10.944	10.798	0.000
BCC Borrowing Requirement	160.809	98.734	62.075	0.000
Interest Charges	65.367	32.504	32.863	0.000
Total EZ Cost	226.176	131.238	94.938	0.000
Funded By				
EZ Business Rates	(226.176)	(131.238)	(94.938)	0.000
Net Cost to BCC	0.000	0.000	0.000	0.000

7.4 Procurement Implications (if required)

- 7.4.1 This report does not contain changes to the existing approved construction and supplier contracts awarded under this project.

7.5 Human Resources Implications (if required)

- 7.5.1 There are no human resources implications from this report.

7.6 Public Sector Equality Duty

- 7.6.1 EINA reference 472209/2013 completed for project as a whole, included at Appendix 1.

8 Background Documents

- 8.1 Relevant Officer's file(s) on the matter, save for confidential documents
- 8.2 List of Appendices accompanying this Report (if any):

- Appendix 1 – Paradise Equality Analysis
- Appendix 2 – Paradise update presentation