

CABINET	AGENDA ITEM No. 10
11 March 2024	PUBLIC REPORT

Report of:	Cecilie Booth – Executive Director for Corporate Services and s151 Officer	
Cabinet Member(s) responsible:	Cllr John Howard, Deputy Leader and Cabinet Member for Corporate Governance and Finance;	
Contact Officer(s):	Cecilie Booth – Executive Director for Corporate Services and s151 Officer	Tel. 01733 747474

HILTON HOTEL

RECOMMENDATIONS	
FROM: Executive Director for Corporate Services	Deadline date: March 2024
<p>It is recommended that Cabinet:</p> <ol style="list-style-type: none"> 1. Authorises the Council to submit a credit bid (up to the value of the amount it is owed for the loan) to secure the freehold interest in the Hilton Hotel. 2. Delegate authority to the Executive Director of Corporate Services, in consultation with the Director of Law and Governance to take all necessary steps including entering into any legal agreements to facilitate the decision in recommendation 1. 3. Subject to approval of Recommendation 1, delegate authority to the Executive Director of Corporate Services, in consultation with the Director of Law and Governance and the Cabinet Member for Corporate, Governance and Finance to progress the next steps to ensure the hotel is developed to completion, including preparation of a business case, with details of the procurement plan for suitable partners which will be submitted to Cabinet for approval. 	

1. ORIGIN OF REPORT

- 1.1 The Council provided a loan to Fletton Quays Hotel Ltd (“FQH”) to build a Hilton Garden Inn hotel. The loan agreement was extended three times, the last time in May 2023. Due to lack of progress since then, the Council exercised its powers in the loan agreement to place the hotel developer into administration in November 2023. The Council has repeatedly said it is committed to ensuring the hotel is completed and the Council’s investment is protected. This report sets out the next steps to ensure this is the case.

2. PURPOSE AND REASON FOR REPORT

- 2.1 The purpose of this report is to seek Cabinet approval to submit a credit bid to the administrators to secure the freehold interest in the hotel and to seek an endorsement from Cabinet on the approach to be followed by officers following a successful credit bid.

3. **TIMESCALES**

Is this a Major Policy Item / Statutory Plan? Yes

If yes, date for Cabinet Meeting 11th March 2024

4. **BACKGROUND**

- 4.1 The loan was provided to FQH into as part of the wider regeneration of the Fletton Quays development, for the purposes of regeneration and was approved unanimously by Cabinet in September 2017. The cabinet report including the rationale is included at Appendix A.

At the time the loan was entered into, the parent company of FQH (Norlin Hotel Holdings Ltd) fell into financial difficulties and transferred the hotel to a different company (Propiteer Hotels Ltd). Due diligence was completed on all 3 companies and its directors before the loan agreement was entered into. Reports have been approved by Cabinet for each change or extension to the loan agreement.

Each amount drawn down was subject to a report from a Quantity Surveyor (QS) who confirmed the value of the work completed, including assurance that it was not greater than 83% of the value of the asset under construction. On this basis it was believed that the loan was secure.

The loan was extended three times, mainly due to Covid and Brexit, which resulted in a shortage in labour and materials, inflation and a general downturn in the construction market.

The developer approached the Council in April 2023, asking for a third loan extension, which was granted. However, little or no progress was made on the construction of the hotel after this extension, and on 17 November 2023 the Council put FQH into administration. The loan had not been defaulted upon as interest accrued is due at the end. However, the loan was due to be repaid on 31 December 2023 and it was believed the contractor and owner of the company had run out of funds. Notice was served as the hotel had been unoccupied for a period of more than 28 days. At this stage the interest accrued was £2m.

The Council's loan agreement with FQH was for a maximum amount of £15m and in total £14.7m has been drawn down. The loan agreement stated that the value of the Council's loan should not exceed 83% of the asset valuation at any time.

FQH purchased the land on which the hotel is located from the Peterborough Investment Partnership (PIP) separately, the Council did not fund the land acquisition.

The Council has repeatedly said it is committed to ensuring the hotel is completed and the Council's investment is protected.

As the asset is currently in the hands of the administrators, at this stage the Council needs to consider the options available to continue to protect the investment to date and to determine whether or not to submit a credit bid.

As advised by the administrators, Teneo, the hotel, in administration, was marketed as a 'closed' procurement exercise, limited to companies with a legal interest in the Hotel, on 13 February 2024.

The Council have been advised that a full marketing exercise would take at least a year, and it would be expensive to prepare the full marketing documentation. Doing so would mean that the hotel would remain undeveloped for a much longer period. The property is currently not heated

and would deteriorate if left for another winter. In addition, delays would incur additional security costs and interest payments being incurred.

The marketing exercise closes on 4 March. The report is seeking approval to submit a credit bid of up to the value of the outstanding balance of £17m. The Council does not have to meet the bid deadline and can bid later with the benefit of seeing the other bid before making its own. This means the Council may choose to accept an alternative bid if it is within a suitable tolerance range.

4.2 The objectives for the Council's proposals for the hotel are:

1. To continue to protect the initial investment in the hotel. This is £14.7m plus £2m of accrued interest (note this is the amount of interest charged at a commercial rate and not the amount it cost the Council to borrow).
2. To ensure the hotel is built and completed to a high specification to support the Fletton Quays regeneration objectives.

The loan was made for regeneration purposes and the hotel is an important and strategic part of the Fletton Quays development site. It is important to the Council that this remains a flagship development site; the Hilton Garden Inn is a top end hotel and of a higher quality than Peterborough would normally attract. It is therefore important that the hotel is built to the anticipated standard. Hilton remains committed to having a Garden Inn operating from this site.

4.3 The recommendation is to submit a credit bid for the hotel. This means that the Council will submit a bid up to the value of the amount it is owed for the loan, i.e. £17m. It is not assumed that another company would submit a bid that high. The size of the Council bid is aimed to ensure the Council can continue to protect its investment and ensure the hotel is developed to the original high quality, including the sky bar.

The Council would then develop the hotel to completion with a suitable development partner and a range of advisors and with an operating partner in place to run the hotel as a Hilton Franchisee post completion. This is believed to be the quickest way to complete the hotel and is the established delivery route for this type of development.

The optimal value of a hotel is reached after 3-5 years of trading. At this stage, any owner or operator would be buying an established business and not just a building. Therefore, the proposal would be for Council to complete the hotel and then operate it with an operating partner for at least 3-5 years. After this period, the Council can decide whether to sell the hotel to continue to run it. Full details of the proposals will be included in the business case which will be submitted to Cabinet for approval at a later date.

The financial position is set out later in this report.

There are several risks in this strategy and the most significant are laid out in the table at Appendix B.

4.4 It should be noted that the Hilton remains committed to the Peterborough hotel. Council officers have met with the Hilton brand on several occasions and the Hilton are helping the Council to develop the hotel to completion. The Hilton brand works as a franchise, the Hilton do not own hotels but work with approved developers and operators to run hotels for them.

Communications about the development of the hotel have been joint with the Hilton. They are supportive of the Council's approach and are helping us to plan the next stages.

The Council has spoken to four other Councils who also own a Hilton Hotel. The feedback is that hotel occupancy rates are good and has exceeded expectations. The food and beverage element of sales are behind predictions, but overall, all are happy with their hotels, their operation and the trajectory they are on.

An additional factor that may impact stakeholder involvement is that on 17th February 2024, administrators were also appointed to Propiteer Fletton Quays Limited, the company which owns the apartments adjoined to the hotel. The hotel administrators are in discussions with the administrators for the apartments to understand their proposed strategy so they can consider any implications for FQH. At this time the implications are unknown. Although the Council has no financial exposure to the apartment development, we will keep a close eye on progress and an update will be provided in the next Cabinet report.

4.5 **Option 1- Submit a credit bid to buy the freehold interest of hotel**

The Council would put in a credit bid to buy the hotel, up to the value of the outstanding investment. The hotel would need to be developed by the Council in conjunction with a Hilton approved developer and run by the Hilton approved operator. This would be an absolute requirement in the procurement exercise. It should be noted that no new money is required to submit the credit bid, except the cost of the administration process, keeping the building safe and associated procurement costs to secure the necessary partners and advisors.

This option would ensure the Council would protect the investment to date and develop the hotel to the right scope. It would ensure the finish is not compromised, the regeneration of the Fletton Quays development site is not compromised and the regeneration of the Fletton Quays development site is protected. The Council will also ensure that procurement procedures are complied with.

Further reports will be submitted to Cabinet in due course, as and when the project develops, and more detailed information about the future costs are available.

Option 2- Decline to submit credit bid

The hotel is currently being marketed to a small audience and one of these parties could put in an acceptable bid. This will not be known until 4 March at the earliest.

The hotel as it stands today will be valued as a 'distressed asset', and any third-party bid is likely to be significantly lower than the Council's current debt.

It is therefore expected that a credible proposal will not be made. It is also questionable whether the hotel could be completed to the high standard expected of this flagship regeneration site, during earlier discussions with the parties involved, there was talk of a lower standard hotel or an asylum seekers hotel.

If and when bids are received from the other interested parties, these can be considered.

It is recommended that the Council submit a credit-bid to secure the asset, develop the hotel to completion and develop a strategy to work with Hilton approved companies to ensure completion in the most efficient and effective way.

A full business case will be submitted to Cabinet for approval.

4.6 CONCLUSION

- 4.6.1 If and when bids are received from the other interested parties on 4th March, these can be considered.

If bids received are not within an acceptable tolerance level, the Council should submit a credit-bid to buy, develop and complete the hotel, and to develop a strategy to work with Hilton approved companies to ensure the hotel is developed and completed in the most efficient and effective way.

Further reports will be presented to Cabinet in due course.

5. CORPORATE PRIORITIES

- 5.1 The provision of the services described in this report contribute across many of the Council's priorities, most notably:

- Our Places and Communities: especially relating to improving health and wellbeing, providing local jobs, and providing community spaces.
- The recommendations in this report however focus on the structure and model of delivery, which contributes directly to:
- Sustainable Future City Council: by mitigating the Council's financial exposure the development and avoiding a financial loss.

6. CONSULTATION

- 6.1 This report has been considered by:

- Corporate Leadership Team
- Cabinet Policy Forum

7. ANTICIPATED OUTCOMES OR IMPACT

- 7.1 If the recommendations are endorsed, it is anticipated that the city will benefit from a flagship hotel supporting the regeneration objectives and delivering jobs and prosperity to the City.

8. REASON FOR THE RECOMMENDATION

- 8.1 To secure the Council's existing investment and to ensure the hotel is completed as quickly as possible

9. ALTERNATIVE OPTIONS CONSIDERED

- 9.1 The alternative position to decline to submit a credit bid and accept a third-party bid would increase the Council's financial exposure to the development and carries significant risk around the use to which the partially built hotel will be put.

10. IMPLICATIONS

10.1 Financial Implications

Before the hotel was put into administration, the Council employed a company to complete a revised valuation of the hotel on the following basis:

1. as it is,
2. once it has been completed,

3. after it has traded for 3-5 years.

The report is currently delayed whilst the full 'cost-to-complete' the hotel costs are finalised by the Administrator.

Prior to the hotel being put into administration it was believed that the costs for the hotel would be approximately as set out in Table 1 below:

Table 1

	£m
Council loan	(15)
Costs to complete	(10)
Hotel value after 5 years trading	25
Additional expenses, including stamp duty and legal fees	(1)
Loss of interest payable on the loan	(2)
Overall loss	(3)

It should be noted that the Council loan already exists; this is not "new money", and interest due on the loan is already included in the Council's budgets. The £10m costs to complete the hotel are included in the 2024/25 capital programme, which was approved by Full Council on Wednesday 21 February.

The position is now more nuanced as, following the work by the property consultants, the costs to complete have increased. In addition, the expected value of the completed hotel has reduced, this is primarily due to an increase in the investment yield, and is a result of harder trading times for hotels. The valuers have not confirmed the final value of the completed, or part finished, hotel, but it is believed to be in line with Table 2 below.

Table 2 (current estimate)

	£m
Credit bid for the hotel	(17) (already invested)
Costs to complete	(14.4)
Additional costs to complete the hotel, including stamp duty and legal costs	(0.6)
Administrators costs, to be borne by the hotel	(0.5)
Total costs	(32.5)
Value of a completed hotel after 3 years trading	22
Loss/ amount to be written off the Council	(10.5)

Not included in Table 2 above is the use of grants to reduce the Council's own investment. Other Councils have used Government grants to reduce the costs of developing a hotel. It is believed that the same could be achieved in Peterborough and we are currently looking for future grant opportunities, using the knowledge of Opportunity Peterborough.

If grants were utilised, the £10m currently within the capital programme to complete the hotel should be sufficient. Government grants could be used to reduce the overall Council loss, the amount by which would depend on the size of the grant received.

If no grants are available and more funding were required from the Council, then the £10m contained within Minor Capital Programmes could be utilised.

Also, the costs-to-complete from the consultants are being challenged as there are certain costs and assumptions that could be reduced or removed. This includes where it is proposed to pay

previous suppliers in full so warranties can be received. A full review of the costs-to-complete will be concluded in March and will inform the final business case to support any acquisition. This review will also recommend the procurement and delivery route for the works required.

In any event, the hotel may remain in Council ownership until capital valuations increase in line with market conditions, assuming income from the hotel covers the Council's cost of capital. Other Councils have done so.

The alternative is to accept a bid from a third party. It is believed this would result in a greater loss than the proposed option.

The current 'as is' valuation (indicated at circa £1.45m) assumes the site is sold today and accounts for the estimated costs-to-complete of £14.4m. The valuation also accounts for construction risks, borrowing costs and profit for any purchaser/developer taking on the project.

Table 3 below, sets out the potential assessment:

Table 3

	£m
Council loan	(17)
Maximum expected bid	1.45
Other costs incurred	(0.3)
Loss/ amount to be written off the Council	(15.85)

10.2 Legal Implications

The Council has legal powers to submit a credit bid to secure the freehold interest as proposed in this report.

A full business case will be submitted and approved by Cabinet as per the recommendations which will set out more detailed legal implications in respect of the proposal in the event that the credit bid is accepted.

10.3 Equalities Implications

None

11. BACKGROUND DOCUMENTS

11.1 N/A.

12. APPENDICES

12.1 Appendix A – Original Decision
Appendix B - Summary of Risks

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