Hallbankgate Hub

Management Committee Note on Purchase Process for Shop Premises

Phase 1 : Launch to bid decision (January – April 2015)

The ad hoc Steering Group formed from the public meeting held in December 2014 when Scottish Midland (ScotMid) announced their decision to close the Hallbankgate Co-op, and which met for the first time on 5th January 2015, initially contained divided views over whether to pursue purchase of the existing shop premises. Some felt this to be desirable both for local heritage reasons and to minimise the time during which the area would be without a shop; others felt that a locally-run enterprise would only succeed if it made a new start in a new location, and also that the purchase price would be beyond the means of a community group. Additionally, many had concerns over the condition of the existing building and the complicated nature of its multi-occupancy.

To ensure that we retained the option to purchase the existing premises, we applied for their designation by the City Council as a Community Asset, which took place in March 2015 and thereby preserved for six months our right to bid.

During the period January – March 2015 our concerns about the shop premises were addressed by commissioning a survey of title from solicitors Minihan McAllister, a valuation survey from Edwin Thompson (March) and a pre-acquisition building survey from the same source (available 9th April). Alternative options involving Portakabins or new-build were also canvassed and to some extent costed.

The results of these investigations were considered at a meeting of the Steering Group held on 23rd March 2015, when after thorough discussion it was decided by a majority vote to pursue a bid for the existing premises. This was on the basis that our surveys had shown these premises to be in adequate condition and potentially affordable, while a Portakabin option (whether rental or purchase) would not provide us with a sufficiently valuable asset against which to raise loans or obtain grants, would be ineligible for the Parish Trust donation of £13k which had been agreed in March, and raised siting problems. The single proposed new-build option was judged to be unacceptably speculative as to cost, site and feasibility.

A further meeting of the Steering Group on 13th April 2015 agreed to put forward to ScotMid a bid with a ceiling of £26k, but with a starting offer in the region of £16-20k. This reflected the value of £46k which the valuation survey had put on the premises, against which we hoped to offset the approximately £30k's-worth of necessary repairs identified by the building survey. The bid was to be for the shop premises, outbuildings and access road, though it later transpired that the outbuildings had been in the meanwhile sold separately by ScotMid to David Armstrong. A negotiating team was appointed comprising Steve Bowles (then Treasurer), John Foster (Chair) and Robin Murray.

Phase 2 : The bid process (April – June 2015)
On 13th April the Steering Group had also voted to reconstitute itself as the Management Committee of the recently-incorporated Hallbankgate Hub Ltd Community Benefit Society. The Committee, appointed in accordance with the Model Rules of the Plunkett Society which had been adopted as our Constitution, met for the first time on 20th April 2015 and confirmed the above approach. The broad strategy agreed was to pay as little upfront as we could in order to buy an asset that would provide some security for those in the community who would buy shares, and to get an agreement and a sale as rapidly as we could. By producing an innovative and well-costed business plan we hoped to maximise our equity and minimise our loans (particularly from banks), encourage as many people as possible from the community to purchase shares in the shop and use the community buy-in together with the innovative business plan to raise matching grant funds. We could then treat our governance as a trial period to see if the community was able to run a collaborative venture.

The negotiating team met with senior executives of ScotMid in Edinburgh on 24th April 2015. Present from ScotMid's side were John Brodie (CEO), Malcolm Brown (Director of Corporate Communications) and Adrian Lorimer (Director of Property Services). At this meeting ScotMid clearly rejected the Hub's offer of £20k on the grounds that their own 2013 valuation of the premises (plus outbuildings) by nationwide property consultants Sanderson Wetherall had indicated a value of £70k. ScotMid officers felt that a bid at the level to which the Hub team was empowered at that stage to go would not be acceptable to their Board because it would be seen to involve disposing of an asset far below market value to the disadvantage of the wider membership of their Co-op. At the end John Brodie indicated that the bid would need to have 'a 5 in it to be acceptable to their Board', while one with a 4 in it would be uncertain in its outcome. An option to lease the premises as an alternative to purchase was put forward in outline by John Brodie, and later costed in detail by Adrian Lorimer. Discussion continued amicably but concluded with matters unresolved, the Hub negotiating team feeling unable to proceed without reporting back.

An emergency meeting of the Management Committee convened on 25th April 2015 to consider the results of this first approach decided (a) that we should not lease, since this would cost us a sum similar to the purchase price over five years while leaving us without an owned asset, and (b) that we could not within any plausible business-planning parameters make an offer extending even to £40k. In reporting the first of these decisions to ScotMid we indicated our hope that our purchase bid could lie on the table while we tried to find a way forward, and as a gesture of goodwill they agreed to keep the Hallbankgate Co-op open until 1st June (the originally planned closure date having been 1st April) in the hope of a successful outcome.

At a further meeting on 4th May 2015, with the prospect of a match-funding grant application to the newly-announced Power to Change programme looking feasible, and in the light of ongoing work by Duncan Sperry and Robin Murray on a business plan including detailed three-year financial projections , it was agreed that we could increase our bid to a ceiling of

£35k. Duncan Sperry, with considerable experience of corporate deals, at this point joined the negotiating team.

A revised bid of £35k was put to ScotMid in a formal letter from the Chair to John Brodie dated 29th April 2015. This was accompanied by an appeal for flexibility on their part in line with their published values of collaboration between co-operatives and supporting local communities. This bid was eventually (at our request) put before ScotMid's Board at its meeting of 28th May 2015, but rejected.

Discussion then proceeded by telephone and email, principally between Adrian Lorimer for ScotMid and John Foster (in continuous consultation with the other members of the negotiating team) for the Hub, in an attempt to keep our bid alive. The upshot was to leave a gap of £10k between our offer of £35k and what emerged as ScotMid's effective bottom line of £45k. However, it also appeared that this gap might in principle be bridged by the offer to ScotMid of shares in the Hub to the value of £10k on top of the maximum cash offer of £35k. From ScotMid's side they would have the prospect of being able to apply to realise the value of their shares were the fortunes of the Hub successful enough for any future Committee to approve such a cashing in of the shares. From the Hub's point of view, they would have less initial capital to find, and at the same time could apply for further £10,000 from the Power to Change fund as matching ScotMid's £10,000 share investment.

At the same time, ScotMid would be able to guard against our re-selling the Hub premises for a capital gain through the inclusion of an overage agreement whereby they would share 50:50 in the profits (net of any improvement costs) of any onward sale of the premises within ten years.

At a Management Committee meeting held on 8th June 2015 it was agreed to offer to proceed on this basis. A factor in this decision, in addition to our continuing desire to purchase if we could, was our concern that the community asset provision was coming to an end in August and therefore there was the possibility that if we could not successfully conclude a deal, ScotMid might then after all seek to sell the premises for development.

ScotMid via Adrian Lorimer having indicated acceptance in principle of an offer thus framed, we moved to the appointment of a solicitor (again Jayne Minihan of Minihan McAllister). ScotMid similarly placed the transaction in the hands of their corporate lawyers, Anderson Strathern of Edinburgh.

Meanwhile, the Hallbankgate Co-op had closed on 1st June 2015

Phase 3 : Heads of Terms to completion (July – November 2015)

From this point onwards matters proceeded more slowly, because the deal developed complexities in relation to the overage agreement and the terms on which ScotMid were to hold shares.

Discussion on draft Heads of Terms indicated in July that ScotMid were asking not just for overage but for a guaranteed rate of interest on their shares and for a pre-arranged timetable for their selling them back to us. The Management Committee meeting on 27th July 2015 agreed that these latter two demands were incompatible with the provisions in our Constitution (paras. 8.4 and 8.5) giving the Committee for the time being absolute discretion over both interest payments and realisation of investments. We also received legal advice from our solicitor that the Constitution did not permit us to change these provisions in favour of any particular shareholder.

A way forward was agreed in direct negotiations with ScotMid during July and early August, to include:

- provision by the Hub of a side letter to the purchase contract indicating that any future Management Committee would exercise its discretion over the repurchase of shares reasonably and would keep ScotMid fully informed ongoingly of the Hub's financial position;
- undertaking by ScotMid not to seek to withdraw more than £2.5k per financial year and starting only after three years had elapsed; and
- agreement by ScotMid not to pursue the matter of interest on their shares.

The Management Committee agreed a draft side letter in line with the above at its meeting on 17th August 2015, the terms of which were shared with ScotMid via the solicitors.

It then transpired, however, that ScotMid (via Adrian Lorimer) were being advised by their solicitor that the side letter as drafted did not sufficiently protect their interests as shareholders in the Hub, and that their Board would need formal advice from the same source that those interests were being protected before it could sign off the proposed deal. ScotMid's concern was to ensure that at the minimum they recouped the value of their shares. The Management Committee addressed this situation by agreeing to strengthen the overage agreement so that should the property be sold on within ten years, ScotMid would receive either 50% of net profit on sale or the value of their outstanding shareholding, whichever was the greater. This way of proceeding was considered and agreed by the Committee at its meetings of 14th and 28th September 2015.

Throughout these discussions, it was clear that ScotMid were attempting to maintain the accounting value of their sale, while from the Hub side we were clear that we had no intention of selling the premises within ten years, unless we proved unable to run the shop profitably, in which case the precise distribution of any surplus on the sale value of the Hub premises should not be considered as a deal-breaker. For us the major risk was not concluding a sale that would allow us to re-start the shop.

The final lap involved dealing with a series of refinements sought by Anderson Strathern on behalf of ScotMid affecting the precise text of the side letter, definitions respectively of ‘improvements’ to be netted from any profit on sale for overage purposes and of ‘market value’ in this connection, and the terms in which reference to the Parish Trust first charge on the property was to be made. On the advice of the negotiating team (to whom the issues had been delegated by the Management Committee at its meetings on 1st September and 12th October) and in order to expedite the process at this stage, these matters were all resolved as per the contract document, overage agreement and side letter as finally signed.

For the same reason there remained a number of ambiguities in the sale which could have led to much longer delays. Chief among them was the exact area of ScotMid’s asset, since there was an ambiguity in the Land Registry records, and in the obligations for repair falling to the Hub in relation to the building as a whole. The Hub Committee took the view that these could be addressed after the sale had taken place, because of the dangers of further delays.

Contracts were finally exchanged and purchase completed on 18th November 2015.

In summary :
The Hub has been able to purchase 2,000 square feet of retail space for £35,000 (net) – a price of £17.50 a square foot. It has been able raise this sum through its community share issue and the backing of the Parish Trust. Any future obligation to re-purchase the ScotMid shares is dependent on the Hub’s success in its first ten years, and in any case would be considerably less than the nominal £10,000 if the sum is discounted to its present value today.

The cost of repairs is likely to be more than our original estimate of £30,000. But thanks to the generosity of those who have bought shares, and the backing of the Village Trust, we have been able to raise matching grant funds to cover a large part of the repair costs and the start up finance, and have reasonable prospects of obtaining further grant funding for the rest.

From a financial point of view it means that we have primarily equity funding, with our only loans the £20,000 bridging loans, which we intend to pay off through raising further equity investment once the shop is opened. Most important, we have been able to avoid relying on bank finance, and so preserve our financial autonomy.

John Foster
30th November 2015