The City of Edinburgh Council

10.00am, Thursday, 1 May 2014

The Edinburgh 12 - Progress Report

St James Quarter Regeneration Accelerator Model

Item number	8.6
Report number	
Executive	
Wards	City Centre

Executive summary

The Edinburgh 12 is a Council led initiative intended to unlock strategically important gap sites within the city. These 12 proposed developments have potential to deliver:

- Gross Value in excess of £2.14 billion
- Up to 20,000 FTE jobs and 28,000 construction jobs
- An estimated 1.5 million sq ft of Grade A offices
- Over 1500 residential units.

Prominent among the Edinburgh 12 is the **St James Quarter** which is a part of the city currently in long term physical decline. This paper sets out the rationale for public sector intervention in the regeneration of the Quarter and proposes a new investment model referred to as the **Regeneration Accelerator Model** (RAM).

This model represents a partnership between the City of Edinburgh Council, Scottish Government and TIAA Henderson Real Estate, the owners of the St James Quarter. The new model will secure £850m of inward investment for Edinburgh, unlock 42,500m^2 of high-quality retail space, 2,300m^2 of grade A office space, a 210-bedroom five-star hotel, a 152-bedroom four-star hotel, a 55-bedroom apart-hotel, a theatre, restaurants and 138 residential units.

Links

Coalition pledges	P15, P17, P29
Council outcomes	CO7, CO8, CO19
Single Outcome Agreement	SOA1

Report

St James Quarter Investment Model

Recommendations

1.1 It is recommended that the Council:

- Confirm the rationale for public sector intervention at the St James Quarter as part of its wider focus on the Edinburgh 12.
- Approve a new financing model to unlock this development.
- Approve £61.4 million in new prudential borrowing which would be maintained and repaid over up to a 25 year period through a combination of public and private sector investment.
- Approve Council officers taking forward detailed negotiations on this proposed funding mechanism, including setting up a new partnership board to oversee the development of the Quarter.
- Agree the three performance targets set by the Scottish Government as part of the condition for their annual contribution to the model.
- Agree a new retail and hospitality skills academy be established to provide training support for targeted employment opportunities for those furthest away from the market.
- Agree a permanent new Shop Mobility scheme be included within the programme of works.
- Agree new charging points for electric vehicles be included within the programme of works.

Background

2.1 Launched in 2013, the Edinburgh 12 is designed to unlock of 12 strategic sites in the city. Prominent among these is the St James Quarter. The Quarter occupies a strategic location within the city and its redevelopment is a unique opportunity to regenerate the wider area.

Main report

Introduction

3.1 Redevelopment at the Quarter has long been anticipated because it would stimulate significant additional international spend and strengthen the nation's capital as a visitor attraction.

3.2 The proposed mixed-use development includes high-end retail, leisure opportunities and a five-star hotel, all within a well-designed, high-quality city centre setting. When combined with the new tram route from Edinburgh Airport to St Andrew Square, the proposition becomes ever more compelling.

3.3 As a result, in January 2014, a draft business case for public intervention in the redevelopment of the Quarter was submitted by City of Edinburgh council officers to the Scottish Government. This paper sets out the principles of a new funding mechanism to unlock this stagnating area of the city. The paper asks for Council approval to proceed as proposed. This innovative new funding model hereinafter is referred to as the Regeneration Accelerator Model (RAM).

3.4 The Regeneration Accelerator Model (RAM) model is based on a £61m investment in enabling infrastructure. This would be maintained and repaid by an annuity payment by the Scottish Government and the owners of the Quarter TIAA Henderson. The borrowing cost per annum would be £4.77m and would be fully met by new funding streams to the Council, provided specific targets are met. The project will create significant overall growth to the economy, thousands of new jobs for Edinburgh and restore city competitiveness.

3.5 If agreed, the Council is also asked to approve officers entering detailed discussions with officials from the Scottish Government and the owners of the Quarter, so as to refine and agree the operation of the new model. An outline timetable for delivery of the regenerated area is set out at 3.29.

Context for the Scheme

3.6 Edinburgh plays a central role in linking Scotland to the world economy. In 2012, the city accounted for 57% of international visitors, 37% of all international students and 27% of foreign nationals registering to work in Scotland. The Quarter occupies a strategic location within the city. The new development will draw custom from the city's main rail station (used by over 22 million people each year) and the new tram service, initially expected to be used by over 4.5 million passengers annually.

3.7 Outline planning consent was granted in June 2009 (Application Ref: 08/3361/OUT). The planning consent is for redevelopment and refurbishment including demolition works and new buildings to provide mixed use development. Discussions on the Approval of Matters Specified in Conditions (AMC) are taking place.

Employment & Skills Academy

3.8 As part of the plans, a regenerated Quarter would provide significant numbers of new full and part-time jobs, creating opportunities for those being supported through the Council's employment services. The Quarter would also be an important source of employment for those needing additional help to enter the labour market; people such as school leavers, the young and the long-term unemployed, as well as residents in areas of multiple deprivation, or those experiencing systemic barriers to work. Targets for recruitment include North Edinburgh and Craigmillar. Construction work associated with the regeneration will also create many new apprenticeships. The Council's Edinburgh Guarantee would be an important supporting programme.

3.9 In response, it is proposed that a new retail and hospitality skills academy be established to provide training support for these target groups. The academy would be a partnership between the developer, TIAA Henderson, the Council and other key agencies, including Capital City Partnership, Jobcentre Plus, Skills Development Scotland and Edinburgh College.

3.10 TIAA Henderson has agreed in principle to invest up to £500,000 to set up the academy. Although subject to more detailed negotiations, this academy is envisaged to be for the provision of high quality training space and capital equipment. The Council would provide staff through the Economic Development Service to run the academy on a day to day basis. This type of facility has successfully been set up in both Liverpool and Birmingham, both of which are competitor cities for the tourism pound.

Wider Benefits

3.11 This report suggests that there will be other beneficial catalytic effects to the redevelopment of the Quarter. For instance, regeneration will have a positive impact on the value of residential and commercial properties in streets adjoining the area and will also stimulate economic activity.

3.12 The new Quarter would complement the proposed "Registers Lane" development (at feasibility stage), which seeks to create a new mix of uses to the south west, between Multrees Walk and Princes Street. Establishing a new thoroughfare between St Andrew Square and the Quarter would deliver enhanced public realm. This feasibility study was commissioned in partnership with the private sector and approved by Economy Committee in 2013.

Why intervention is required

3.13 Developments of this scale by the private sector require an appropriate Internal Rate of Return (IRR). Based on a review of the project's finances, and subject to public-sector support, the project's required IRR is considered to be in line with other developments. To unlock £850m development investment, TIAA Henderson need to ensure its investors receive “normal” (market) returns from its investment. There is a convincing case that without support for key enabling infrastructure, inward investment on this scale and quality would not happen and the area will continue to decline.

Infrastructure Investment Plan

3.14 The Council has identified a programme of infrastructure which would provide the necessary impetus to take the redevelopment forward. These include improvements to the physical environment at James Craig Walk, designed to increase the accessibility, permeability and the user experience of the areas; new public realm at Picardy Place, together with the provision of a multi-modal transport interchange at the junction of Leith Walk, Leith Street & York Place. A new energy centre designed to provide power, heat and cooling to the development and, potentially, the wider area will also be constructed. The value of the new infrastructure is projected at £61.4m.

3.15 Redevelopment of the Quarter provides an opportunity to complement the transport improvements that will be delivered through the Leith Programme. With additional funding from Sustrans Scotland, the programme will deliver major improvements for pedestrians and cyclists for the entire length of Leith Walk. The design has been informed by an analysis of the streets functions and its importance locally, as well as across the city as a major connector.

3.16 Picardy Place is a key travel route connector so there is a real opportunity for the Council to combine Leith Programme design features for active travel, thus joining up schemes in Leith Walk, the City Centre and Picardy Place.

Economic Impact

3.17 A Council commissioned economic impact assessment indicates that proposed public sector support would unlock 42,500m^2 of high-quality retail space, 2,300m^2 of grade A office space, a 210-bedroom five-star hotel, a 152-bedroom four-star hotel, a 55-bedroom apart-hotel, a theatre, restaurants and 138 residential units.

3.18 Between 2015 and 2040, the redevelopment of the Quarter would also support 2,300 permanent jobs and a net increase in the gross value added of Scotland of about £644 million, an average of £25 million per annum.

Delivery Process

3.19 Subject to Council agreement and based on an appraisal of the procurement and state aid regulations as well as discussions with the developer, an in-principle agreement has been reached. This would allow, to the extent the public works fall within the relevant legislation, the publicly funded work packages to be procured by the developer within OJEU, the procedural framework. Council officers would continue to appraise the situation as the detail of the work packages evolves so as to ensure no procurement regulations are breached. It is proposed that reimbursement of these costs to the developer, would only take place on practical completion of the whole project when new business rate revenues are being generated.

Proposed Funding Mechanism

3.20 Given current fiscal constraints, the Council is unable to shoulder the cost of required borrowing within existing resources. A collaboration with the Scottish Government and Scottish Futures Trust on the newly developed **Regeneration Accelerator Model** is therefore recommended as the preferred option.

3.21 This innovative new model of financing proposes a total borrowing of £61.4 million which would require annual repayments of £4.77 million over a 23 year period. This is 2 years shorter than the proposed 25 year term of the model.

3.22 The proposed funding mechanism itself would be a partnership between the Scottish Government, the Council and the Developer. Council borrowing costs would ultimately be completely offset by new income streams, subject to proposed targets being achieved.

3.23 As part of the negotiations with the Developer, it is anticipated that an Energy Centre would generate an income of £150,000 per annum. Furthermore, TIAA Henderson has agreed in principle to provide for an additional £350,000 of the costs of borrowing per year (for the agreed term). These contributions would effectively reduce the annual funding requirement to £4.27m.

3.24 It is further proposed that the remainder of the annuity payment be tied to the achievement of the following deliverables, resulting in three separate income streams to cover the remaining funding gap of £4.27m:

I. a predetermined uplift in rateable value derived from within the St James Quarter itself (55%);

II. an uplift in rateable values from within a wider area as a result of the catalytic effects of the new Quarter (25%); and

III. the achievement of employment and training targets to support the long term unemployed and the harder to reach groups and areas (20%).

3.25 The Scottish Government contribution of £4.27m is linked to the delivery of these three outcomes, over four years initially from 2018. However the timeframe will be reviewed if the targets are not met in this initial period. The Government's contribution is also linked to a proportional percentage performance against targets. So, for instance, if 80% of the respective targets are achieved, the Scottish Government will only provide for 80% of its contribution.

3.26 The risk of not meeting the above targets would sit with the Council. However, should the Council be unable to achieve these objectives because of unprecedented market changes, it is proposed that there is a renegotiation of the previously agreed long stop dates. This would allow the Council to realise a full funding commitment over the life of the project.

3.27 Another important feature of the model is that overall funding by the Scottish Government would be capped at £97m. This would not increase over the life of the project. Any reduction in borrowing, due to lower than forecast infrastructure costs would be reflected in a corresponding reduction in the annuity payment from the Scottish Government and TIAA Henderson.

3.28 As an incentive for the developer to drive down the cost of the supporting infrastructure, for the first £700,000 of any reduction in the annuity payment, there is a proposed even split in the reduction of contributions between the Scottish Government and TIAA Henderson. This would roughly equate to the first 15%, equivalent to first £9 million reduction in infrastructure costs. At this point, all future reductions in the cost of infrastructure would also result in a reduction of the annuity payment for the Scottish Government alone. However, any increase in borrowing requirement, or change in interest rate above 5.5% assumed, would be met by the Council alone.

3.29 Finally, TIAA Henderson has agreed in principle to share any surplus above normal returns on the wider investment. This surplus or “super profit”, should it occur, would be split between the public and private sector. The exact mechanism and split would be determined in more detailed negotiations between the Council with the Scottish Government and the Developer.

Governance

3.30 It is proposed that an Executive Group be set up comprising senior representatives from the Scottish Government, the Council, the Scottish Futures Trust and the Developer TIAA Henderson to govern the overall delivery of the project. The Council would dedicate specific management resource capacity to the programme. The structure of the partnership would also ensure the developer successfully undertakes all development works in accordance with an agreed timetable. As part of the governance, the new board would be set up to oversee the development. This would include Council Officers, the Scottish Government and TIAA Henderson Real Estate.

Next Steps

3.31 Approval of this proposal has been granted by Scottish Government in order to unlock the Quarter. This is conditional on Council agreement to the financing mechanism described above.

3.32 The following timeline will be required to meet the projected delivery schedule:

- Formal approval by the Council – May 2014
- Legal Agreement with Scottish Government – May / June 2014
- Legal Agreement with TIAA Henderson – June 2014
- Publication of CPO to acquire third-party interests – June 2014

- Construction start – June 2015

Measures of success

4.1 The high quality redevelopment of an important strategic location within the city.

4.2 The employment and training target is 1,200 training places and 600 people employed from hard to reach groups in the first two years of operation.

4.3 A new retail and hospitality skills academy.

4.4 A new energy centre.

4.5 A permanent new shop mobility scheme.

4.6 New car charging facilities for electric vehicles.

Financial impact

5.1 This paper proposes total Council borrowing of £61.4 million which would require annual repayments of £4.77 million over a 23 year period.

5.2 Repayment would be made through a partnership with the Scottish Government (providing an annual grant of £4.27m), the Developer (annual repayment of £350,000) and revenue at the Energy Centre (set at £150,000.)

5.3 There would be no annual revenue cost for the Council, assuming that proposed targets are achieved.

5.4 Any increase in the borrowing requirement, or change in interest rate above 5.5%, would be borne by the Council.

Risk, policy, compliance and governance impact

6.1 As stated in the body of this paper, the Scottish Government contribution is linked to the delivery of three target outcomes. These would be measured over four years initially from 2018. However the timeframe will be reviewed if the targets are not met.

6.2 The Scottish Government's contribution is also linked to a proportional percentage performance against targets. So, for instance, if 80% of the respective targets are achieved, the Scottish Government will only provide for 80% of its contribution.

6.3 The risk regarding movements in interest rates will be managed as part of the Council's Treasury strategy and a buffer of 1% compared to current long-term borrowing rates has been built into the business case.

6.4 A turnkey arrangement with the developer for the delivery of the council’s infrastructure is proposed which would result in agreed payment not being made until the specified assets were provided.

Equalities impact

7.1 A newly developed St James Quarter would provide employment for those needing additional help to enter the labour market; people such as school leavers, the young and the long-term unemployed, as well as residents in areas of multiple deprivation or those experiencing systemic barriers to employment.

7.2 A new retail and hospitality skills academy would be established to provide training support for these target groups.

7.3 There is also an aspiration to maintain the proportion of hard to reach target groups at 25% of all employment at the Quarter. This will be monitored on an ongoing basis.

Sustainability impact

8.1 Any negative impacts would be offset by a much more energy efficient development than exists in the current aging buildings. A combined, heating, cooling and power centre is proposed as part of the development as is wider access and shop mobility. There will be electric charging points, extensive facilities for cyclists, photovoltaic panels, solar tubes and a city car club. The new tram system will form an important public transport component. The mixed development Quarter also reflects Council aspirations to encourage city centre focused retail, commercial and leisure activity.

Consultation and engagement

9.1 Consultation through regular Visitor and Public Surveys reflects a desire to see continual focus on high quality development in the city centre. If approved, the programme would also include extensive consultation with local residents and businesses, as stipulated in the planning and construction requirements.

Background reading / external references

The St James Quarter Redevelopment Business Case, 2014.

The St James Quarter Redevelopment Supplementary Funding Proposal, 2014.

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Links

Coalition pledges	P15 - Work with public organisations, the private sector and social enterprise to promote Edinburgh to investors P17 - Continue efforts to develop the city's gap sites and encourage regeneration P29 - Ensure the Council continues to take on apprentices and steps up efforts to prepare young people for work
Council outcomes	CO7 - Edinburgh draws new investment in development and regeneration CO8 - Edinburgh's economy creates and sustains job opportunities CO19 - Attractive Places and Well Maintained – Edinburgh remains an attractive city through the development of high quality buildings and places and the delivery of high standards
Single Outcome Agreement	SO1 - Edinburgh's Economy Delivers increased investment, jobs and opportunities for all
Appendices	