5.2 LEASE AGREEMENT FOR CIVIC ADMINISTRATION BUILDING

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CONFIDENTIAL

Reason for considering this matter with confidential	Grounds under the Local Government Official Information and Meetings Act 1987
Section 7(2)(h) - the withholding of the information is necessary to enable [the Council] to carry out, without prejudice or disadvantage, commercial activities	Section 48(1)(a)(i) - the public conduct of the relevant part of the proceedings of the meeting would be likely to result in the disclosure of information for which good reason for withholding would exist under section 7
Section 7(2)(i) - the withholding of the information is necessary to enable [the Council] to carry on, without prejudice or disadvantage, negotiations (including commercial and industrial negotiations)	Section 48(1)(a)(i) - the public conduct of the relevant part of the proceedings of the meeting would be likely to result in the disclosure of information for which good reason for withholding would exist under section 7

PURPOSE

To seek approval for the:

- disposal of the property located at 67 Horomatangi Street; and
- taking of a lease for new office premises in a building to be constructed at 67 Horomatangi Street.

To delegate authority to the Mayor and Chief Executive to sign:

- an updated Memorandum of Terms reflecting the key commercial terms set out in this paper;
- a Sale & Purchase agreement to dispose of 67 Horomatangi Street;
- an Agreement to Lease for new offices at 67 Horomatangi Street; and
- any other documents required to give effect to the above transaction.

EXECUTIVE SUMMARY

At the Council meeting 14 December 2021 Elected Members instructed officers to enter into negotiations with Te Whare Hono o Tūwharetoa Limited Partnership to reach agreement on a new office space for Council to lease. These negotiations have taken place and it is proposed that Te Whare Hono o Tūwharetoa Limited Partnership (TWHT) will purchase the Council owned site at 67 Horomatangi St for an agreed value ($3m), then develop and lease the building back to Council [redacted]

The parties have agreed the building design, specification, and a set of key commercial terms in the form of a non-binding Memorandum of Terms. Of specific relevance is that the building structure is being designed to Importance Level 4 (IL4) as requested by Council. The next step in the process is to convert the agreed Memorandum of Terms into a binding Agreement to Lease (ATL). The ATL documents detail the obligations and processes to achieve a completed building and this point in the process is not an opportunity to re-negotiate the agreed key terms.

[redacted]

It is recommended that delegated authority is granted to the Mayor and Chief Executive to enter into the transaction based on the agreed key commercial terms.

Finally, we note the value of the relationship with Ngāti Tūwharetoa. Both parties seek to create a closer and enduring relationship and partnering in this development project is symbolic of that aspiration.

RECOMMENDATION(S)

That Council:

1. Revokes resolution TDC202112/C01; and

2. Approves:
   a. the disposal of the property located at 67 Horomatangi Street to Te Whare Hono o Tūwharetoa Limited Partnership (TWHT) for $3million dollars (plus GST if any), with settlement to follow satisfaction or waiver of the following conditions:
      - Finalising the Agreement to Lease and Deed of Lease
      - TWHT obtaining its board approval;
      - Council obtaining all necessary approvals and completing any consultation or disclosure process in relation to the agreement, and
      - Practical Completion of the building or lease commencement by Council (whichever the latter)

   b. subject to settlement of the sale of the land at 67 Horomatangi Street, agrees to take a lease of new office premises from TWHT in a building to be constructed by TWHT on the land at 67 Horomatangi Street, on terms and conditions that are materially consistent with the below:

   c. Key Commercial Terms:
      [redacted]
      - Net Lettable Area: Estimated at 3,030.60m2.
      [redacted]
      - Fleet Parking: 39 covered and secure carparks with EV charging stations at $25 plus GST per carpark per week.
      - Total Annual Net Rent: (including fleet carpark) and based on the above Estimated Net Lettable Area: $1,323,552 plus GST.
      - Annual rent increases: Stepped annual increases. Annual adjustment to CPI [redacted]
      - Building structure: Steel frame, designed to achieve Importance Level 4.
      - Practical Completion: Estimated second quarter 2024; and

3. Delegates authority to the Mayor and Chief Executive to sign, in accordance with these terms:
   - an updated Memorandum of Terms reflecting the key commercial terms set out in this paper;
   - a Sale & Purchase agreement to dispose of 67 Horomatangi Street to TWHT;
   - an Agreement to Lease (which includes the Deed of Lease) for new offices at 67 Horomatangi Street; and
   - any other documents required to give effect to the above transactions; and

4. Notes the intention to share information regarding the finalised agreement with the community and media, with the timing of any communication to be agreed between Council's Chief Executive and TWHT.

DISCUSSION

Council has been represented in the negotiation with TWHT by TwentyTwo – Independent Property Advisors, with Bell Gully providing legal support and preparing the documentation required to support the transaction.

<u>The Memorandum of Key Terms</u>

The most important step in the negotiation process is agreeing the key commercial terms, which include the outline building design and specification, programme, leased areas, facilities and the lease terms. The process also included agreeing the site sale price. These terms have been renegotiated following a detailed review by TWHT which showed the project would only be feasible if the key terms are modified.

At a confidential workshop session with Council on 13 April 2022, Council discussed the key terms set out in the table below. [redacted]

- Base Building Greenstar. The developer does not propose to seek Greenstar design & build certification given the premium cost to achieve this. However, the ATL will record that the parties will endeavour to achieve reasonable sustainability outcomes where possible (to be agreed).

- Tenant Fitout Greenstar (or similar). Council does have the ability to achieve a Greenstar certification in its fitout works. There are also more advanced sustainability initiatives better suited to the occupier (e.g. WELLS) that Council will explore.
  The Net Lettable Area has been reduced from 3,100m2 to 3,030m2, effectively excluding some areas now classified as building amenities. [redacted]
- [redacted]

The final attributes of the transaction are summarised below, including comments from Councils external property advisers.

[redacted]

Fleet Parking	39 covered and secure parks (15 with EV charging stations) at $25 per park per week	[redacted]

		[redacted]
Total Annual Net Rent including carparks and incentive	[redacted] x Net Lettable Area: $3030.60m^2$ **= Net Annual Rent: $1,272,852** + Carparks: $50,700 + Estimated Opex: ~$121,200 **= Total Annual Net Rental: $1,444,752**	Total Annual Net Rental will be $594,752 higher than the cost estimated in Long Term Plan of $850,000. During RFP no offers were received which would have supported an annual rental aligned with LTP.
Site Purchase	$3m. Settlement at commencement of site works. [redacted]	[redacted] Settlement occurs upon practical completion of the base building works. Council will issue Tūwharetoa a licence to occupy and develop the site for the time period between works commencement and settlement.
[redacted]	[redacted]	
Rent increases	Stepped annual increases to CPI [redacted]	[redacted]
Structure	Steel frame to Importance Level 4	Suitable for containment of our Emergency Operating Centre
Practical Completion	Q2 or 3 – 2024 TBC	On par
Conditions	Subject to final Agreement to Lease Subject to approval by the TWHT and Council.	

Note: All Figures in table above are exclusive of GST

<u>Process for final binding agreement</u>

1. Memorandum of Terms agreed and approved by Council
2. Agreement to Lease documented (includes the Deed of Lease)
3. Agreement to Lease executed (by delegated authority)
4. Sale and Purchase Agreement executed (by delegated authority)
5. Licence to develop the site prior to settlement executed (by delegated authority)

Discussions with the TWHT on the Memorandum of Terms has been completed.

The Memorandum of Terms consists of the agreed key commercial terms and agreed outline building design and specification as summarised above. This report enables Council to consider and approve the Memorandum of Terms as outlined in the recommended resolution.

Once approved, the parties will commence documenting the agreed key terms and specifications by way of an Agreement to Lease (ATL). The ATL is a detailed and binding agreement that documents the obligations, processes, accountabilities and programme to develop and lease the building and is based on the agreed Memorandum of Terms. The key terms are not re-negotiated during the ATL documentation stage as these have been pre-agreed.

<u>Delegated Authority</u>

The resolution also seeks approval to delegate authority to the Mayor and Chief Executive to enter into the ATL, Sale and Purchase Agreement and any other necessary documentation to give effect to the transaction. These agreements will be based entirely on the agreed Memorandum of Terms.

Delegated Authority enables prompt conclusion so both parties can act with certainty in a climate where delay may have impact on the project feasibility.

The Local Government Act 2002 enables the Council to delegate, for efficiency and effectiveness, to an officer of Council any of its responsibilities, duties, or powers except those listed in Clauses 32(1) (a) to (h) of the Seventh Schedule to the LGA. The signing of the Memorandum of Terms, a Sale & Purchase agreement to dispose of 67 Horomatangi Street and an Agreement to Lease for new offices at 67 Horomatangi Street is outside the existing financial delegation from Council to the Chief Executive Officer as it is substantially more than $500,000. Therefore, a new delegation is required for this project. The proposed delegation is consistent with the requirements of the Local Government Act.

OPTIONS

Based on this information it is considered that there are two options. Either for the Council to:

- agree to the disposal of the property at 67 Horomatangi Street; and taking of a lease for new office premises in a building at 67 Horomatangi Street, based on the key terms outlined; or
- not agree to the key terms and require staff to renegotiate new key terms.

<u>Options for approving the lease agreement</u>

Option 1.- Agree to the disposal of the property at 67 Horomatangi Street; and taking of a lease for new office premises in a building at 67 Horomatangi Street, based on the key terms outlined.

Advantages	Disadvantages
• Provides certainty for both TWHT and the Council • Provides comfort to TWHT to continue design and negotiation phase with confidence • Project team will not need to return for further approval of the same material matters • [redacted] • Enables execution of the detailed Agreement documentation to occur efficiently once agreement is reached without waiting for the next Council meeting to seek agreement • [redacted]	• Total cost exceeds that set out in the Long Term Plan by $594,752. Council will need to fund this difference through efficiency gains, cost savings, rates increases or a combination of these things.

Option 2.- Do not approve the key terms and request staff to renegotiate the memorandum of key terms.

Advantages	Disadvantages
• [redacted] • Ensures that the Council sees and approves the final deal	• Results in delay in reaching agreement and signing agreements. • [redacted]

Analysis Conclusion:

Option 1 is the preferred option as it will enable negotiations to continue, provide some certainty of terms for both parties, [redacted] and faster and more efficient signing of the agreements.

CONSIDERATIONS

Alignment with Council's Vision

Council's vision is 'to be the most prosperous and liveable district in the North Island'. This is accompanied by a core set of values to underpin decision-making, the following of which are relevant to this particular proposal: Charming; Quality; and Value.

Financial Considerations

Long-term Plan/Annual Plan

A total of $850,000 per annum is budgeted for the annual lease cost from 2024/25 (inflation adjusted to $892,000 for 2024/25 going forward in the Long-term Plan 2021). The negotiated lease agreement ($1,272,852) exceeds this by $594,752 (an increase of 47%). As outlined earlier in this report this is due to:

- an increased area of floorspace (3,030m^2 instead of 2,500m^2); and
- increased rent proposed by the developer which reflects the rising costs of commercial rents due mainly to the increasing costs of construction and investor yield.

[redacted]

In the context of Council's overall rates, the difference between the proposal amounts to at most a 0.51% increase (in the 2024/2025, with lesser increases in other years). This will need to be funded from rates.

The LTP also budgeted $3,500,000 in the 2024/25 year ($3,773,000 inflation adjusted) for fit out costs for the Council Offices. The estimated fit out costs have changed and are currently in the order of $4,900,000. This is a reflection of:

- the increased area of floorspace (2,648m^2 instead of 2,500m^2 as Council will only fitout the net usable area)
- increased fitout costs due to a heated construction market, supply chain issues and labour shortages.

It is now proposed to do the fit out of the building in an integrated way as it is being constructed requiring the fit out expenditure to be brought forward to 2022/23 and 2023/24. These fit out costs do not form part of the lease agreement with TWHT.

The average cost per ratepayer per LTP is different from the figures outlined in the Consultation Document for the LTP 2021-31. This is because the savings made by not having to rent multiple premises in the town centre, that Council staff are currently housed in, were not factored into the calculations in the LTP. Instead, in the consultation document, the direct cost of both options (leasing a building or owning a building) were compared.

Legal Considerations

Local Government Act 2002

The matter comes within scope of the Council's lawful powers, including satisfying the purpose statement of Section 10 of the Local Government Act 2002 (LGA). That section of the Act states that the purpose of local government is (a) to enable democratic local decision-making and action by, and on behalf of, communities; and (b) to promote the social, economic, environmental, and cultural well-being of communities in the present and for the future. It is considered that economic, environmental and cultural well-being are of relevance to this particular matter.

Sections 77-81 of the LGA are relevant for Council decision making. Section 78 requires the Council, in the course of its decision-making process, to give consideration to the views and preferences of persons likely to be affected by, or to have an interest in, the matter. The Council first consulted with the community in early 2017 (as part of the Annual Plan 2017) on different options, from refurbishment to a new build, for the new Council offices. Consultation has continued until most recently in March 2021 when the Council asked the community, through its consultation document for the Long-term Plan 2021-31 whether it thought Council should lease a building or own a building. Council confirmed, as part of its decision on the LTP, that it would lease a building for Council Offices and budgeted $850,000 ($892,000 inflation adjusted) every year from the 2024/25 year. Council also budgeted $3,500,000 in the 2024/25 year ($3,773,000 inflation adjusted) for fit out costs in the LTP. Through the draft Annual Plan for the 2022/23 year Council has signalled an intent to bring the fitout forward and increase the budget to $4,900,000.

Clause 32(1) of the 7th schedule to the Local Government Act 2002 enables "for the purposes of efficiency and effectiveness in the conduct of [Council's] business," for the Council to delegate to an officer of Council any of its responsibilities, duties, or powers except those listed. A delegation from Council to the Mayor and Chief Executive for the signing of a Memorandum of Terms reflecting the key commercial terms set out in this paper, a Sale & Purchase agreement to dispose of 67 Horomatangi Street to TWHT, an Agreement to Lease for new offices at 67 Horomatangi Street; and any other documents required to give effect to these transactions is consistent with this part of the Local Government Act.

Policy Implications

As outlined above a budget for the lease and fit out of a building for the Council Offices has been included in the LTP 2021-31 and was consulted on as an option in the consultation document for this LTP. However, the budgets now required, the timing of these budget and the impact on the average cost per ratepayer have changed. The changes to the average cost per ratepayer reflect the increase in leased floorspace, the increased rent (in accordance with market rents), increased fit out costs and increased fit out floor area. These changes reflect the changing market conditions. A decision to agree to the financial terms in the Memorandum of Terms is not inconsistent with the LTP.

Māori Engagement

Iwi and hapū groups were provided the opportunity to express their views on the proposal to lease a building for Council's administrative functions as part of the Long-term Plan. No further targeted engagement with those groups is considered necessary to inform Council's decision making on the terms of the actual lease agreement.

With the Tūwharetoa Māori Trust Board, Tūwharetoa Settlement Trust, Ngāti Tūwharetoa Fisheries, Te Pae o Waimihia and Lake Taupō Forest Trust as partners in TWHT, this presents a clear opportunity to strengthen the partnership between Council and Ngāti Tūwharetoa. With the first three partners mentioned as tenants within the building, this development would also create an opportunity for better collaboration and co-location with Council to enhance the working relationship between these organisations. Indeed, this co-operative endeavour would reflect the partnership envisaged for iwi and local government creating a unique flagship building for the future of the Taupō district.

This procurement can leverage broader outcomes that enable the involvement of Māori suppliers, including TWHT and Tūwharetoa cultural advisors, artists and kūmātua that will be involved in the project. It is acknowledged that this building will become a taonga of both organisations, and appropriate steps to recognise and display what is precious to the Taupō region will be embraced through design.

Risks

The risks associated with the project now fall into two categories:

1) Cost escalation. As TWHT have completed a detailed assessment of the development feasibility and re-presented commercial terms to reflect that due diligence, the risk of movement in cost has been mitigated by way of the agreed Memorandum of Terms. Once the Agreement to Lease (ATL) has been agreed and executed, then Councils lease costs and key lease terms are secured.

   There are a number of levers to mitigate or accommodate this risk:

   a. Make a decision quickly
   b. Enter into a binding ATL so no changes can be made

2) Delivery risk. Contractor availability and supply chain issues may impact TWHT's ability to deliver the building on time. This may have a flow on effect to Council's current leases and fitout costs. To mitigate this, the Agreement will include a clear communication process to deal with delay (or Force majeure events) including the potential of a penalty regime, and Council will seek to negotiate flexibility in its leases in its current portfolio, where possible.

SIGNIFICANCE OF THE DECISION OR PROPOSAL

Council's Significance and Engagement policy identifies the following matters that are to be taken into account when assessing the degree of significance of proposals and decisions:

a. The level of financial consequences of the proposal or decision;

b. Whether the proposal or decision will affect a large portion of the community or community of interest;

c. The likely impact on present and future interests of the community, recognising Maori cultural values and their relationship to land and water;

d. Whether the proposal affects the level of service of an activity identified in the Long Term Plan;

e. Whether community interest is high; and

f. The capacity of Council to perform its role and the financial and other costs of doing so.

Officers have undertaken a rounded assessment of the matters in clause 11 of the Significance and Engagement Policy (2016) and are of the opinion that the proposal under consideration has a high degree of importance and so is significant. This is because the decision to approve in principle a lease agreement for the Council Offices and the sale of the land at 67 Horomatangi Street will have:

- a high level of financial consequences;
- will affect a large portion of the community;
- will impact on present and future interests of the community; and
- the community interest is high.

The engagement section below analyses the Significance and Engagement Policy (2016) further and concludes that no further consultation is required.

ENGAGEMENT

In March 2021 Council sought feedback from the community, through the consultation document for the Long-term plan 2021-31, on the future for meeting Council's office space requirements. The document asked for feedback on whether to lease or own a building to house council staff and stated that Council's preferred option was to lease a building. The consultation document outlined all the consultation and council decisions on the Council Offices so far, from the initial consultation to determine options for the Council Offices back in May 2017. The document set out the advantages, disadvantages and costs including the average cost per ratepayer for two options. These options were to lease a building or to own a building on the Tūwharetoa Street car park. 138 submissions were received on this issue with feedback overwhelmingly (81%) in favour of leasing. The reasons for this were that it was considered cheaper overall to lease, there was less risk in leasing, less cost uncertainty and it was important that any lease must be at market rates. As part of the decisions on the LTP 2021-31 Council confirmed that leasing is the preferred option for the future of the Council Offices.

While the average cost per ratepayer has increased for the lease of a Council Offices since the LTP was adopted, this is due to increases in the floor area required, an increase in market commercial lease rates and fit out costs and bringing forward of the fit out of the building. Officers have sought advice and formed the view that further consultation is not required as the overall proposal is fundamentally the same as what was consulted on (i.e. a long-term lease), the specific location was not part of the Council's consultation (so the Council is not bound to any particular location) and the increase in the cost does not reach the level where further consultation is required. This conclusion is supported by the overall circumstances which also point away from any further consultation being legally necessary.

The Significance and Engagement Policy outlines situations when Council may not engage during the decision making process. Section 8 of that policy is relevant:

Council may choose not to engage when:

a. There is already a good understanding of the views and preferences of those that are affected or interested;

b. There is need for confidentiality;

c. The costs outweigh the benefits;

d. The matter has already been addressed through Council policies and plans;

e. An immediate or quick decision is required;

f. Emergency works are required; or

g. The matter relates to the operation and maintenance of a Council asset and responsible management requires the works to take place.

Subsections (a), (b), (d) and (e) are relevant in this case.

It is considered that further engagement with the community is not required at this stage as:

- These cost increases, when assessed on the overall impact on rates, are small (see table in financial considerations section of this report).
- The negotiations with the developer are at a crucial stage and it is prudent to continue to negotiate out the key commercial terms.
- The financial component of the commercial terms are commercially sensitive and so cannot be disclosed to the community at this time.
- Halting negotiation at this stage to engage with the community could potentially result in the deal being lost.
- [redacted]
- Council is aware of views and preferences of the community on the leasing option for the Council Offices as extensive engagement has occurred on this topic since 2017, especially through the community's submissions during the development of the LTP 2021-31.

Accordingly, Council is aware of the views of the community on whether leasing is a good option. And while the costs of leasing have escalated since the consultation in March 2021, so too have the costs of construction correspondingly escalated meaning that the earlier comparison of leasing relative to owning remains valid. On that basis officers advise that Council does not need to undertake further engagement to understand the views and preferences of the community.

[redacted]

COMMUNICATION/MEDIA

A communications plan has been developed and information on the progress of the council administration building is continuing to be shared with the community, including local and national media. Following this decision, communications will be shared with the community and media about this finalised agreement, with timing to be agreed between both council and TWHT.

CONCLUSION

TWHT and the proposed Memorandum of Key Terms remain the most favourable option for Council to successfully deliver its objective of a fit for purpose, single site solution. The drivers for this recommendation are:

[redacted]

While there is some risk that the Memorandum of Terms may be amended as TWHT advance the detailed design, the sooner Council reaches Agreement to Lease the greater certainty it will create. Much of this progress to Agreement will be driven by TWHT but we believe they have genuine positive intent and appreciate Council has little appetite for material change.

ATTACHMENTS

Nil