

FUNDING THE NEW BUS TRANSPORT INTERCHANGE

REPORT OF THE DIRECTOR OF ECONOMIC DEVELOPMENT

AGENDA ITEM: 10

**PORTFOLIO: INVESTMENT & DEVELOPMENT (COUNCILLOR RUSSELL
GOODWAY)**

Appendices 2, 3, 4, 5, and 6 of this report are exempt from publication because they contain information of the kind described in paragraphs 14 and 21 of parts 4 and 5 of Schedule 12A to the Local Government Act 1972.

Reason for this Report

1. To report the commitment of the new Council administration to the delivery of a new bus interchange on the former Marland House/Wood St NCP Car Park site at Central Square and to outline the challenges which need to be addressed to facilitate its construction.
2. To seek the new Cabinet's 'in-principle' agreement to a revised funding strategy required to facilitate the delivery of the bus Interchange and to request that delegated authority be given to the Director of Economic Development in consultation with the Cabinet Member for Investment & Development to enter into appropriate contractual agreements with the developer to secure a start on site at the earliest possible date.
3. To secure Cabinet authority to address and deal with all outstanding pre-development costs relating to a new Bus Interchange development including design, planning and site preparation costs.

Background

4. The new Administration has set out its policy priorities in the Vision Statement "Capital Ambition" which, amongst other things, prioritises:
 - The delivery of a new business district and gateway to Wales to the north and south of Cardiff Central Station.
 - Delivering a new transport interchange which will be at the heart of the Cardiff Metro.

5. Furthermore, the Administration has confirmed support for the 2013 proposal to redevelop Central Square and to provide a suitable state-of-the-art bus station facility, on a suitable site, that will equip the city with the modern transport interchange befitting our nation's capital.
6. Initially, it was envisaged that the bus interchange would be located on land south of Cardiff Central Station as part of the emerging proposals for the Cardiff Metro. However, on 15 May 2014, Cabinet decided to locate the new facility on the site of Marland House, which as a consequence, required the Council to acquire the long leasehold interest in the Wood Street NCP Car Park. This decision confirmed the earlier decision to:
 - Facilitate jobs growth by working with partners to deliver 300,000 sq ft of office accommodation within Central Square by March 2019.
 - In partnership with developers, transport operators and businesses deliver a new Central Transport Interchange
7. In total, the Central Square development will deliver over 1 million sq ft of high quality office-led mixed use development and is anticipated to accommodate up to 10,000 jobs. The regeneration scheme has been delivered through a public-private partnership between Cardiff Council and local development company Rightacres Property Ltd with funding provided by Legal & General Pensions Ltd. This agreement committed the Council to acquiring the leasehold interests in Marland House and St David's House on Central Square along with the site of the former Thomson House on Havelock Street.
8. The project now needs to progress to the next phase following the completion of 1 Central Square and with 2 Central Square and the BBC Wales building currently under construction. Plans for the development of the land north of Wood Street will accommodate a major new grade A* office development comprising 265,000 sq ft in phase 1, accommodating circa 3000 jobs. Negotiations between the developer and a potential occupier are at an advanced stage and it is hoped to conclude matters in the near future. The scheme will also include a substantial new public square on Wood Street.

Current Position

9. The Council and the developer have over time made substantial investments in bringing forward the Bus Interchange project. The project was initiated through a WELTAG public consultation exercise which established the key design criteria for the new facility. Following a competition, world leading architects Foster + Partners were appointed by the developer to produce a scheme, and subsequently to prepare a planning application.
10. On 3 December 2015 and 16 March 2016 Cabinet provided authority for the Council to enter into a Pre Planning Agreement (PPA) with Rightacres Property Ltd relating to design and site preparation costs necessary to

bring forward delivery of the Bus Interchange in accordance with the Council's programme.

11. The agreement essentially provided an underwriting of costs up to an agreed cap to enable the developer to incur costs and progress the development in advance of having in place an agreed funding package with the Council. This acknowledged that costs would be reimbursed in the event that no agreement was in place by 30 June 2017. At its meeting on 28 September 2016 Cabinet agreed for the cap to be increased to cover additional design costs relating to the preparation of a planning application for the development.
12. Planning consent was granted on 1 March 2017, subject to the completion of a Section 106 Agreement. The scheme comprises of a Bus Interchange, including a cycle hub and ancillary retail units on the ground floor; 225 car parking spaces and an interchange lounge on the first floor (to provide a potential future link to the Central Train Station); a Private Rented Sector (PRS) development of 195 units on the Wood Street elevation; and 120,000 sq ft of grade A* offices at the Saunders Road end of the development. An illustration of the scheme is provided at Appendix 1.
11. Site preparation works were concluded in June 2017. These primarily included the relocation of businesses from Marland House; the demolition of Marland House; and the demolition of the Wood St NCP Car Park. Details of the costs associated with design, planning and site preparation are provided in Confidential Appendix 2.
12. The Council has recently reimbursed the developer for costs expended up to the value of the agreed cap. The developer has incurred further costs relating to design, planning and site preparation at risk and the Council is now required to settle these costs. The cost incurred by the Council for land assembly and design, planning and site preparation will be apportioned against each key element of the development in the final development appraisal as outlined in Confidential Appendix 3.
13. An allocation of £20 million has been included in the Council's Capital Programme for the delivery of the Bus Station element of the Bus Interchange building. This is dependent on securing capital receipts to this value from the sale of leasehold interests in the council owned land holdings within the Central Square development. Details of the costs of land assembly for the Bus Interchange building and the associated capital receipts are provided in Confidential Appendix 4.

Key Funding Challenges

14. It has become increasingly apparent that the Council's decision to deliver the new Bus Interchange project on the site of the former Marland House and Wood Street NCP Car Park has created significant funding challenges. In particular the decision has created a significant land premium for the development; it has limited the potential of capital receipts that can be generated from what would otherwise be a prime development

site; and has added costs to the construction of the overall development scheme. Whilst the developer remains committed to delivering a solution, these issues have created a very difficult financial equation to resolve.

15. At the outset it was the intention to recover all of the costs of land assembly through capital receipts generated from within the development site. This aspiration took account of the fact that the purchase price of existing buildings such as St David's House and Marland House was in excess of the value of the plots as development sites, but reflected the realistic assumption that through a comprehensive regeneration scheme and major investment in public realm improvements across the entire site, an uplift in land value would be achieved to off-set the premium required to purchase buildings. This has largely been achieved. However, the specific costs associated with the purchase the Wood Street NCP Car Park has placed a major burden on the Bus Interchange development (Confidential Appendix 4).
16. In addition to the specific costs outlined above, the Wood St NCP Car Park was also the subject of existing parking leases that needed to be resolved in order to enable demolition of the building. This has meant that the development proposal for the new Interchange building also needs to incorporate 225 car parking spaces. The nature of the site and the mix of uses within the development has made the provision of this car parking expensive to deliver. In particular, ground floor bus station limits the number of columns that can be used in construction to minimise the obstruction of bus movements. This dramatically increases the cost per space of providing car parking. The cost of land, and the cost of car parking has made the financial equation extremely difficult to resolve.
17. Furthermore, the agreement with the developer established in 2013 assumed a market driven development designed to allow market demand to drive end use on plots across the scheme's masterplan. However, as the scheme developed, the Council's aspirations for the building has effectively created constraints on the developer that have prevented the pursuit of high yielding opportunities involving student accommodation and budget hotels. In order to expedite the development it is recommended that Cabinet reverts to the original approach and allows the developer to pursue market driven opportunities.
18. It is the norm for any developer of office buildings to wait to secure tenants for some if not all of the building before committing to a construction contract. This approach mitigates risk, and provides the developer with a clear understanding of the value of the building before incurring significant costs. This is because the value of office buildings relates to the strength of covenant of the tenant(s) and the terms upon which they are secured. The Cabinet's preference has, until recently, been for the space above the Bus Interchange building to be predominantly offices, which has meant that until a proportion of the space is let, the development has been unable to proceed.

Funding Proposal

19. The developer has now submitted a proposal to the Council setting out a financial framework for delivering the Bus Interchange development based on a market driven solution outlined in Confidential Appendix 5. The developer is proposing to take advantage of current market opportunities to maximise the value of the development and to maximise the capital receipts payable to the Council. In particular, the developer is seeking to secure a student accommodation scheme at the Wood Street end of the development to replace the consented scheme for Private Residential Sector (PRS) units. The developer will continue to pursue an office scheme for the Saunders Road end of the development but will only commence development of the scheme once over 50% of the office area is let. In terms of potential office occupiers, the Council and Rightacres have been pursuing a number of live enquiries which have the potential to be secured over the next few months. In the event that office tenants are not secured within a reasonable timescale, the developer is proposing to extend student accommodation across the whole of the building. It is understood that any change of use or changes to design will require a further planning application.
20. The Developer's Proposal suggests that the Council completes the full land assembly by acquiring the remaining Saunders Road Car Park site from Network Rail. The developer would then pay a premium to the Council (which will include a share of the pre-development costs) to acquire a long leasehold interest in the whole site, with the Council retaining the freehold interest. The Council would then lease back the bus station element of the building for a peppercorn rent based on payment of an up-front premium equating to the cost of construction of the bus station element. The Developer's Proposal establishes a financial envelope for delivery of the bus station which is more or less in line with the resources available to the Council and the capital programme allocation. Confidential Appendix 3 explains the Council's affordability envelope. However, it must be noted that the timing of delivery of a bus station facility remains dependent on securing appropriate tenants for the building.
21. In addition to the above, Cabinet should note that the developer's proposal also confirms there is no contribution required from the Council towards the provision of car parking spaces. The developer will also be able to deliver the anticipated contribution towards the broader Central Square public realm improvement scheme as well as the specific extension of the scheme around the Interchange building (see Appendix 7).
22. The costs provided for the construction of the bus station element at this stage are high level and subject to independent review by an external cost consultant. Whilst technical fit-out has been excluded from the proposal, further work is required to confirm the exact extent of internal fit-out that is included in the developer's proposals. In regard to technical fit-out costs, the Council has made a bid to Welsh Government for a contribution towards these costs and the costs of highways improvements that will need to be made to the road network in the area surrounding the bus station to improve access for buses and pedestrians. The Council's

financial strategy is reliant on a contribution being realised from Welsh Government, as set out in Confidential Appendix 3.

Scrutiny Consideration

23. This report was considered at a joint meeting of the Economy & Culture and Environmental Scrutiny Committees on 18 July. The letter from the Chair is attached at Appendix 8.

Reason for the Report

24. To seek in-principle agreement from Cabinet to the proposed funding proposal from the developer for delivery of the Bus Interchange development and to secure delegated authority to conclude arrangements to deliver the development within the Council's financial envelope including settling outstanding design, planning and site preparation costs.

Financial Implications

25. The existing Capital Programme includes an allocation of £20 million for the 'Delivery of Central Square development including a new Integrated Transport Hub', which is to be fully funded by capital receipts and s106 contributions associated with Central Square. In addition, £3.739 million of the Central Square Public Realm budget is currently reliant on resources generated at Central Square.
26. The Central Square developments are being progressed on the basis that schemes are fully self-financing from land and s106 receipts and any deviation from this base assumption could impact on the council's financial resilience strategy and its ability to support other major projects and initiatives being progressed by the council at this time.
27. In March 2016, Cabinet authorised the completion of a pre-planning agreement. This committed the Council to underwriting costs incurred by the contractor up to a specified maximum figure for the first phase of works. In September 2016, an additional Cabinet authorisation was received to include the second phase of works, and therefore increasing the specified maximum figure that the Council will underwrite. On 5th July, the Director of Economic Development exercised the delegated responsibility granted in these Cabinet reports to make payment to the contractor for the specified maximum figure for these phases of works.
28. The details of these costs are contained within commercially confidential appendices to this report. An additional set of financial implications have therefore been set out in confidential Appendix 6, which should be considered in conjunction with this report.
29. The attached report provides details of recent progress on the Interchange development including current high level proposals submitted by the developer. The report confirms that the developer has been paid for pre-development work up to the cap previously agreed by Cabinet in September 2016. The Developer has though continued to incur additional

costs on these activities, at his own risk, to values over and above the previously agreed cap. The developer is now expecting the Council to reimburse these additional costs and the attached Cabinet report is seeking authority to make this additional payment to the developer relating to design, planning and site preparation. The payment of this additional sum will take Interchange expenditure above its approved Capital budget for 2017/18 and will require budget to be brought forward from 2018/19. The element of these pre-development costs that relate to the Commercial elements of the scheme will be subsequently passed back to the developer.

30. The Interchange is due to be fully funded by capital receipts and s106 contributions associated with Central Square. However, these capital receipts will not be realised in advance of these pre-development payments being made. This represents a short term funding issue for the council with revenue expenditure implications either through short term borrowing costs or reducing income from Treasury activities.
31. The financial implications of incorporating the car park in the development are highlighted in the report in terms of reducing the commercial value from the site and the additional expenditure from the engineering solution required to incorporate the car park on the first floor.
32. The report recommends reverting to a market driven approach for the commercial space within the development. Maximising development value will minimise, but not eliminate, the funding required from the Council to deliver the new Bus Transport Interchange.
33. The current development proposal is conditional on securing sufficient tenants to fill the commercial space. Although the developer is confident of finding tenants there is a risk of a delay to the development if sufficient tenants are not found to cross this threshold. If this delay were to materialise, this could result in the scheme needing to be redesigned which could have a detrimental impact on the delivery, timeliness and costs of the scheme.
34. At this stage the construction costs included in the proposal are high level assessments which brings the risk that costs could increase as more detailed proposals are developed. With the financing sources for the Interchange being largely fixed this would present funding implications that would need to be addressed if the proposal was to proceed.
35. The Developer's Proposal suggests that the Council completes the full land assembly by acquiring the remaining Saunders Road Car Park site from Network Rail. Although a price has been agreed with Network Rail for the land in Saunders Road, this land has yet to be acquired which brings with it associated risks.
36. The report acknowledges that technical fit-out and junction improvement costs will be required but are outside of the scope of this development. The expectation is that the Council will rely on Welsh Government contributions to fund these works but this funding is not currently

confirmed which exposes the Council to the financial risk that it will need to step-in and fill any fit-out funding gap. The lifecycle costs of the council operating the bus station will also need to be considered alongside the more detailed development proposals that will subsequently follow.

37. Given the specialist nature of this development the Council will need to engage the Professional Advisors to ensure that the proposals presented by the developer are deliverable and represent VFM. Adequate budget to engage these advisors will need to be identified.

Legal Implications

38. The Council is required to be mindful of its fiduciary duty to its Council taxpayers and to ensure value from money in regard to its land acquisitions and disposals. The Council's Procedure Rules for the Acquisition and Disposal of Land require the advice of a professional valuer to be taken at all stages. The intention is to ensure that due probity and accountability can be demonstrated at all times and value for money achieved. Similarly the Council will be required to ensure value for money in regard to the delivery of public infrastructure, fit-out and operating arrangements and will require detailed cost consultants' advice in those regards. The appendices to the report provide relevant information for consideration at this stage. More detailed information will need to be considered in advance of the exercise of delegated powers.
39. Changing market conditions impact on the saleability and rental income from commercial premises. If disposals are not achieved promptly then holding costs can occur alongside an inability to service project funding. Value for money is an essential element in demonstrating that the Council is not providing unlawful State Aid to developers, funders, occupiers and operators and that it is complying with its fiduciary duty to the local taxpayers.

RECOMMENDATIONS

The Cabinet is recommended to:

- (1) Allow the developer to maximise capital receipts for the commercial floor space within the Bus Interchange development by allowing end use to be driven by market demand.
- (2) Delegate authority to the Director of Economic Development in consultation with the Cabinet Member for Investment & Development and the Cabinet Member for Finance, Modernisation and Performance, the Section 151 Officer and the Monitoring Officer to:
 - (i) Negotiate and conclude a final agreement with the developer subject to the financial envelope outlined in Appendix 3 for the delivery of the Bus Interchange project and appropriate external advice.

- (ii) Settle outstanding design, planning and site preparation costs as outlined in Confidential Appendix 2 subject to independent verification of costs.
 - (iii) Acquire the Saunders Road Car Park site owned by Network Rail to complete the land assembly as outlined in this report, subject to independent valuation.
- (3) agree that budget be brought forward from the approved 2018/19 Capital programme into 2017/18 budget to meet the pre planning and land assembly costs outlined in the report.

NEIL HANRATTY

Director

21 July 2017

The following appendices are attached:

Appendix 1:	Illustration of Consented Scheme
Confidential Appendix 2:	Design, planning and site preparation costs
Confidential Appendix 3:	Bus Interchange Financial Strategy
Confidential Appendix 4:	Bus Interchange Land Acquisition and Disposal
Confidential Appendix 5:	Developers Proposal
Confidential Appendix 6:	Confidential Financial Implications
Appendix 7:	Plan of Central Square Public Realm Scheme
Appendix 8	Letter from the Joint Economy & Culture and Environmental Scrutiny Committee