

Cabinet (Resources) Panel

26 April 2023

Report title	i11 Building, 4-5 Victoria Square - Investing in the City's Offer	
Decision designation	RED	
Cabinet member with lead responsibility	Councillor Bhupinder Gakhal City Assets and Housing	
Key decision	Yes	
In forward plan	Yes	
Wards affected	St Peter's	
Accountable Director	Julia Nock, Deputy Director of Assets	
Originating service	City Assets	
Accountable employee	Julia Nock	Deputy Director of Assets
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Report to be/has been considered by	City Assets Leadership Team	(5 April 2023)
	Strategic Executive Board	11 April 2023

Recommendations for decision:

The Cabinet (Resources) Panel recommend that Council approve:

1. The creation of a capital budget for the refurbishment and fit out works of i11.
2. Delegate authority to Cabinet Member for Resources and Digital City and Cabinet Member for City Assets and Housing in consultation with the Director of Finance and Deputy Director of Assets to finalise the capital fit out works and associated budget.

The Cabinet (Resources) Panel is recommended to:

1. Approve subject to appropriate due diligence the Council entering into a 10 year Profit Share lease agreement with IWG (Regus) or IWG Franchise to let and fully manage the office space at building i11 as a dedicated Serviced Office location.
2. Delegate authority to the Cabinet Member for City Assets and Housing, in consultation with Deputy Director of Assets to approve the lease agreement and final Heads of Terms for the Profit Share Lease.

1.0 Purpose

- 1.1 To seek approval to enter into a 10 year lease with IWG or IWG Franchise on a profit sharing arrangement whereby the Council are to receive a share of the net profits following deduction of a platform fee and all outgoings, subject to further due diligence.
- 1.2 To seek approval for the report to be submitted to Council for approval of a capped capital investment of £XXXXXX to meet the fit out costs to convert the i11 building to the IWG 'Spaces' brand standard for dedicated Serviced Office occupancy.

2.0 Background

- 2.1 Situated adjacent to the Wolverhampton Bus Station and the Queens Building, the i11 development provides 9315 sq ft of ground floor accommodation currently let to Sainsbury Supermarkets (Convenience Store), West Midlands Passenger Trains Services and Unite and first floor offices comprising of 10,086 sq ft above, currently vacant.
- 2.2 Following the development of the i11 building by the Council, the Revenues and Benefits Service took occupation of the i11 first floor open plan office space during the refurbishment period of the Civic Centre (April 2015- May 2018).
- 2.3 The accommodation remains vacant, despite the building being marketed through Property Agent Knight Frank. The building is being marketed at a rent of circa £160,000 per annum (£16.50 psf). Whilst the i11 building is a prime asset in an excellent location, the quality of fit out to the 1st floor offices are in need of refurbishment to attract a corporate occupier of good covenant. The Council are currently losing the opportunity to recover service charges and Business Rates from a tenant. This equates to the Council forgoing an income of £279,000 per annum.
- 2.4 The global commercial office real estate market is undergoing a revolutionary change and a dynamic shift has been seen in demand for office space as a result of the changing work model. Global demand for office space has reduced with organisations operating a hybrid working model requiring less space.
- 2.5 Organisations need less office space, and as a result, are terminating long-term commercial office leases at an unprecedented rate, often replacing them with shorter-term agreements or new arrangements with flexible workspace providers such as IWG.
- 2.6 The Council therefore needs to respond positively and adapt its strategy to offer both potential corporate occupiers and local businesses that have the potential to grow, high quality office space on a more flexible basis to meet the change in demand for space and to meet their specific requirements.

3.0 Proposal

- 3.1 The proposal is to enter into a 10-year Profit Share lease agreement with IWG (Regus) to let and fully manage the 1st floor office space at building i11. IWG will build on their existing presence in the City Centre, using their premium 'Spaces' brand, to provide a differentiated offer alongside their brand Regus to capture demand for premium office and meeting space. This would become a showcase example for the City's regeneration

momentum, acting as a catalyst for further economic growth within the main commercial district and further private sector investment.

- 3.2 The Profit Share lease agreement is compliant with Section 123 of the Local Government Act and includes the Council receiving X% of net profits after a platform fee and all property and operational outgoings have been deducted (including utilities and repairs and maintenance). IWG will be responsible for paying the Business Rates charge irrelevant of occupancy levels.
- 3.3 The proposal assumes an ongoing occupancy rate of X% and due to the current occupancy levels of IWG's Salop Street offices (Regus) being X%, there is high confidence that this can be achieved and sustained throughout the 10 year lease.
- 3.4 A capital investment of £XXXXXX is required to complete a full refurbishment fit out of the building including office entrance, stairwell to 1st floor, office accommodation and facilities to the IWG 'Spaces' brand standard. The proposal is an opportunity to convert the capital investment into a revenue income, backed by IWG whom are a FTSE 250 global market leader.
- 3.5 It is intended for the fit-out works to be completed by IWG utilising their own design team whom are knowledgeable on the 'Spaces' brand specification and will prove cost effective in reducing timescales with the Council not needing to procure contractors and suppliers. The Council as part of its due diligence will consider whether such financial assistance is a subsidy before entering into the lease. This is reflected further within the Legal implications of the report.
- 3.6 The capital investment from the Council is capped at £XXXXXX, the risk of costs exceeding £XXXXXX will be carried by IWG and any saving against this forecast cost will mean a saving on the required investment by the Council. The Council will make payment to IWG based on evidenced expenditure. A detailed specification will be agreed and payment of the £XXXXXX will be made via tranches on IWG reaching agreed milestones within the fit-out programme. With IWG undertaking the works, the Council will not be subjected to comply with the PCR Procurement Regulations.
- 3.7 Further details on the organisation IWG and the proposal for the i11 building can be seen in Appendix 1 (excluded from Public Version of this report).

4.0 Need and Demand for Serviced Office Accommodation

- 4.1 IWG have provided evidence to demonstrate that on average 45 enquiries per month for office space in Wolverhampton City Centre are received. This proposal will provide a fully managed office service solution whilst boosting the local community with new jobs, encouraging new businesses into the City, benefitting local economic growth and thereby supporting the Wolverhampton Pound. IWG already has experience of partnering successfully with 25 local authorities on similar projects.
- 4.2 i11 is expected to become highly popular in Wolverhampton due to its aspirational 'Spaces' brand appeal and strong transport links within Wolverhampton interchange. IWG would be building on an already successful service office accommodation within the City Centre at 84 Salop Street which is running at over 90% continued occupancy rates.

- 4.3 The proposal increases the variety of office space available to Wolverhampton businesses and residents. IWG's Spaces is both flexible and aspirational, broadening the target market to smaller companies and high growth companies and would assist in meeting the Council's digital co-working space objectives with easy in/out flexible basis of occupation attractive to new start-up business.
- 4.4 The i11 building branded as 'Spaces' would provide a conveniently located solution for those local business that have outgrown using the space available in Ignite located opposite the i11 building to expand.
- 4.5 The Council would encourage IWG to strongly promote the building with the 'Spaces' branding being very prominently displayed and with appropriate illuminated external signage on the building subject to meeting planning requirements.

5.0 Benefits of the Proposal

- 5.1 The proposal contained within this report would provide the following benefits:
- Spaces at i11 will supply high quality office space for up to 200 jobs into the emerging Wolverhampton Commercial District
 - Additional retail and transport spend of up to £600,000 per annum (assuming average annual spend of £3,000 per worker)
 - Increases the variety of office space available to Wolverhampton businesses and residents. IWG's Spaces is both flexible and aspirational, broadening the target market to smaller companies and high growth companies.
 - Validates the Council's investment into the transport Interchange, which provides crucial connectivity to facilitate further growth
 - The proposal is an opportunity to convert the fit-out capital investment into a significant revenue income within a short period of time
 - IWG would be building on an already successful serviced office accommodation within the City Centre at 84 Salop Street which is running at over 90% continued occupancy rates.
 - IWG are already receiving enquiries from customers who want to be closer to the train/bus station or generally in a more central location
 - Captive market already in place to get some early occupation at i11, aiming to open on day one with as high occupancy as possible

6.0 Supporting Delivery of the Strategic Asset Plan

- 6.1 Corporate Landlord have developed a Strategic Asset Plan that was completed and approved by Cabinet on 17 October 2018. This provides the structure and management of the Council's land and property portfolio over following five years, to 2023, and incorporates the Our Assets principle. The plan is structured into three parts:
- Asset Management Policy
 - Asset Management Strategy
 - Asset Management Action Plan
- 6.2 The Asset Management Policy establishes a clear mission with supporting principles for the management of land and buildings, ensuring it is fit for purpose and benefits the people of the City of Wolverhampton and to use land and buildings following rationalisation and disposal of land and buildings, that will enable a financial return to

stimulate development and growth, support and encourage local businesses and promote joint-working.

- 6.3 The proposed Profit Share lease with IWG or IWG Franchise for i11 supports the policy as outlined and in particular delivery of items A1, A9, B5 and B6 of the Action Plan.

7.0 Evaluation of alternative options

- 7.1 Option 1: The Council could continue to market the vacant office accommodation via specialist Property Agents and agree to invest in refurbishing the entrance, stairwell and office space in an attempt to attract a new occupier (cost to be confirmed). However, given that it has stood empty since the vacation of the Revenues and Benefits Service in 2018 with no replacement tenant having been secured, there is perhaps an improved likelihood of completing a letting in current market conditions after significant capital expenditure to improve the quality of fit out. However, such investment would remain very speculative and not guarantee a deal being agreed in the short term. In addition, a corporate occupier would likely expect other incentives including rent free capital contribution and a likely lease break option to sign up to a 10 year lease or longer term.
- 7.2 Option 2: An alternative option would be for the Council to sell the freehold interest however this is considered a prime investment asset and at present, with only the ground floor fully let and the upper parts remaining empty, this would impact negatively on the capital value achievable and it is therefore unlikely a sale would provide at this time would provide an attractive return on the Council's investment This is not therefore an option that could be recommended at this time.
- 7.3 Option 3: To leave the first floor office accommodation in its existing and relatively poor condition and continue to market via specialist Property Agents. This option would however be unlikely to generate a letting in the short to medium term given the current market conditions and the condition of the accommodation is likely to deteriorate further and become less attractive to potential tenants whilst it remains empty.

8.0 Reasons for decision(s)

- 8.1 If the Council were to do nothing, it is highly likely that in the short to medium term, it will continue to miss out on generating a revenue return from the offices on the first floor of building i11, plus the condition of the accommodation will likely deteriorate whilst vacant thereby becoming less attractive to a potential new occupier.
- 8.2 Whilst the Council could look to improve the accommodation by refurbishing, this could prove a very speculative investment and not necessarily result in a satisfactory letting being achieved given current market conditions. In addition, it would be necessary to offer incentives such as a rent-free period, capital contributions and flexible lease terms (including break provisions prior to lease expiry) to encourage a corporate occupier to agree a longer-term commitment.

- 8.3 It is considered the recommendation for the Council to invest £XXXXXXX to fit out the vacant office accommodation on the first floor of building i11, to meet the requirements of IWG's 'Spaces' branding, combined with entering into a 10 year profit sharing lease arrangement would increase the Council's likelihood of receiving a return on this required capital investment. Based on an assumption of X% occupancy being achieved and for occupancy to be maintained at this level until year 10, this would result in a net estimated rental income, after borrowing costs to the Council of approximately £XXXXXXX over the 10 year lease period. This return would be variable depending on occupancy and the level of costs incurred.
- 8.4 It should however be noted that this return is not guaranteed and there remains a risk that should an occupancy not achieve this level, the return would be lower. Similarly, should occupancy levels of X% be reached or exceeded the income stream to the Council would increase over the lease term. The level of operating costs could also impact the overall return to the Council and the impact of this will be further reviewed as part of the Council's due diligence.
- 8.5 IWG are highly confident of reaching X% occupancy by year three and maintaining occupancy at that level based on their own experience of letting another Wolverhampton City Centre office building of 8,655 sq ft similarly branded at the Regus centre on Salop Street which has proved highly successful and sustains a 90% occupancy level.
- 8.6 The Council do not have the resource or in-house expertise to manage the building ourselves as a dedicated Serviced Office offer.
- 8.7 Officers have met with IWG and have inspected their Salop Street Serviced Offices and Birmingham Mailbox 'Spaces' offer to assess the quality of fit out and offer available.
- 8.8 Entering into a Profit Share lease agreement with IWG or IWG Franchise for 10 years will return the asset to beneficial use, generate income, create jobs, help support existing local businesses as well as encouraging new businesses into the City with the provision of flexible, fully serviced and high-quality office accommodation.

9.0 Financial implications

- 9.1 This report seeks approval of a capital budget of £XXXXXXX funded through Council borrowing at an estimated annual cost of £XXXXXXX per annum, over the 10 years of the lease.
- 9.2 The proposed lease terms would generate a revenue income for the Council based on an X% profit sharing arrangement with IWG or IWG Franchise. The profit share terms to be included in the lease are that the Council and IWG split the income, after costs on an XX:XX basis, with the Council taking an XX% share. As demonstrated in the table below operating costs and the IWG "platform fee" are deducted from revenue before the profit share calculation is made. (Table excluded from Public version of this report)
- 9.3 The capital investment from the Council is capped at £XXXXXXX the risk of costs exceeding £XXXXXXX will be carried by IWG and any saving against this forecast cost will

mean a saving on the required investment by the Council and would therefore reduce the amount the Council will be required to borrow. The Council will make payment to IWG based on evidenced expenditure, as the key milestones are reached as approved by the Council's monitoring surveyor which will ensure the building is fitted out to the agreed specification and to the 'Spaces' brand standard.

- 9.4 It should be noted that the Council will remain liable for the operational costs of the building if no rental income being received, (utilities, compliance, servicing and repairs and maintenance), however the platform fee is based upon X% of rental income and therefore would not be payable were the building to remain unoccupied. In addition, IWG will be responsible for the payment of business rates from the outset of the agreement. At the time of this report as mentioned above the office space is unlet therefore no income is being received and the Council is responsible for holding costs.

Table 1 - Forecast Income and expenditure projections (Excluded from Public version of this report)

Table 2 - Forecast annual cost of borrowing (Excluded from Public version of this report)

- 9.5 The figures are projections and there are risks to the Council should rental levels not be achieved or if operational costs increase. Business rates of approximately £57,000 per annum will also be received by the Council, IWG will pay the full business rates for the property regardless of occupancy levels. As detailed in paragraph 2.3, the accommodation is currently empty and the Council is losing the opportunity to recover service charges and business rates totalling around £270,000 per year (the council is responsible for the payment of business rates).
- 9.6 The data provided in the table 2 demonstrates that in year 1 at an average occupancy of X%, there is a net loss to the council, after borrowing costs (excluding the income from business rates), it is estimated that an occupancy level of approximately X% is required to cover the cost of borrowing over the 10 years of the lease. However projected occupancy levels are X%, if this is reached the costs of borrowing are covered and a surplus income is generated for the council. The surplus income could therefore be used to repay the borrowing earlier or to contribute to the Council's Medium Term Financial Strategy, currently no income is assumed in existing revenue budgets. The worst case scenario, which is unlikely would be that the accommodation remains vacant, in this case the council would not receive any profit share towards the cost of borrowing, however, the council would still receive the business rates of around £57,000 which are currently being paid by the Council.

[HM/21042023/U]

10.0 Legal implications

- 10.1 The Council has a general power of competence to enter into the proposed arrangements by virtue of section 1, of the Localism Act 2011, which provides that a local authority has power to do anything that individuals generally may do. This power is both

wide ranging and discretionary and enables the council to do anything that it considers is likely to promote or improve the environmental, economic and social well-being of its administrative area. In exercising its general power of competence, the council is still subject to public law requirements, thus must act reasonably, fairly, rationally and in accordance with the law.

- 10.2 Under section 123 of the Local Government Act 1972, the council has a duty to achieve best value from the disposal of its land and property. The negotiated terms of the lease must represent value for money.
- 10.3 The council must be satisfied that its proposal does not contravene the Public Contract Regulations 2015 (PCR), and its own Contract Procedure Rules. The disposal of property by way of the lease is essentially a property related agreement and the PCR does not apply to contracts for interests in land.
- 10.4 Should the Council choose to carry out the fit-out works this will require competitive tendering because the Council is legally required to advertise public contract opportunities. Where the estimated value of a contract exceeds the relevant financial threshold, the procurement is subject to the full procedural requirements of Part 2 of the (PCR). The current threshold for works is £5,336,937. Where the contract opportunity is below threshold but exceeds £25,000 there is a requirement to publish the opportunity on Contracts Finder. This is also a requirement under the Council's own Contract Procedure Rules.
- 10.5 Should the fit-out works be completed by IWG, with the Council contributing £X towards the fit-out costs, the Council must consider whether such financial assistance is a subsidy for the purposes of the Subsidy Control Act 2022 (the Act), such that it confers a specific economic advantage on one or more enterprises and is capable of having an effect on competition or investment in the UK or trade and investment between the UK and another country.
- 10.6 Where any financial assistance is given directly or indirectly by a public body which confers an economic advantage and is capable of having an effect on competition and investment such financial assistance will be a subsidy and will require assessment against the Subsidy Control Principles set out in the Act. This would be a self-assessment carried out by the council.
- 10.7 The Council shall seek external advice with regard to subsidy control as part of its due diligence. The proposal cannot proceed if it is in breach of subsidy control requirements.
[PG 19/2023]

11.0 Equalities implications

- 11.1 All development plans will consider and meet the needs of all people within the local community and an all-inclusive approach will be taken by Wolverhampton City Council.

12.0 Schedule of background papers

12.1 Strategic Asset Plan 2018-2023 – Report to Cabinet on 17 October 2018 including:

Asset Management Policy 2018-2023

Asset Management Strategy 2018-2023

Asset Management Action Plan

13.0 Appendices

13.1 Appendix 1: IWG Brochure and IWG Proposal for i11 (Excluded from Public version of this report)