



Haringey Council

Report for:	Decision by the Leader - 10 April 2014	Item Number:	
Title:	Acquisition of Munro Works		
Report Authorised by:	Lyn Garner, Director of Planning, Regeneration & Development		
Lead Officer:	Roy James, Senior Valuer, Asset Management: 0208 489 2368, roy.james@haringey.gov.uk		
Ward(s) affected: Bounds Green	Report for Key/Non Key Decisions:		

1. Describe the Issue Under Consideration

1.1 This report addresses the exercising of a contractual option to purchase the freehold interest of Munro Works, a medium-sized industrial estate at Cline Road, N11 2LZ.

1.2 Munro Works is part of the Council's Commercial Property portfolio, which was reviewed recently by DTZ in their report 'Investment Portfolio'.

- DTZ identified Munro Works as:
- Having significant voids;
- Being a weak Performer;
- Having a significant cost liability; and,
- Being inhibited by tenure arrangements.

1.3 This report addresses at Paragraph 4 below the range of options for addressing this loss-making commercial asset:



Haringey Council

- Pursuing the Option to Purchase that is included in the head lease;
- Continuing to Manage the Asset without changing the lease structure;
- Restructuring the letting arrangements at the estate so that the estate may be let to one tenant in accordance with the lease terms; and,
- Surrendering the Existing lease and Renegotiating Terms under a New lease Structure.

1.4 The Council holds a long leasehold interest in the property. The lease has onerous conditions for the Council, which mean that this is an on-going loss making asset for the Council. However, there is an option to purchase within the lease, which would enable the Council to purchase the freehold interest, bringing the Council's long leasehold interest to an end.

1.5 The freehold interest in the site was acquired by Carmel Southend Ltd on 8 May 2001 following the sale of the site at auction by the London Residuary Board [LRB].

1.6 The onerous clauses within the lease are those that forbid the Council from sub-letting individual units, the full repairing liability of the whole estate, and the rent review provisions. The actual lease terms are provided at Appendix C but the main highlights of those clauses are given below.

1.7 The lease restricts the occupation of the site to that of a single letting of the whole of the demised premises. This is quite normal with regard to single industrial units or shops but completely inappropriate for a whole estate. The deed pack shows that this restriction was never exercised under the original lease with the GLC, as there were several sub-let units prior to a fire that occurred in 2005.

1.8 The Council began advertising individual units following the refurbishment of the building and the completion of the works to the roof in 2011. Carmel Southend Ltd has adopted a much more aggressive approach to sub-letting. They have refused to grant permission to the Council to sublet individual units without varying the terms of the lease to be even more onerous to the Council than they are at present.

1.9 Legal advice is that the previous breaches that were tolerated by the GLC and the LRB do not set a precedent for further sub-letting, as this would amount to further new breaches of the lease and could lead to forfeiture of the lease and an associated claim against the Council.

1.10 The head rent is currently £105k p.a., with a present income of around £36.5k p.a. with regard to two units that have been sub-let for many years. Those two units are holding over on expired leases, which have not been renewed given the effect that might have with regard to alleged breaches of the alienation clauses within the lease, as set out below. Therefore, there are three vacant units which can not be let under the present terms of the lease.



Haringey Council

- 1.11 The rent review pattern is five yearly, upwardly only to full market value. Thus, the Council has very little opportunity to recoup even its management costs let alone make a profit.
- 1.12 This financial situation is exacerbated by the rental voids, caused by not being able to sub-let individual units currently without breaching the terms of the lease, and further by the Council's repairing liability for the whole estate, given that the Council is only able at present to pass on a part of its repairing liability. This lease would arguably be a loss-making asset for the Council even if the estate were fully-let.
- 1.13 The option to purchase was triggered on October 27 2013 by the required six months' notice period, which expires on 28 April 2014.

2. Cabinet Member Introduction

2.1 The purchase of the freehold interest in this property will allow the Council to exit an historic onerous lease and to support economic development within the Borough.

3. Recommendations

- 3.1 To note the current onerous leasing arrangement of Munro Works and ongoing annual cost to the Council.
- 3.2 To note the opportunity to reduce the financial liability of Munro Works to the Council via the purchase of the freehold interest of the estate in accordance with the option to purchase contained within the head leasehold interest.
- 3.3 That approval is granted for the Council to purchase the freehold interest in the Munro Works as outlined in Option 1 below (shown edged red on the plan attached) for a consideration not exceeding the purchase price detailed in the exempt section, Part B, of this report with delegated authority for the Section 151 Officer and the Director of Regeneration, Planning and Development Reduction to agree the final terms of the acquisition, after consultation with the Cabinet Member for Finance, Employment and Carbon Reduction.
- 3.4 To agree that the addition of the capital cost of the purchase and any associated costs of refurbishment, as outlined in this report, be added to the Council's capital programme.
- 3.5 To note that the funding for the purchase cost is to be met from the future rental income to be generated from commercial letting of the site.

4. Alternative Options Considered

- 4.1 Asset Management has approached the freeholders in the past with regard to relaxing the sub-letting and rent review provisions within the head-lease for Munro Works so that vacant units might be let to applicants for commercial tenancies. Further information on the options appraised is included in part B of this report.



4.2 Aside from the financial business case for options, other non economic factors and benefits have been considered such as the potential to support regeneration.

4.3 Option 1 - Pursuing the Option to Purchase that is included in the Head Lease.

4.3.1 The option to purchase the freehold interest is perceived as the only viable wayforward in view of the financial outcomes of the other options addressed below. Financial modelling indicates that this is a financially better option for the Council than either continuing to manage and maintain the current situation [Option 2 below] or to make radical changes in tenant structure in order to comply with existing lease terms [Option 3 below] or to in order to move forward with a modern lease structure that benefits both the freeholders and the Council [Option 4].

4.3.2 The price is to be the current open market value of the premises.

4.3.3 The option to purchase is exercised by serving six months' notice on the owner of the freehold interest, which was done on 28 October 2013, subject to Cabinet approval and subject to contract. Therefore, the effective date of the expiry of the notice is 28 April 2014.

4.3.4 There is only one opportunity within the terms of the lease to exercise this option.

4.3.5 The Council undertook a procurement exercise with regard to the external valuation of the site and engaged Lambert Smith Hampton to provide that valuation. Please refer to the exempt section, Part B, for the main findings within the valuation report and the financial implications of this option.

4.3.6 The landlords have engaged Knight Frank to carry out a valuation on their behalf. The lease sets out the valuation may be referred to the RICS in the event that the respective valuers are not able to agree the purchase price of the site.

4.4 Option 2 - Continuing to Manage the Asset without Changing the Lease Structure.

4.4.1 The Council may decide not to pursue the opportunity to exercise the option to purchase the freehold interest of this site that is presented to the Council within the Head Lease.

4.4.2 The Council would continue to suffer an annual net loss in this situation, which would worsen for the remainder of the lease, and be exacerbated at the end of the lease in the likely event that a schedule of dilapidations would be served on the Council at that time.

4.4.3 The vacant units were taken out of the Rating List following the fire in 2008. Those units were brought back into the Rating List in September 2013, albeit with exemption for six months from NNDR, as they were vacant. Those



exemptions expired in March 2014 so full rates are now payable by the Council on the empty units at Munro Works.

4.4.4 Further information on this option is included in part B of this report.

4.5 Option 3 – Restructuring the Letting Arrangements at the Estate so that the Estate may be let to one tenant in accordance with the Lease Terms

- 4.5.1 This option would involve identifying an industrial tenant that is in the market for a large amount of commercial space, as the whole of the estate is approximately 30,000 sq.ft., which is considered to be highly unlikely in the present commercial market.
- 4.5.2 The narrow access to the estate is a known deterrent against industrial users requiring access for large distribution vehicles.
- 4.5.3 The rental income derived from letting the estate as a whole would be less than achieved as individual units, if such a tenant were to be found.
- 4.5.4 It is highly likely that a significant rent free period would be expected by such a tenant in order to address the considerable fitting out costs that would ensue from a re-organisation of the estate.
- 4.5.6 There are currently two units at the estate that are let. The leases or those existing leases would have to be terminated, for which compensation would have to be paid to the tenants. It is highly likely that the current tenants would expect to be found alternative premises and for the Council to pay their relocation costs in these circumstances
- 4.5.7 Therefore, this option is considered to be very high-risk, as it would involve the loss of the existing income of £36.5k p.a., with no guarantee that a potential tenant for the whole premises would be achieved, and if there was such a tenant that a considerable rent-free period would have to be given to induce the tenant to take over the responsibilities of the whole estate.
- 4.5.8 There is an additional risk factor which is that the Council's risk with regard to voids, rent arrears and lease default is increased substantially where there is only one tenant, whereas it is spread in situations where there are many individual tenants.

4.6 Option 4 – Surrendering the Existing lease and Renegotiating Terms under a New lease Structure.

- 4.6.1 Attempts to date to renegotiate the terms of the existing lease have been less than successful to date, which has resulted in there being little confidence that this option would benefit the Council.
- 4.6.2 The landlords have offered to relax the letting clause and the user clause in exchange for the removal of the option to purchase and an adjustment to the rent review clause to reflect these changes.
- 4.6.3 This would not lead to a positive asset, although the losses might well not be as great as they are currently.



Haringey Council

4.6.4 The landlords are likely to expect to receive a capital sum for the surrender of the existing lease, i.e. they would expect to be compensated on the basis of the lost rental income for the remainder of the lease but discounted to take account of the receipt of an immediate capital sum rather than an annual rental income.

4.6.5 There would probably be a further claim for dilapidations in addition to the surrender of the lease.

4.6.6 This option is considered in further detail within Part B to this report. However, it is highly likely that the combined figure for the surrender value plus dilapidations would be very similar to the purchase price under Option 1 but with the outcome that the Council.

4.6.7 In view of these factors, this option is less attractive than exercising the option to purchase.

5. Background information

5.1 The Council's long leasehold interest in Munro Works began on 9 December 1983, after the GLC purchased the freehold interest as part of a joint venture with the Council with the objective of generating and protecting local employment.

5.2 The GLC granted a 99 year full repairing and insuring [FRI] lease to the Council from 9 Dec 1983. The original firm on the site was R W Munro Ltd., an engineering firm. The original firm dates from 1783 and made parts for the Babbage computer and Scott's Antarctic expeditions.

5.3 There was a clear interest for the LBH to attempt to protect and retain those engineering skills in the Borough. This probably accounts for the LBH engaging in onerous lease terms with the GLC, which include a rent review pattern that is five yearly, and upwardly only to full market value, i.e. there is effectively no rent-sharing between the parties. Also, it is likely that the Council entered into this site management arrangement at nil cost to the GLC in consideration for the GLC injecting the financial capital into the original purchase of the site.

5.4 The site comprises two large industrial/warehouse units and three small factory units forming part of a medium-sized industrial estate, the estimated net internal area of which is approximately 29,500 square feet.

5.5 The estate is accessed via an access road known as Munro Drive, which is part of the demised land and premises. The site is shown coloured pink on the attached plan at Appendix A and photographs are included at Appendix B.

5.6 A fire devastated most of the estate on 24 March 2005.

5.7 Two units are let at the estate: those tenants having been in occupation since before the purchase of the freehold interest by Carmel Southend Ltd.



5.8 Repairs to the roof and the windows were carried out enabling the vacant units to be marketed for let in 2011. However, the onerous lease terms at the source of this report has stymied any potential lettings at Munro Works.

6. Comments of the Chief Finance Officer and Financial Implications

6.1 The current position is that the Council pay rent of £105k per annum for the site and due to the lease condition is only currently achieving rental income of £36.5k per annum, leading to a **net deficit of £68.5k** per annum. This is before taking into account any costs of management, repairs and maintenance.

6.2 The restrictions on the lease are likely to prevent this asset generating further income, which means the asset will continue to lose money for the Council. It is estimated that the potential income generation of the asset could be between £125k per annum and £150k per annum at 85% occupancy if the Council had the freedom to determine the best letting pattern and terms.

6.3 Modelling of various scenarios including the costs of buying out the lease based on the unexpired portion of the lease has been undertaken, the details of which are provided within Part B to this report.

6.4 That modelling demonstrates that provided demand is sufficient to achieve a minimum of 70% occupancy, it would be financially advantageous to the Council to buy out the lease so as to fully control the site.

6.5 The options to locate one tenant to take the whole of the letting and the surrender and renewal of the lease are not modelled, as we do not have sufficient information to do so. However, these options have been considered on the basis of estimated figures within Paragraph 4 above.

6.6 The Council has recently undertaken the refurbishment of this estate after a fire some years ago. The total cost of the refurbishment was £505k, with £161k paid from insurance receipts with regard to building works, and an additional £37k with regard to rent loss. Although these are sunk costs and should not necessarily have a bearing on the future site options, they are pertinent for the consideration of residual value of the asset and for the decision process overall.

7. Head of Legal Services and legal implications

7.1 The Council has a lease of the property known as Munro Works for a term of 99 years from 9 December 1983. The lease contains an option in favour of the Council to acquire the freehold interest. The Council has already served notice to exercise that option and is to acquire the freehold for the same purpose for which the leasehold interest is presently held.

7.2 The Council has the power under section 120 of the Local Government Act 1972 to purchase the freehold interest for the purposes of any of its function or the



benefit, improvement or development of its area even if that land is not immediately required for that purpose.

8. Equalities and Community Cohesion Comments

Not Applicable to this report.

9. Head of Procurement Comments

Not Applicable to this report.

10. Policy Implication

Not Applicable to this report.

11. Reasons for Decision

11.1 The Munro Works site is an onerous asset that in its current form is costing the Council £68,5000 p.a., potentially to lease expiry in 68 years, due to the restrictive covenants on sub-letting contained within the head lease to the Council.

11.2 Financial modelling confirms that this option represents a financially better option than any of the three other options considered within this report and Part B to this report.

11.3 It is expected that the site would remain a financial liability if the option to purchase is not pursued, as even with improved lease terms under a new lease, negotiations for which may take years to reach settlement, this long-leasehold interest will always remain as a financial liability to the Council.

11.4 Therefore, officers have given notice of the option to purchase the freehold interest which crystallises the Council's position.

11.5 Market testing indicates that there is strong demand for units of this type and that a properly managed estate could yield a surplus of up to £150,000 per annum to repay financing costs of the purchase.

11.6 The availability of these units could possibly support the decant required to assist in the Tottenham regeneration.

11.7 A review of all properties within the Corporte portfolio is nearing completion, and this asset, Munro Works, is regarded as the only remaining truly onerous lease.

11.8 The opportunity to take action is time-driven, as a decision on whether the option to purchase is to be exercised has to be communicated to the freeholders by the end of April 2014.

12. Use of Appendices

Appendix A: Plan of the Munro Works site

Appendix B: Lease Terms

13. Local Government (Access to Information) Act 1985



Haringey Council

Appendix C: Local Government (Access to Information) Act 1985 – Exempt

COUNCILLOR CLAIRE KOBER

.....

DATE

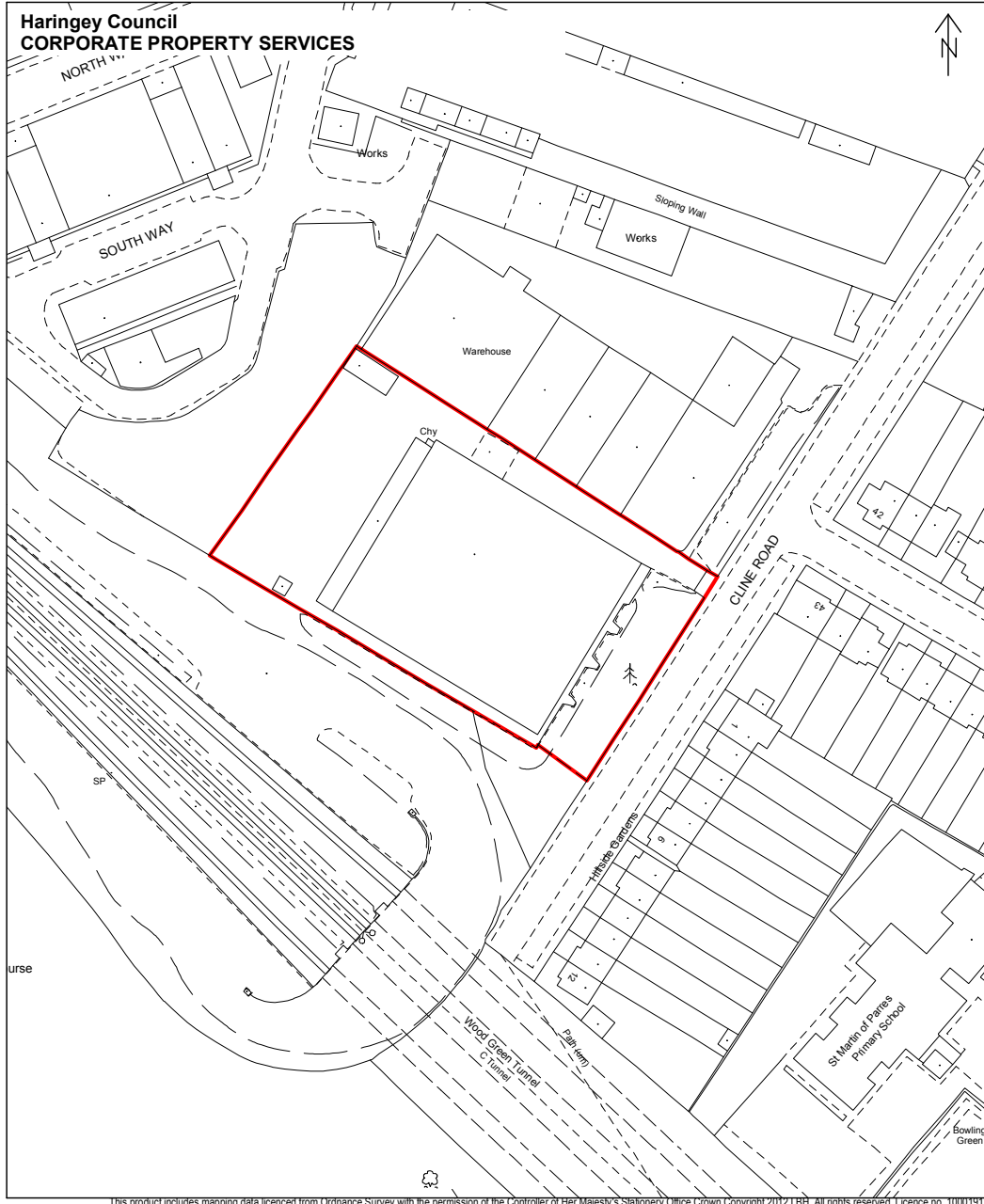
.....



Haringey Council



Haringey Council



This product includes mapping data licenced from Ordnance Survey with the permission of the Controller of Her Majesty's Stationary Office Crown Copyright 2012 LBR. All rights reserved. Licence no. 100019195

**Munro Works
Clive Road
LONDON
N11**

CPM No. 0915

Overlay : *Corporate - Commercial*

Plan produced by Janice Dabinett on 16/10/2012

Deed packet :

LR title no. :

Site Area (hectares) :

Scale 1:1250

Drawing No. BVES A4 1741c



Lease Terms

Alienation Clauses

The alienation provisions are contained within Paragraph 10 et seq of the Lease:

- (10) Not to assign any part (as opposed to the whole) of the Demised Premises
- (11) Not to assign the whole of the Demised Premises without the consent in writing of the Director
- (12) Not to underlet the whole of the Demised Premises without the consent in writing of the Director
- (14) Not (save by way of permitted assignment or underletting as aforesaid) to part with or share possession or occupation of the Demised Premises or any part thereof.

The Permitted Use

Use within Class III of the Schedule to the Town and Country Planning (Use Classes) Order 1972, which has been varied by a subsequent Deed of Variation dated 15 June 1992, which permits the premises to be used within class B1 of the 1987 Use Classes Order.

Sub-clause (25) on page 13 of the lease prohibits the use of the premises for anything other than the permitted use.

The Option to Purchase the Freehold Interest

The lease contains an option to purchase at Paragraph 9 of the lease. The references given below identify the most significant clauses to the lease:

9 (a) IF the Tenant shall desire to purchase the reversion in fee simple of the premises hereby demised and shall not less than twelve months before the expiration of the Term give to the Landlord six months' notice in writing of such desire then the Landlord hereby covenants that he will upon the expiration of such notice ('the purchase date') and upon payment of the price hereinafter agreed ('the purchase price') together with all arrears of rent up to the expiration of such notice and interest on the said purchase price at the rate specified in Clause 4 (4) hereof from the purchase date until the actual payment thereof transfer the Demised Premises to the Tenant in fee simple but until the purchase price together with interest as aforesaid and the said arrears of rent shall have actually been paid this lease shall continue in full force and the Tenant shall not be released from any of his obligations hereunder



Haringey Council

- (b) (i) The purchase price shall be whichever is the greater of either the current open market value of the Demised Premises at the time of the purchase date or Three hundred and twenty-five thousand pounds (£325,000)
- (ii) Any agreement between the Landlord and the Tenant as to the current open market value of the freehold of the Demised Premises shall be writing by both parties
- (iii) The current open market value of the freehold of the Demised Premises shall be the price which such premises with vacant possession might reasonably be expected to fetch on the open market at the purchase date as between a willing vendor and a willing purchaser such price to be determined in case of dispute by an independent valuer appointed the parties.