SECTION 3:
FINANCIAL ROBUSTNESS

Confidential

SW2 Enterprise Centre: Final Tender

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KAJIMA

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3.1 FINANCIAL DELIVERABILITY

INTRODUCTION

The project Maximum Commitment is £63.5m (excluding VAT and finance of £0.9m) with forecast peak funding of £31.3m in Q2 2017. This includes all returns to Kajima (including our 7.5% Out-turn Risk Return, which is fully at risk against, inter alia, price increase, delay and contractor default).

The Maximum Commitment is protected by Kajima's wrap-around guarantee equivalent to 15% of the Maximum Commitment, equivalent to £9.5m.

FUNDING STRATEGY

Kajima's proposal is for the Council to fund the majority of the project from surplus site sales. For the interim financing, the Council will either finance from capital or take advantage of the favourable terms offered by Public Works Loan Board borrowing. This strategy has been worked up with the Council during dialogue and to reduce to a minimum the financing costs of the development and improve viability.

The Council retains total flexibility of funding options and can, at their sole discretion, fund through alternative means. Kajima also remain open to the principle of project finance which, once design has been developed, would be more feasible (although would subject additional costs to the project).

Funding will fall into two elements:

Pre-Construction Funding

During the conditional stage of the Development Agreement, Kajima will submit single monthly invoices against our pre-approved design cost expenditure. This will be based on the design development budget submitted in Appendix A3.1 and in the submitted model.

We expect this budget to be subject to regular review and amendment with the Council in terms of timings of payments and quantum, within the scope of costs submitted. Payments are subject to prior approval by the Council if they are not contained within the heads of costs. The budget includes a design contingency equivalent to 1.5% of build costs that allows the Council to act upon our recommendations without increasing the design budget. Unspent contingency remains with the Council and will not form part of the final Maximum Commitment.

A statement of costs will be submitted on a monthly basis and, subject to the Council agreement, paid to Kajima.

Until Viability is achieved under the Development Agreement, the Council are not committed to spend monies beyond the design stage, and costs up to this point are effectively capped at £5m.

Construction Funding

Once the Development Agreement is unconditional and construction starts, the Council will fund the development up to the extent of the Maximum Commitment. Invoices will be submitted to the Council on a monthly basis against a valuation of works undertaken provided by the Employer's Agent. These sums will exclude any retention agreed as part of the Contract, which will fall due on the first anniversary of Practical Completion subject to any deductions.

The Maximum Commitment the Council will be exposed to at completion of development (excluding finance costs of £0.9m) is £63.5m including all returns to Kajima, but excluding VAT and finance costs. In the event that costs are in excess of this sum (as varied prior to the unconditional date in line with the Development Agreement), and Kajima's Out-turn Risk Return has been fully eroded, additional costs up to 15% of the Maximum Commitment will be covered by Kajima's guarantee.

Sources of Council Finance

Save for the forecast deficit of £8.98m (and subject to any improvements down to savings identified in Section 3.2), the project will be backed off against the receipts from surplus site sales.

Kajima's proposal to the Council will deliver fully committed sales contracts on each of the Council's surplus sites as a Condition Precedent to the Development Agreement going unconditional.

The timing of completion of these sales is driven by vacant possession of each site, which is derived in turn by the development programme for the Town Hall and the Enterprise Centre.

The exact timing of sales remains subject to agreement with the Council after a review of occupational requirements. Our initial assessment of expected operational needs has been developed into a draft programme of site sales as follows:

Prior to Planning

Wanless Road: Target sale within 3 months of Development Agreement to fund planning costs. (Q1 2014)

After Start on Site

Hambrook House: First major site sold, to permit development concurrent with the SW2 Enterprise Centre. (Q1 2016)

Upon Occupation of Enterprise Centre

Ivor House: Youth Offenders Service and IT department transferred to the new civic offices. (Q3 2017)

Phoenix House: Occupants transfer to the new civic offices. (Q3 2017)

Upon Re-Occupation of Town Hall

Olive Morris House: Customer Service Centre transferred to new Town Hall facility and occupants transfer to the Town Hall and new civic offices. (Q1 2018)

These timetables remain subject to final agreement. Earlier receipts may be possible subject to a short term leaseback to the Council. The assumption would be that the income payable in rent is offset against a higher sale value and would be neutral, albeit allow earlier capital receipts.

The graphs below illustrate the flow of cash throughout the project, including all costs and revenues and are extracted from the model.

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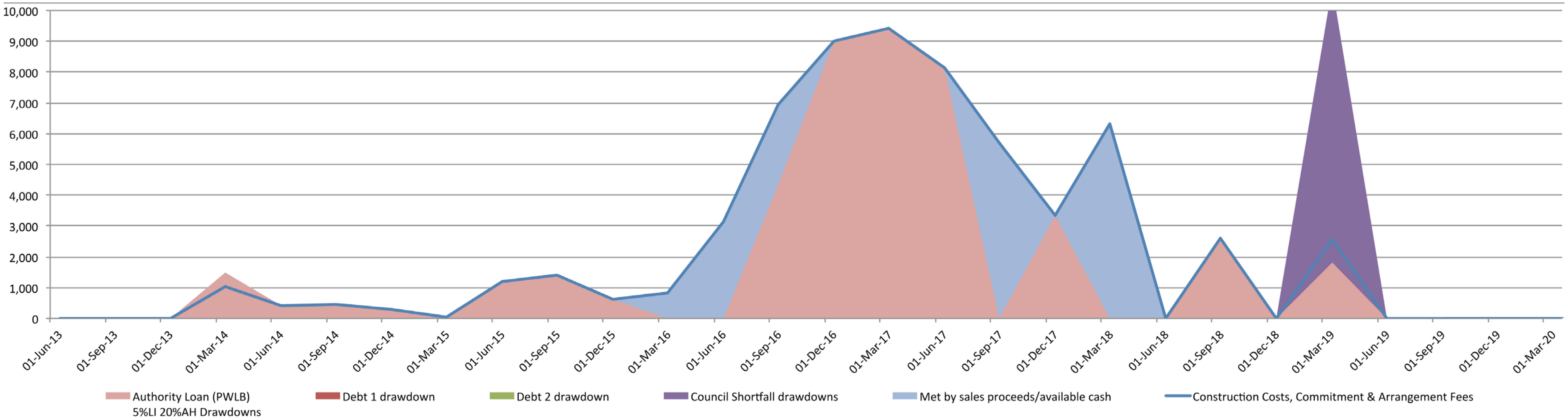
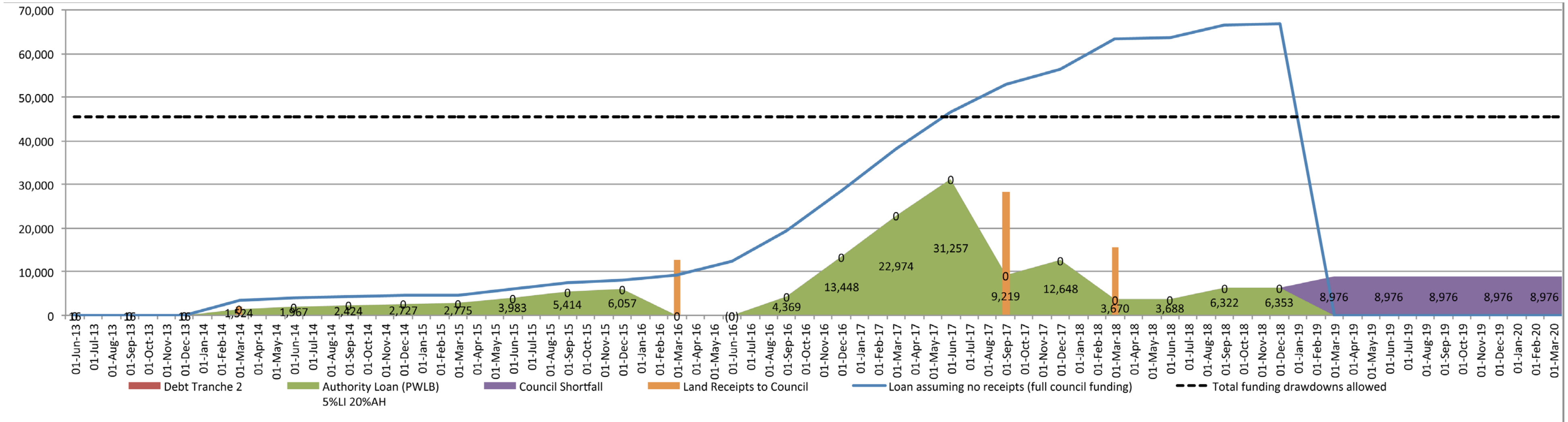


Construction cashflows



Debt balances

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Kajima Financing Option

An alternative funding basis is for Kajima to agree with the Council to enter into a finance arrangement. This type of arrangement is one Kajima is comfortable with in principle, although would clearly need to be considered in detail between the parties.

Kajima would commit a proportion of equity, typically 10-20% but dependent on the gearing secured and quality of the guarantee offered, with the remainder of the Maximum Commitment funded by way of a construction finance loan with the benefit of the Council's shortfall funding guarantee originally offered.

Kajima would expect a priority return on its equity of 10-12% depending on the quantum of the loan and quality of the guarantee offered. We have had preliminary discussions with SMBC Bank, with whom we have an extremely strong, long and successful relationship, and they would be interested to explore this in more detail if appropriate. A letter to this effect is attached in support of our submission at Appendix A3.2.

Based on our analysis, this would prove very expensive to the Council. By seeking PWLB borrowing the project value for money is materially improved by approximately £4m.

In any case, third party funding would require the Council to provide significant guarantees in order to raise the senior debt, and therefore there is strong logic for the project to be funded through prudential borrowing or reserves, backed by surplus site receipts.

Sale & Leaseback Option

In addition to the above methods of financing the development, a more radical approach would be to seek to secure institutional funding for the new civic offices. The principle would be that the Council enter into a lease for the new civic offices at an acceptable rent for a 25 year term with inflation linked rent increases and sell the asset to an institution. This would have the potential to generate sufficient capital value to pay for all construction work and associated costs and leave the surplus sites in the control of the Council.

SALES TO THIRD PARTIES

Kajima propose that all surplus land be sold to third parties on an openly tendered basis to capture best value for the Council.

If sold up front, the site values would be discounted by a number of factors:

- A premium profit margin to reflect the time, cost and risk of securing planning permission and time to deliver to market;
- The opportunity cost of carrying the capital commitment to purchase the sites on their balance sheet for 4-5 years without being able to develop or trade the sites on at a profit until the Council's accommodation has been built;
- The double application of Stamp Duty Land Tax insofar that the sites would be traded at least once before being built;

Such a bulk discounted site sale does not offer best value for money to the Council. Given that the majority of the sites are already owned by the London Borough of Lambeth, there is no additional risk in holding onto this land until its value has been enhanced with the help of Kajima's management.

Kajima's role will be to act as the manager of the process so as to maximise the values of these assets. Our scope of obligations in relation to the surplus sites is set out in detail in the Development Agreement, although the principle is simple. Kajima will employ, on behalf of the Council, the design team for the surplus sites to create value through the design and planning process, removing the risk of unfavourable planning, and then market and sell to third parties prepared to pay the best price for each site.

Kajima will manage the timing of sales to achieve the Council's continued occupational and operational needs. In the process the Council will benefit from a rising London market, which is explored in detail in Section 3.2.

This offers Lambeth a significant number of benefits for no additional material risks:

- Whilst there will be a cost to securing planning permission for each site, this sum is able to be capitalised against value and therefore is, in commercial terms, cost neutral.
- Once planning permission is secured, the value of the sites will increase to reflect the change in use from poor quality suburban offices to high quality town centre residential use.
- Each site can be sold independently to a special purchaser best motivated to acquire the particular type of development that best suits their business model.
- Once planning risk has been removed and the sites competitively tendered, the proportion of value given over to developer and contractor returns shrinks to reflect the lower risk, greater certainty, better fundability, more advantageous time horizon and competitive bidding.
- The core value generated by the sites will not be fettered by third party valuations which tend to favour developers/purchasers in a rising market and rarely capture true worth.
- The Council will benefit significantly from the re-energised London and Brixton housing market and negate any local criticism of selling before a period of sustained growth in values.
- The Council will capture 100% of the increase in value of favourable planning consent without the challenge of agreeing transparent and effective overage agreements with developers;
- The Council can choose when to make a final decision on Affordable Housing (AH) percentages that takes account of unresolved 'value vs policy' debates.

Kajima's proposal also ensures that the Council retains control of the viability condition insofar that there are no provisions within the Development Agreement to compel the Council to start on site if sufficient receipts from site sales have not been committed. The unconditional date, i.e. the date when all Conditions Precedent have been met and the physical build can commence, is within Council control.

GUARANTEES AND SUPPORT

Kajima Lambeth Regeneration Partnership (KLRP) will be incorporated upon selection and will be a wholly owned subsidiary of Kajima Partnerships Limited.

KLRP as developer is contracting with the Council to undertake all development obligations within the Development Agreement. This is in turn guaranteed by Kajima Partnerships Ltd (KPL) on a joint basis and provides a significant guarantee to the Council equivalent to 15% of the Maximum Commitment after all Out-turn Risk Return has been eroded.

Kajima Partnerships Limited is a substantial investor and developer of public sector assets in the UK with net assets of £30m. We are a wholly owned subsidiary of the Kajima Corporation, a major international contractor, developer and civil engineer with operations in over 45 countries and consolidated revenues of some £10bn a year. A copy of KPL's latest (2012) accounts is included in Section 0 in accordance with the ISFT requirements.

The guarantee is described in detail in Schedule 12 of the Development Agreement. It is a comprehensive guarantee that obliges Kajima as developer both financially and in terms of performance.

The triggers for this guarantee to the Council are based on non-performance and on increases to cost over the Maximum Commitment. The Council is able to take action against KPL as guarantor at the same time or in priority to taking action against KLRP.

A letter of support from Julian Rudd-Jones, Managing Director of Kajima Partnerships Ltd, is attached at Appendix A3.2.

TAXATION

We have assumed no irrecoverable VAT cashflows arise in relation to the SW2 Enterprise Centre development on the basis that expenditure is incurred by the Council and will be fully recoverable.

We have not assumed any capital allowances will be claimed on development undertaken by the Council, but may be available for future purchasers, through suitable elections being made at the appropriate time on the surplus site.

We have assumed that SDLT will be payable by purchasers of surplus sites.

We assume that, as a Local Authority, Corporation Tax and Capital Gain Tax do not apply to the disposal proceeds of surplus sites in the ownership of London Borough of Lambeth.

All of these assumptions are consistent with the Financial Model.

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PRIMARY MODEL OUTPUTS

Based on the analysis outlined in detail below, and illustrated numerically in the attached model at Appendix A3.3, the net position at the completion of all development and surplus site sales, including all costs for the Council in accordance with our Variant A bid (20% Affordable Housing), will be as follows:

Total Development Costs[1]	£63.507m
Other Council Costs[2]	£4.159m
Surplus site receipts[3]	£58.690m
Deficit	**£8.976m**

1. Costs calculated by QS and subject to detailed design development, collaborative value engineering and price tendering. Includes all costs, fees, developer returns.
2. Includes Hambrook option payment, costs of sales and finance costs.
3. Open Market Value assessment including 5% pa growth, subject to improvement through competitive marketing.

We have identified an additional £7.8m of potential value enhancements and savings below, excluding potential savings from the £4.5m IT budget.

Please note that any minor discrepancies in the figures in this section against the detailed cost plan and financial model are due to rounding and/or the conversion from square feet to square metres.

CIVIC OFFICES & TOWN HALL COSTS

Build Cost Summary

Davis Langdon (DL) have worked extensively and closely with the design team from the outset of the project to determine an accurate and detailed cost plan for the proposed development. The cost plan is attached in detail at Appendix A3.4 and is summarised as follows.

Category B Works

Our Variant Bid A allows for Category B works (including IT cabling and furniture) to the sum of £8.18m. This figure is a c.£10m discount to the £20.13m figure provided by the Council. Our bid also includes £4.5m for IT as required by the ISFT submission.

Build Cost Commentary

Davis Langdon have submitted a robust cost plan for this stage of design and allowed for sufficient contingency to reflect the level of detailed information available. Their assumptions are also derived from the Employer's Requirements provided by the Council and commented on as part of our submission in Appendix A2.3.

Davis Langdon have an unrivalled benchmark database on which to assess the cost plan

The costs have been benchmarked against similar projects (in terms of size, scope and location) currently and recently undertaken by Davis Langdon and Kajima for elements that are not yet defined by the design. DL have been involved in developing over 70 million square feet of office space in London over the last 12 years and therefore have an unrivalled benchmark database on which to assess the cost plan. They have used benchmark data for the mechanical and electrical costs from their in house engineering services team based on similar buildings and systems.

Civic Offices

Headline cost item	Cost £psm/ Percentage	Total (£m)
Demolition & Enabling Works	£34	£0.30
Structure & Envelope	£769	£6.84
Internal Finishes and Fittings	£180	£1.59
Services and M&E	£386	£3.44
Ext lights & Soft Landscaping	£4	£0.04
Category A works	£278	£2.47
Preliminaries	13% (10% of Cat A)	£1.83
Overheads & Profit	3%	£0.50
Design & Build Risk	2%	£0.33
Design Reserve	5%	£0.87
Construction Contingency	5%	£0.87
TOTAL	**£2,143**	**£19.08**

Town Hall

Headline cost item	Cost £psm/ Percentage	Total (£m)
Demolition & Enabling Works	£107	£0.99
Structure & Envelope	£502	£4.63
Internal Finishes and Fittings	£187	£1.82
Services and M&E	£358	£3.29
Ext lights & Soft Landscaping	£0	£0.00
Category A works	£241	£2.23
Preliminaries	13% (10% of Cat A)	£1.62
Overheads & Profit	3%	£0.44
Design & Build Risk	2%	£0.30
Design Reserve	5%	£0.77
Construction Contingency	5%	£0.77
TOTAL	**£2,142**	**£19.08**

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The Triangle, Substations and Landscaping

Headline cost item	Cost £psm/ Percentage	Total (£m)
Triangle demo, build & landscape	n/a	£0.47
2 x Substation relocation	n/a	£0.30
Site wide landscaping	£198	£0.77
Preliminaries	13%	£0.20
Overheads & Profit	3%	£0.05
Design & Build Risk	2%	£0.04
Design Reserve	5%	£0.09
Construction Contingency	5%	£0.09
TOTAL	**n/a**	**£2.01**

The cost plan is a robust analysis of the current RIBA Stage C design benchmarked against the current market and will be subject to further improvements during design development and tendering, as outlined below. Given the limited scope of detailed information available at this stage of the project, we fully expect to be able to review each cost item against the developing design in terms of the Council's revised aspirations and surveyed and documented knowledge of the sites, in particular the Town Hall.

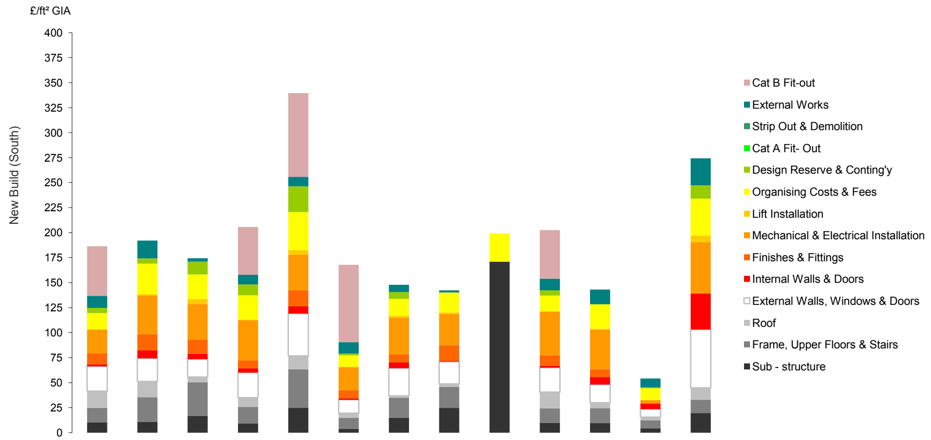
In considering the cost plan, particular attention has been paid to the complexities and challenges of the site. The A23 road, the listed buildings, the adjacent residential and leisure uses, the party wall conditions and the Zone 2 location all have a material impact upon the cost of delivery. These location challenges, as well as the clear requirement to deliver a development of sufficient quality and function, are taken into account in our cost plan.

Over 20% of the cost is attributed to Contractor preliminaries, OH&P, D&B risk and contingencies. The competitive tender process outlined below will seek to recover some of this cost.

Once tendered and included in the Maximum Commitment, the Council are protected from cost over-runs by the erosion of Kajima's 7.5% Risk Return and our 15% wrap around guarantee.

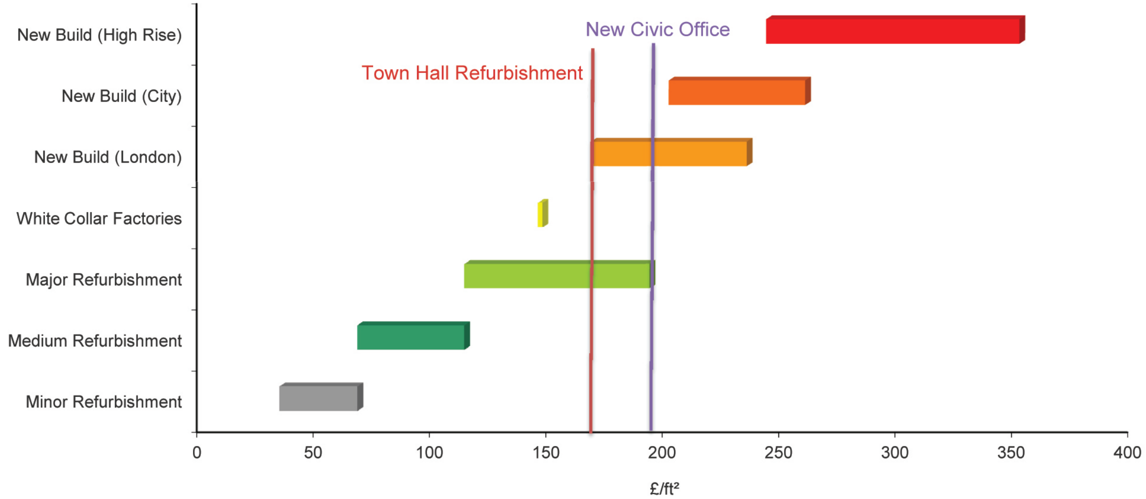
Costs exclude all other prject related costs such as VAT, professional fees, S106/278 etc

Offices New Build Projects £/ft² at Current Prices and Average Benchmarking Ranges



Graphical summary of Key Project Elemetal Costs - current prices

Benchmarking Ranges £/ft² Shell & Core Including Category A at Current Prices



Graphical representation of Benchmarking Ranges - current prices

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Professional Fees and Design Costs

A comprehensive, detailed schedule of all expected professional fees, design costs and surveys is attached at Appendix A3.1 and is summarised in total and by stage in the table adjacent.

With regard to the Town Hall, new Civic Offices and The Triangle, total design and professional fees reflect a 12.65% cost on top of build costs which is typical of a complex scheme of this nature. This equates to an expenditure of £4.8m.

Design and professional fees in relation to surplus sites relate only to the cost of developing the designs for these sites up to and including obtaining planning consent.

The costs summarised in the table above will not be incurred in a linear profile, and for the purpose of summarising the model they can be split into three stages:

Detailed Design and Planning Costs

The first stage of design will be pursuant to submitting a planning application and securing an implementable consent.

Kajima will co-ordinate the design with the appointed team in accordance with the agreed Employer's Requirements to bring the designs up to full RIBA Stage C+ standard. Kajima will also commission physical and other surveys and investigations to enable an accurate design to be drawn.

We will also engage with the Council (acting in a statutory capacity) to undertake necessary due diligence in relation to planning, heritage, transport and environmental matters, pursuant to the Design and Access Statement that will be submitted as part of the planning application.

During this stage we will also engage with the Council as occupiers, neighbours and the local community both in terms of statutory consultations and in accordance with Lambeth's 'Cooperative Council' status.

Total projected expenditure: £1.73m including survey costs, planning application fees and surplus site Stage C design fees.

Technical Design and Tender Costs

The second stage of design will commence once planning permission has been secured. The majority of these costs relate to detailed technical design and co-ordination to RIBA Stage E to provide sufficient detail to put the design package out to tender. Design work will be monitored and limited to ensure that it is sufficient to protect the quality and integrity of the design and that sufficient information is available for the tendering parties to understand and competitively price the risks.

Additional costs during this stage will include legal fees in relation to the S106/CIL/S278 agreements and the build contract together with party wall surveyor fees.

Total projected expenditure: £2.41m

Construction Costs

The balance of design fees and costs will be incurred during construction. In our assessment we have accounted for all design costs but, on the assumption that the key design team will be novated to the contractor, some costs may be assumed by the contractor directly under their Design and Build contract and consequently reduce.

During the build a key consultant will be DL acting as Employer's Agent, who will monitor the development expenditure and ensure that it is accounted for in accordance with the cost plan and development progress.

Total projected expenditure: £1.55m

Professional fees and design costs

	Total	Fees to PP/ Stage C+	Fees to Stage D	Fees to Stage E	Build Fees
Principle Design/Professional Fees	**£4.23m**	£0.76m	£0.95m	£1.09m	£1.43m
Secondary Design/Professional Fees	**£0.57m**	£0.21m	£0.75m	£0.17m	£0.12m
Total Design Fees, ex Contingency	**£4.80m**	£0.96m	£1.03m	£1.25m	£1.55m
Design Fees - Surplus Sites	**£0.47m**	£0.47m	-	-	-
Survey Costs	**£0.23m**	£0.18m	£0.01m	£0.03m	-
Planning, Statutory & Legal Costs	**£0.19m**	£0.11m	£0.03m	£0.05m	-
Totals	**£5.69m**	**£1.73m**	**£1.07m**	**£1.34m**	**£1.55m**

Design Contingency

Within the model we have allocated a pre-construction design contingency equivalent to 1.5%. This is a prudent inclusion to cover any unexpected costs, for example any specialist design or surveys that may arise as a result of surveys. It is to cover 'unknown unknowns'. It remains the Council's contingency, but if unused it will roll up to protect the Council from unbudgeted design expenditure.

Cost Saving Opportunities

The delivery of the project's design, operational and quality objectives at the most competitive price is a fundamental principle of the SW2 Enterprise Centre project and it will be where Kajima's experience will add significant value.

Once appointed, we will proactively seek to interrogate the project throughout Detailed and Technical design stages to ensure that the Council get best value for money. The nature of our appointment means that we are heavily incentivised to make the project perform financially and that the whole scheme is viable – our interests are aligned.

Cost saving opportunities we will explore include:

Risk reduction

Unknown and unquantified risk has a disproportionate inflationary impact on build costs in any project. At this stage of development design, costs for unknown elements are estimates and include a risk premium as well as a design development and construction contingency.

Through a systematic and detailed programme of surveys and investigations, we will remove risk and quantify those risks that cannot be removed with an appropriate provisional sum and contingency. The more information that can be provided to the contractors during the tendering process, the lower the risk premium contractors will build into tender returns.

Review of Areas and Density

The simplest way to save cost is to build less. One of our first steps will be to undertake a revised audit of occupancy requirements on a department by department basis. The objective is to identify where any cross-over of uses might exist, particularly in relation to public areas, meeting rooms, communal spaces, circulation and support spaces, storage and hot desk allocation, and how space might be better used over and above our design.

The density has been optimised to present a bold but deliverable scheme in planning and heritage terms. Once through the competitive process, we will further test the planners in terms of density to identify any opportunities for additional height with the planners where this would increase the value of the surplus sites.

We have explored in outline, as an

additional cost item (and not included in our bid), the opportunity to re-use and build into the existing basement for the Civic offices. We are not accurately aware of the extent of the basement or its condition although, based on the information provided being correct and assuming a reasonable condition, could provide for an additional 622 sq m at an additional cost of £1.09m plus contractor costs and fees. A cost/benefit analysis of this against above ground build savings, and other opportunities identified during detailed design, will be undertaken following appointment.

Value Engineering

Value engineering of the design and the optimisation of the opportunities to save costs whilst maintaining the design, operational and quality objectives will be an ongoing process managed by Kajima. Typical areas where cost savings might be identified include a tighter programme, product choice, performance criteria, prioritised finishes selection, optimising re-use of existing conditions and post-survey adaptations. This process will be ongoing and dynamic throughout design.

We will advise the Council in detail of the advantages and impacts of each option, and the decision on which cost saving opportunities to adopt will be made jointly. Areas of savings (excluding contractor costs and fees) we have identified at this outline stage include:

- Use of conventional boilers instead of Combined Heat and Power: -£1.7m
- Omit community roof terrace: -£0.08m
- Omit greywater reuse: - £0.06
- Omit goods lift: - £0.17

This is not an exhaustive list but indicates the types of decisions that will need to be taken in conjunction with the Council. All value engineering needs to be considered against other objectives of the Enterprise Centre project.

Category B Fit-out

The Council has advised bidders to include an allowance of £18.13m for Category B works and a further £4.5m for IT and £2.0m for desks.

In our experience, and in the opinion of DL, this is a very generous allowance which would reflect a premium City of London fit out. This is clearly not in line with the Council's objectives.

Category B costs will be assessed in detail once the Council's space planning needs are better understood. For a civic building of this nature and scale we would anticipate a budget of £8.9m (£50 per square foot NIA, including furniture and IT cabling to desks) to be more appropriate. This figure is adequate for the quality and robustness required. We have been verbally advised by DL that this is benchmarked against the fit-out costs of another current London Borough civic development. It is also similar to Kajima and DL's own fit out costs.

This is benchmarked against the costs of another current London Borough civic development

This £12m saving will be improved when the £4.5m IT budget is reviewed. The proposed budget includes an allowance for IT cabling to terminals and the £4.5m figure appears to be particularly high. We will work with the Council to agree the appropriate elements to be included and those that should remain part of a separate IT hardware tendering process.

Procurement Strategy

The objective of the tendering and final contractor process will be to secure the best main contractor offering the best level of risk transfer and value.

Stage 1 – Pre-Qualification

A tender list of main contractors of appropriate size, experience, available workload, financial stability, quality and experience of proposed team will be agreed with the Council and invited to undertake a Pre-Qualification Questionnaire (PQQ). We anticipate a maximum of 8 – 10 suitable candidates will be invited.

Stage 2 – Interview

Based upon PQQ returns, and our analysis of them, a shortlist of up to five parties will be interviewed to assess their proposed teams and consider their PQQ returns in detail with regard to their fit for the project.

Stage 3 – Shortlist Tender

A shortlist of a minimum of three parties, agreed with the Council in accordance with the Development Agreement, will be invited to develop detailed tenders based on the signed off drawings and specification for the Enterprise Centre. This process will include the negotiation of risk transfer and pricing. Kajima will assess the tender returns in detail and provisionally select the preferred contractor for recommendation to the Council.

As a guide to expected contractor quality, Kajima have over the past 18 months appointed Wates for an office refurbishment in Westminster and Balfour Beatty for a new build hospital. We are currently out to tender with Galliford Try, Morgan Sindall and McLaren for a major City of London Grade II office refurbishment and extension project.

Section 106, 278 and Community Infrastructure Levy Costs

We have worked in conjunction with DP9 to estimate the likely statutory costs that will be applied to the Council Accommodation element of the scheme. We have assumed that all such costs relating to the surplus sites will be paid for by the surplus site purchasers and are outlined below as deductions to the surplus site values.

The costs paid by the Council will comprise two distinct elements:

Mayoral CIL

This is a simple calculation based upon, in simple terms, the increase in provision of commercial floor area multiplied by the Mayoral CIL of £35 per square metre.

The precise calculation will be subject to verification of Gross Internal Areas of the existing buildings and final designs but, based on information we have been provided and the designs we are proposing, this payment is calculated as shown in the following table.

	Existing	Proposed	Difference
Town Hall	8,730	9,079	+349
Civic Offices	0	17,979	+17,979
Town Hall Parade	2,418	0	-2,418
Hambrook House	2,428	0	-2,428
Ivor House	3,868	0	-3,868
Olive Morris House	7,216	0	-7,216
TOTAL	**24,660**	**27,058**	**+2,398**
			x £35 psm
		Mayoral CIL	**£83,930**

The Mayoral CIL will be subject to how Lambeth, as the collecting authority, interprets CIL legislation. Central Government has recently consulted on how the rules relating to existing use are interpreted given the lack of clarity of the 'lawful use for 6 months in previous 12' rule. We would strongly argue the case that all of the existing sites are in lawful use, and guidance on the Council's web site would suggest a similar interpretation. It states that CIL "applies to the net increase...after allowing for any demolition". CIL will be payable upon start of construction.

Should this interpretation for some reason not prevail, Town Hall Parade may be at risk of not being included if it remains unoccupied. The potential additional Mayoral CIL of £84,630 needs to be assessed in the context of Lambeth's policy and any costs of temporary reoccupation (if required to mitigate).

London Borough of Lambeth s106 and CIL

The Council's Draft CIL Charging Schedule confirms that there will be no CIL for office accommodation.

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Section 106 costs are less formulaic. Given the civic nature of the scheme and the substantial investment (as Landowner) the Council will be making in public realm, community facilities, art and enterprise space, and the overall regenerative nature of the Enterprise Centre, we would expect this to more than mitigate any s106 costs that might be expected to be otherwise levied. Combined with the circular nature of such charging – Lambeth paying Lambeth – we expect these figures to be zero.

Section 278

We have allowed £250,000 for highways works associated with the scheme. This is a sufficient estimate to provide for potential bus stop relocations, new pedestrian crossings, Buckner Road restrictions and Porden Road stopping up and cycle lanes. S278 costs will be incurred during construction.

SURPLUS SITES

Development Cost Assumptions

DL have provided an outline cost forecast using the RIBA Stage B designs included within our proposals, based on a 'developer with main contractor' basis with costs benchmarked against current data at Appendix A3.4. This includes a robust allowance for preliminaries (13%), OH&P and D&B risk (5%) and contingencies (10%).

These costs will be open to the individual interpretation of bidding parties, particularly volume house builders who act as contractor and developer and benefit from competitive advantages in terms of costs, overheads and market penetration. Whilst we expect costs to be assessed by prospective purchasers in a variety of ways, and therefore deliver to the Council additional land value, our base case includes them as a robust baseline indicator of cost.

Where we have assumed growth in unit sales receipts we have grown costs by 2% pa on top of these figures. We have allowed 10% for professional fees and 4.5% for marketing and sales costs. These costs will also vary between different bidders. Sales and value generators are as identified later in this section.

We have assumed a 10% 'Profit on Cost' allowance for each site. This number is a challenging one to forecast with accuracy given that it will be determined by a number of factors including the particular developer's appetite for the purchase, their own return requirements and their basis of appraisal. Given the competitive nature of the tendering process , the 'oven ready' nature of the sites and the buoyant market, we expect individual purchasers to bid aggressively and the Council to recapture some of this value through competitive tendering.

We do not propose to develop the designs for the surplus sites beyond RIBA Stage C. This will grant the bidders the opportunity to, in their own opinions, identify additional cost savings and value through additional detailed designs as part of agreeing Detailed Planning Consent and/or Reserved Matters with the Council. This flexibility will make the sites more desirable to a broader range of potential purchasers and underpins our land value assumptions.

Affordable Housing Assumptions

Our Variant A Bid assumes compliance with ISFT instructions to allow for 20% Affordable Housing (AH) across the surplus sites. As requested, Wynne Road is included as a 30-unit affordable scheme but excluded from the calculation of development deficit. We have not been advised of the type of housing (Social Rented, Affordable Rented or Intermediate) that these 30 units will provide.

Our proposals account for a total of 227 units across Olive Morris House, Ivor House, Wanless Road and Hambrook/ Porden, which will therefore deliver a total of 257 homes as a result of the overall project. A 20% AH provision equates to 51.4 units in addition to the 30 provided for on Wynne Road.

We have provided for 53 units which, when combined with Wynne Road delivers a total 20.6% AH. All 53 units are located in a single core of Olive Morris House. The acceptability of this will be subject to discussion with the LPA however in terms of maximising value and viability whilst satisfying the AH provision – which are conflicting requirements of the ISFT - we believe this to be the best compromise and can satisfy all parties.

Detailed arguments will be developed in consultation with the planners and prepared as part of the planning submission, but are as follows:

- Olive Morris House allows for a single dedicated core for AH, and therefore does not have a negative impact upon private values;
- Externally and internally (save for some finishes eg kitchens) the AH will be indistinguishable from Private Dwellings (PD) as part of a larger block which will promote and foster inclusion;
- We have assumed that all AH is sold to a Lambeth-approved Registered Social Landlord who will provide Social Rented homes i.e. at 30-40% of market rents, rather than as Affordable Rented at 50-80% of market rents or Intermediate Housing available for part or shared ownership;
- The Enterprise Centre provides for a significant quantum of community infrastructure and public realm that will include affordable business space.

We have included a Base Bid assuming 40% affordable housing for information purposes only, as requested. This assumes a mix of Social Rented housing and Intermediate Housing across Olive Morris House and Hambrook House/ Porden Road.

We have also included a Variant B option, which delivers only 12% AH limited to Wynne Road. This demonstrates the land value impact of AH on the Base and Variant A bids.

Section 106 and Community Infrastructure Levy

We have assumed that all s106 and CIL costs will be borne by the respective developers of the scheme, although these costs have a negative impact upon land value.

We have assumed a combined s106 and CIL allowance of £12,500 per dwelling. Based on an average unit size across the scheme of 70.25 sqm, this equates to £178 psm comprised of:

- A Mayoral CIL of £35 psm;
- A LB Lambeth Zone C CIL of £50 psm; and
- A s106 contribution of £93 psm.

Our analysis of value is based on the total quantum of homes developed. We would expect to negotiate a reduction in s106 costs for AH and to make an application for Social Housing Relief from CIL be submitted prior to development. These savings are considered below.

Brixton Sales Values

In order to present a robust view of current and expected surplus site values we have considered in detail the forecast economic conditions and the consensus view for London and Brixton non-prime residential growth for the duration of this project. Based on the extremely positive outcome of this research we expect to experience a period of sustained economic growth, and the most **unlikely** situation is that the value of the surplus sites will remain stagnant or fall.

The most unlikely situation is that the value of the surplus sites will remain stagnant or fall

Comparable Schemes and Sales Data

Comparable new build developments in Brixton are limited but two schemes have demonstrated the significant demand for new apartments in the area.

Resonate, a Crest Nicholson scheme of 65 apartments, was completely sold within 4 months of being launched and secured sales values of up to £550 psf. Jones Lang LaSalle, corroborated by the agents we've consulted, considere this location to be inferior to all of the surplus sites we are considering. Barratt's Brixton Square, although an inferior location due to its adjacency to the railway lines, has been similarly successful in securing sales values in excess of £520 psf.

All agents we have spoken to, including Foxtons, Douglas & Gordon, Lauristons, Haart, Wooster & Stock and Beresford, expressed their confidence in market conditions and, anecdotally, that demand is dramatically outstripping supply.

"It's boom time. Prices have gone up at least 25% here in the past year" – Paul Markey, Haart Estate Agents, Brixton (FT, May 2013)

Obtaining accurate existing housing stock value information is challenging due to the lack of empirical data. According to Zoopla (who employ Land Registry 'Price Paid' data), Brixton house prices (including all houses and flats) have demonstrated year on year growth since 2009 of over 5% pa.

Based on conversations with active local agents in June and July 2013, one and two bedroom flats in central Brixton are in particularly strong demand. Of the comparable properties advertised as available for sale by Rightmove within half a mile of Brixton Station, approximately 50% were subsequently established with the agents as being under offer with over 30% of the remaining classed as "about to go". Most flats for sale in central Brixton are put under offer in less than two weeks.

SECTION 3: FINANCIAL ROBUSTNESS
3.2 FINANCIAL VIABILITY AND CREDIBILITY

We have analysed this availability and prices in and around the Triangle site and the surplus sites to better inform our opinion of value.

One bedroom apartments range in price from £220,000 up to £287,000, with an average asking price of £566 per square foot. Two bedroom apartments range in value from £280,000 up to £495,000, with an average asking price of £574 per square foot.

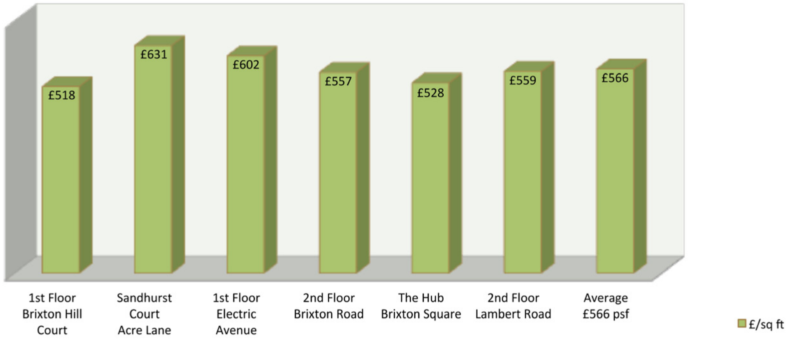
These ranges cover a variety of types of property and levels of repair and the areas of the apartments are likely to not have been measured in accordance with the RICS Code of Measuring Practice and, in any case, the size of these apartments are generally well below the standards expected under the Mayor's Housing Design Standards.

Current Day Sales Values

Taking the average of all the above evidence of Brixton sales and applying a c.10% tolerance either way, the sales tone of Brixton town centre is between £500 and £600 per square foot, subject to a variety of influencing factors including the actual scheme, floor level, aspect, configuration and outlook. Particularly large or small apartments will move outside of this range to reflect the discounting or premium for quantum.

We have applied a 'per square foot' rate to each apartment, and then made individual adjustments to the sale price to reflect influencing factors and also Stamp Duty Land Tax thresholds. Whilst these are an opinion of value we regard them to be an accurate forecast of the sales values that would be generated today if the apartments were available.

A comprehensive 'apartment by apartment' summary of current day sales values for each surplus site is attached at Appendix A3.5.



For Sale: 1 beds - Brixton Station + 500m

For Sale: 2 beds - Brixton Station + 500m

SECTION 3: FINANCIAL ROBUSTNESS
3.2 FINANCIAL VIABILITY AND CREDIBILITY

Growth Forecasts

Given that the surplus sites will not be sold immediately it is critical, in establishing their values and impact on viability, to understand growth expectations.

Material factors that will have a material beneficial impact on the value of the surplus sites include:

- The 'Help to Buy' equity loans scheme, extending to all buyers and all properties under £600,000 in January 2014, offers a 20% interest free loan and mortgage guarantees to buyers;
- The Government's £1 billion 'build to rent' fund providing cheap development finance;
- Employment growth forecasts are stable for the coming years, with largest growth in London;
- Housing construction is currently at historically low levels with only a moderate growth forecast, constraining new supply;

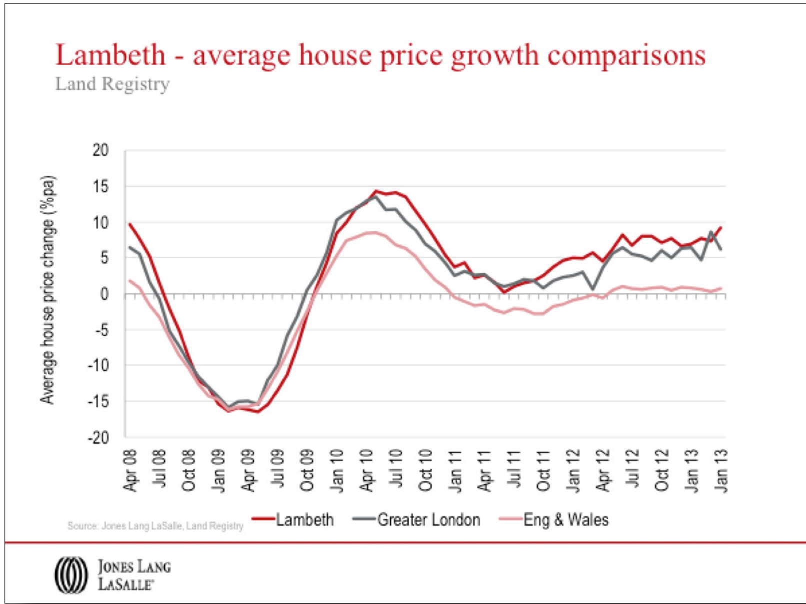
London has, to a large extent, been insulated against the challenging market conditions elsewhere in the country. Economic indicators now widely projecting stronger UK-wide GDP growth and steady inflationary growth, Brixton and London will continue to out-perform the rest of the UK for several reasons:

- The ONS has recently significantly increased their household projections in London by nearly 40% to over 525,000 by 2020.
- Knight Frank calculates that over the same period only 277,000 new units will be delivered. This report (London Calling – June 2013) is attached at Appendix A3.6.

"The overall trend in London shows that demand for housing in the capital will continue to outstrip supply by quite some margin" – Gráinne Gilmore, Head of UK Residential Research, Knight Frank

- Knight Frank/Markitt report that the household property price confidence is at its highest for three years. Their report is attached at Appendix A3.7.
- Savills report that London land values are now greater than their 2007 peak, with demand highest in Zones 1 and 2. This report is attached at Appendix A3.8.
- Savills predict the mainstream London market to grow by 10.3% between now and the end of 2015 (and 21% by the end of 2017). The 'Inner Commute' market, including Brixton, is projected to grow even more. Similar projections are made by Knight Frank and Jones Lang LaSalle.
- Jones Lang LaSalle's overview of the Brixton market is attached at Appendix A3.9, identifying the structural changes taking place in the local market and expected growth of 4-7% per annum for the next 5 years.

We have reviewed our growth forecasts in some detail to ensure that they are robust and credible. Although there has been an increase in expectation generally, we consider the 5% per annum increase we adopted at ISDS to be the correct forecast. We have adopted this growth until 2016, and thereafter assumed a more stable growth of 2.5% per annum.



SECTION 3: FINANCIAL ROBUSTNESS
3.2 FINANCIAL VIABILITY AND CREDIBILITY

Disposal Assumptions
Disposal and pricing assumptions are based on a ‘best price, best purchaser, best time’ principle. The final timetable for disposal will be agreed with the Council to ensure that maximum site value is achieved whilst minimising the Council’s subsidy. Timing will also need to be considered in the context of the final decant strategy.

We have assumed that all sites are sold freehold and with the benefit of planning. 50% of private dwellings are assumed to have been sold ‘off plan’ prior to practical completion of the relevant scheme with the remainder in the subsequent 12 months. All AH is assumed to have been 100% sold up front to a RSL.

Surplus Site Values
Each surplus residential site has been appraised in detail in terms of cost and value, and detailed ‘With Growth’ and ‘Without Growth’ development appraisals in the context of the Base Bid and Variant Bids A and B have been included at Appendix A3.10. These include additional sensitivities showing +/- 10% sales value and cost changes (on top of any explicit growth) and +/-2% profit on cost assumptions.

The model assumes Variant A (with growth) as its base case for site values, but with the ability to adjust between growth and no growth as well as the three AH scenarios in Summary Tab Cell C6. The residential site values are calculated assuming they have the benefit of outline planning and vacant possession, and are ready to develop.

Wanless Road is appraised slightly differently, whereby we have assumed it is sold relatively quickly to finance design development. Phoenix House is appraised on the basis of a short term lease back to the Council and for continued B1 office use.

Summary Site Appraisals
Detailed appraisals for our Base and Variant bids, including and excluding market growth and with sensitivity analyses profiling values dependent on costs and receipts, are attached in Appendix A3.10. Our Variant A bid including growth forms the basis of our Variant submission for the Council’s assessment.

When growth is adopted, costs are assumed to grow 2% year on year over and above the DL Cost Plans.

A summary of each site, and out-turn site value, is as shown in the adjacent table.

These figures are based on our growth assumptions in this section but exclude capture and retention of additional value and cost savings for the Council, as outlined below.

£m’s	Porden Road	Ivor House	Olive Morris House	Wanless Road	Phoenix House
Grown Revenue	£36.78m	£24.49m	£47.25m	£3.80m	£37.2m
Grown Build Costs	£10.95m	£7.47m	£14.43m	£1.03m	£7.25m
Prelims, OHP, D&B	£2.53m	£0.95m	£2.70m	Inc.	Inc.
Contingency	£1.30m	£0.60m	£1.77m	£0.10m	£0.36m
Fees & Other Costs	£4.18m	£2.86m	£6.39m	£0.3m	£3.06m
Finance Costs	£1.64m	£1.16m	£2.06m	£0.10m	£2.58m
Profit	£3.34m	£2.23m	£4.30m	£0.35m	£4.85m
Land Residual	**£12.84m**	**£9.22m**	**£15.60m**	**£1.92m**	**£19.10m**

Cost Minimisation, Value Maximisation
We have stated our views of the values for each site above. However our requirement to seek Viability under the Development Agreement incentivises us throughout the entire process to identify cost savings and value enhancements for the sole benefit of the Council.

Market Growth
We have outlined the environment for growth above and taken our basis of surplus site value as 5% annualised growth to 2016 and 2.5% annualised thereafter. This is based on research identified, economic forecasts and our own experience of markets, but is passive (in that we cannot influence it). But it cannot be ignored.

We will monitor the market on a regular basis, and liaise with agents to advise the Council on local pricing and how this might influence site sales. The timing of site sales, which is outlined in the programme and determined by our proposed decant strategy in line with the Enterprise Centre delivery, can be amended to respond to market changes if it will improve Council revenue.

Competitive Tension
We have based our cost assumptions and profit forecasts on a residential developer purchasing the site in a buoyant market, requiring a return for their risk, and then appointing a main contractor, who would similarly apply a margin.

The main advantage of an open market tendering of the surplus sites is the ability to capture worth, rather than simply value. It is highly likely that a volume house builder will appraise the site on a different criterion to seek a competitive edge. Quality London Zone 2 sites are challenging to acquire, and therefore inspire a ‘best foot forward’ approach that delivers value to the vendor. Items such as profit margin, preliminaries, OH&P and build cost will come under deflationary pressure by a turnover and volume driven house builder building on their balance sheet.

For the residential surplus sites, we have allowed for £20m in costs attributable to profit, preliminaries, contingencies, overheads and D&B risk. In competitive negotiation with different bidders for different sites we would target to maximise retention of these sums, and expect to ‘recover’ a proportion of this sum, say 10% equating to £2m.

Affordable Housing Options
Our Variant Bid A complies with the ISFT AH requirements of 20%. We have analysed the impact of reducing AH further down to a minimum of 12%, which would deliver 30 affordable dwellings on Wynne Road only. Detailed appraisals are attached at Appendix A3.10 and this approach would deliver additional grown sales revenue of £5.2m.

As a matter of course we will seek to maximise surplus site revenue through negotiation with the Council, acting in its statutory capacity, and seek some consensus through pre-application dialogue. There may be scope, once the details of the Wynne Road scheme are known, to reduce the proportion of Social Rented in Olive Morris House down to the Council’s accepted 70/30 split between Social Rented and Intermediate housing, which would add additional value, albeit in relatively small numbers.

We will also explore Affordable Rented and Intermediate social housing, which delivers higher values, and off site provisions and commuted sums. However we recognise the importance of AH within the borough. We also accept that there may be political challenges to overcome with determining the ultimate proportion of AH and what type of AH is adopted and we will work with the Council to ensure that maximum value is accredited to the scheme by Affordable Housing.

S106/CIL savings
Although not assumed in our bid, we would expect to negotiate with the Council to minimise s106 and CIL obligations for both the Enterprise Centre and the Surplus Sites.

SECTION 3: FINANCIAL ROBUSTNESS
3.2 FINANCIAL VIABILITY AND CREDIBILITY

As a matter of course we would apply for relief from CIL and s106 payments in relation to the affordable housing. Based on the 53 AH dwellings within our Variant A scheme this would, on a linear basis, increase site value by £0.6m.

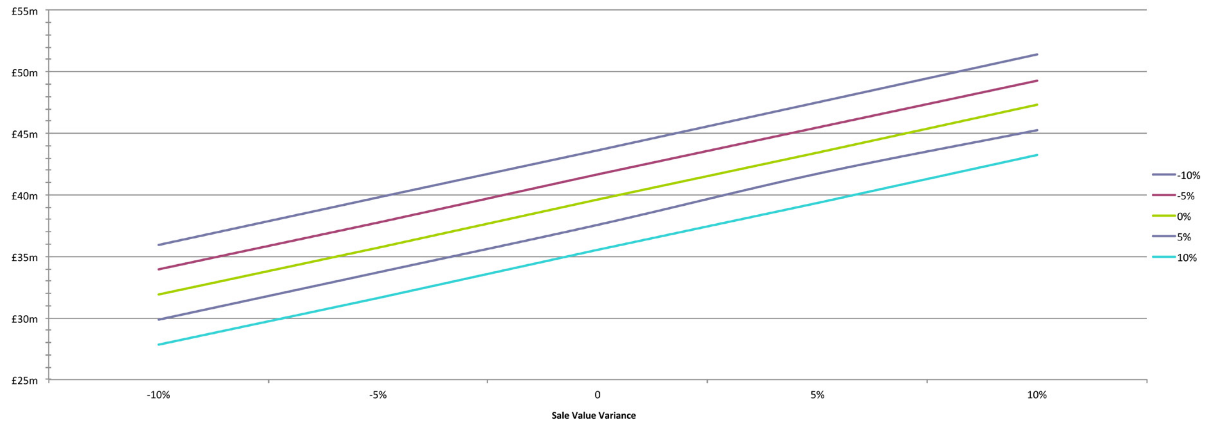
Grant Funding

Whilst available grant funding for capital projects has been limited and extremely competitively sought due to the global economic condition, as the UK European economies start to improve (and a General Election approaches) it is possible that new sources of grant funding for social, localised and community funding may come available. We will work with the Council to identify and obtain such grants where the project, in its widest sense, qualifies.

Planning Density

We have put forward what we consider to be the best approach for the Enterprise Centre in terms of meeting the Council's accommodation and value expectations. Nonetheless, once selected we expect to engage with the Council separately acting as landowner and as statutory authority. We can then seek to challenge further our assumptions of site density to optimise development potential, build costs and surplus values in the context of the planning and heritage context.

The graph demonstrates the sensitivity between cost savings and increases against value growth assumptions of our Variant A proposal.



Impact on Resdidential Surplus Site Values of Cost and Sales Value Variance (Excludes Phoenix House)

SECTION 3: FINANCIAL ROBUSTNESS
3.2 FINANCIAL VIABILITY AND CREDIBILITY

NEIGHBOURLY MATTERS

Rights of Light

We have developed the Enterprise Centre and Surplus Site designs with particular attention to the Rights of Light impacts on neighbouring properties, based upon the outline assessment by Delva Patman provided by the Council. We consider our designs to be sympathetic to Rights of Light and thus the impact is minimised.

The Council will also utilise, in the absence of agreement of any compensation payable, their statutory powers under the Town & Country Planning Act 1990 Section 237, whereby rights can be compulsorily purchased by the Council if the development sufficiently adds to the social, environmental and economic fabric of the area. This in turn limits the compensation payable to the injured parties as it removes the threat of an injunction.

We have allocated a provisional sum of £500,000 for compensation for injury due to Rights of Light. Given the limited scope of potential injury we consider this to be sufficient and will engage with the Council's Rights of Light surveyor during the planning process and seek to settle claims at the agreed point in time. However without the risk of injunction Rights to Light are not a material risk to development.

The Electric and UK Power Networks

Part of the site is leased to UK Power Networks (UKPN), but there are no 'lift and shift' provisions permitting its relocation. UKPN's agreement will therefore be required. We have budgeted £392,000, within the Davis Langdon cost plan at Appendix A3.4, for the relocation of the substations prior to development commencing.

Full consultation with the owners of The Electric will be required immediately following selection to understand their ongoing business needs, to negotiate and discuss access during construction and their route of escape through the Enterprise Centre site.

In due course a Party Wall Surveyor will be appointed to undertake a condition survey and agree a Party Wall Award with The Electric.

ADDITIONAL INCOME POTENTIAL

We have worked with Kajima Community, a wholly owned, 'not for profit' subsidiary of Kajima Partnerships, to assess the expected additional income that can be expected from renting out relevant areas of the Enterprise Centre for enterprise and use by members of the public.

Kajima Community (KC) provides marketing, administration and operational services to our public sector clients, predominantly schools and community centres, ranging from simple training and administration of the booking system through to managing all functions relating to the relevant space. Following selection we will formally introduce the Council to KC to further explore opportunities in line with enterprise space expectations.

The costs we have outlined below have been benchmarked against KC operations in Camden and Northampton and are therefore reasonable forecasts. With proper management, marketing and systems, after five years we anticipate that gross income of £0.3m can reasonably be expected, with additional opportunities for growth depending on better understanding how the Council use the space themselves.

A wide range of local enterprises, clubs, religious groups and members of the public will use the space for a variety of uses. A list of typical users at KC's other facilities is attached at Appendix A3.11, along with additional information about Kajima Community.

Assembly Hall and The Triangle

We have assumed that the Assembly Hall and the Triangle will be available for hire during the day and evening throughout the year. They are flexible spaces we would anticipate being available for regular and one-off uses throughout the day and evening, 7 days a week.

We would expect the Assembly Hall to cost £30-£50 per hour for regular users depending on the time of day (establishing a peak/off peak basis). For one-off events the hall should generate between £80-£110 per hour on Sunday-Thursday and £150-£180 per hour on Friday and Saturday. This is expected to generate £50,000 in year one rising in increments of £15,000 per year to £130,000 in year 6.

The Triangle is expected to recoup less due to its smaller size, although KC would expect to review this depending on the demand given that it will be a very special space with ample external areas. Initially they forecast hire rates of £15-£40 per hour for regular use. One-off events would be charged initially at £60-£90 per hour Sunday-Thursday and £120-£150 per hour on Fridays and Saturdays. This is expected to generate £30,000 in year one rising to £60,000 in year six, subject to upwards revisions based on the unique nature of The Triangle.

Town Hall Meeting Rooms

We have, for the purposes of this analysis, assumed use of the 12 meeting rooms on the ground floor and that they will be used, on average, for 10 hours per room per week, totalling 120 hours of use.

KAJIMA COMMUNITY

Hire rates for the rooms will range between £15 and £25 per hour, depending on the size of the room. Small discounts would typically be available for regular hires. There is no peak/off peak delineation. There is potential to raise additional income by offering refreshments and through offering AV equipment, flip charts and other equipment.

Total expected income would start at £40,000 in year one rising to £108,000 in year four.

Civic Offices Roof Garden

As part of our design we have allowed for controlled public use and access to the terrace in the Civic Offices. We would anticipate that this is made available for hire during the year, subject to planning, although have not included income as this remains subject to agreement with the Council as to its use and by whom.

SECTION 3: FINANCIAL ROBUSTNESS
3.2 FINANCIAL VIABILITY AND CREDIBILITY

RUNNING AND LIFECYCLE PROJECTIONS

We have not undertaken a detailed analysis of the building running costs and lifecycle costs however have been asked to provide an indication of expected levels.

We have liaised with Atelier 10 to provide an indication of energy consumption costs and consulted Kajima's Operations team and Kajima Properties' managing agent Workman & Partners to ascertain typical running and lifecycle costs. Without a detailed specification we have been advised that these numbers are intended as a guide only.

New Civic Offices

The new Civic Offices have been designed to the most efficient standards, utilising natural ventilation and thermal mass, natural daylight and high performance controls, thermal insulation and glazing. Based on the proposed design, together with benchmark data for other similar modern office buildings, we estimate energy consumption as follows:

Regulated

- Heating and Hot Water 60-100 kWh/m2/yr
- Lighting, fans, pumps etc 30-50 kWh/m2/yr
- Unregulated (User dependent)
- Equipment 30-40 kWh/m2/yr
- Catering etc 3-5 kWh/m2/yr

On the basis that the building is built to best Code standards and that the Council operate the building efficiently, we estimate that energy consumption will be approximately 123 kWh/m2/yr. This corresponds to an energy cost of c. £93,000 per annum.

Town Hall

With regard to the Town Hall, without detailed information in relation to U-values for the existing fabric, and without surveys to determine those areas of the existing fabric that can be improved to current standards, an accurate forecast of energy consumption is more challenging.

As a minimum, lighting, systems and controls will be upgraded to current performance standards, the light wells will become internal spaces and the roof will be fully insulated. Furthermore, more than one third of the refurbished and extended Town Hall will be new build accommodation.

However, the refurbished and extended Town Hall will be subject to higher occupancy/user numbers, accommodating 400-450 desks, customer services and a large number of meeting rooms, all of which will be mechanically ventilated in order to achieve modern occupancy comfort levels, and without the ability to use thermal mass and night time cooling as can be achieved in the new Civic Offices.

Regulated

- Heating and Hot Water 110 kWh/m2/yr
- Lighting, fans, pumps etc 60 kWh/m2/yr
- Unregulated (User dependent)
- Equipment 30 kWh/m2/yr
- Catering etc 3 kWh/m2/yr

On the basis that the building is well designed and that the Council operate the building efficiently, we conservatively estimate that energy consumption will be approximately 203 kWh/m2/yr reflecting higher occupancy, increased area and the higher levels of both winter heating and summer cooling required for the building to achieve desired occupier standards. This corresponds to an energy cost of c.£157,000 per annum.

Further analysis and modelling will be undertaken during detailed design, once surveys have been undertaken to the existing fabric. This will identify further areas of the building fabric that can be improved through refurbishment, and will permit a more accurate energy consumption forecast.

Lifecycle costs

Lifecycle costs, i.e. the costs of replacing obsolete or broken building fabric, can only very broadly be estimated. In PFI projects it is a calculated risk taken by the sponsor or a third party contractor and assumes a complicated analysis of lifecycle projections of each item at risk.

In this case, where the Council are taking the risk of ongoing maintenance and replacement (subject to the warranty and inherent defects) expenditure will depend on these works taking place. We have reviewed our recent lifecycle forecasts for projects and the large majority are allowing for between £15-£24 per square metre per annum. This will equate to a lifecycle cost range of £270,000 - £430,000 per annum.

This large variance is due to the differing handback requirements from project to project and the original building specification and expected use. Costs are typically low in the first ten years, rising thereafter to account for ongoing building repairs and obsolescence. On the basis of our design specification and use, we have adopted a lifecycle fund of £8m over 25 years, which is an equivalent cost of £320,000 per annum. This has been profiled in the financial model in accordance with our experience on other comparable projects.

Other Annual FM Costs

The Council should expect to incur other FM costs as identified below, based on a typical London office building. These are estimates only, particularly with regard to quantum of personnel which is generally a matter of preference to individual building occupiers. These costs are also based on regularly tendered prices from third party providers. If the Council prefers to employ these services directly some costs may increase.

FM Manager	£50,000
Building Manager	£40,000
Annual Risk Assessments	£15,000
Water	£30,000
Security Guards	£350,000
Internal Cleaning	£125,000
Window Cleaning	£20,000
Hygiene Supplies	£20,000
TOTAL	**£650,000**
Equivalent £psm	**£36.15 psm**

SURPLUSES AND OVERAGE STATEMENT

A key principle of our proposal is that all surplus site revenues, overages, unspent contingencies and development surpluses are the property of the Council. This unquestionably delivers best value. Kajima remain incentivised to minimise costs and maximise values by way of the viability test as, until this is passed, we do not make any return after deduction of our bid and internal costs.

INTERNATIONAL HOUSE

International House is now excluded from our calculation of surplus site values in accordance with the ISFT directions. Given the late stage it was removed from the process, we had inevitably undertaken considerable work in relation to the scheme. We have for information included a summary of our design, including a new build option and our opinion of worth, at Appendix A3.12.

SECTION 3: FINANCIAL ROBUSTNESS
3.3 FINANCIAL OFFER AND VALUE

FINANCIAL AND COMMERCIAL PRINCIPLES

A detailed financial model is submitted in line with the ISFT requirements, unlocked and based on the technical solution submitted, the assumptions outlined in Section 3.2 and in line with the commercial and financial principles outlined in the Development Agreement.

The populated ISFT Output, Developer Returns Summary and Council Cashflow Templates are attached at Appendix A3.3 showing maximum commitment and surplus revenues.

KEY FINANCIAL TERMS

Maximum Commitment

As identified in the Summary and ISFT Output tabs of the financial model, the Maximum Commitment to deliver the Enterprise Centre will be £63.51m including all construction costs, fees, surveys, fitout costs and returns to Kajima, plus finance costs of £0.93m.

Peak Funding

Peak funding, taking into account our surplus site sale timetable, is forecast to be £31.26m and programmed to occur in Q2 2017.

Surplus Site Revenue

Based on our Variant A bid, which assumes a site wide (plus Wynne Road) 20% Affordable Housing provision and 5% annualised growth to 2016 and 2.5% thereafter, we calculate total surplus site revenue to be £58.69m. This will be netted back to £55.46m once costs of sale and the Hambrook House option payment are taken into account.

The total deficit is calculated to be £8.98m.

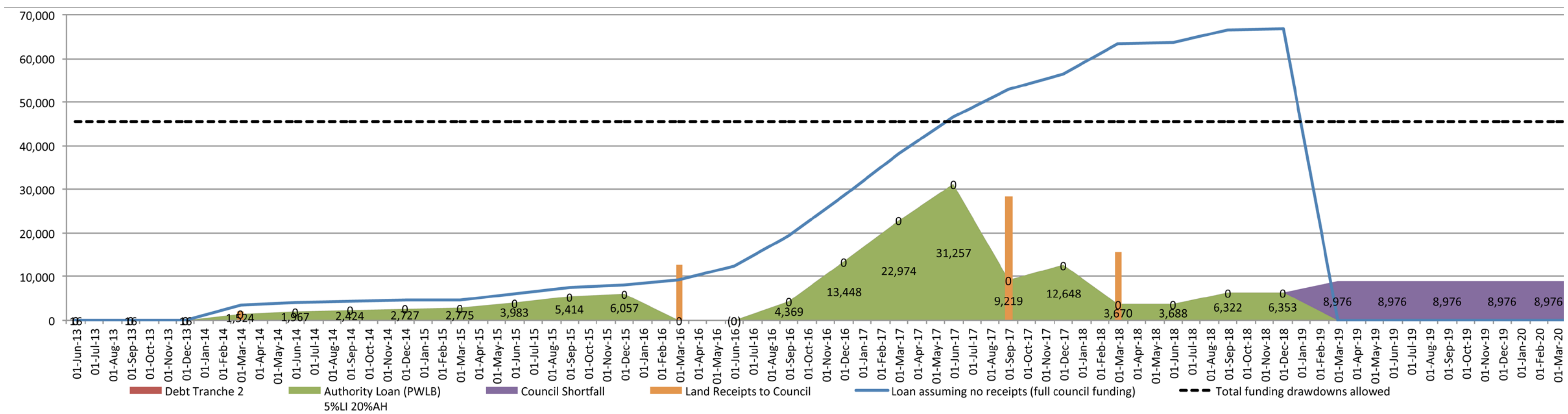
Surplus site sales are clearly stated throughout the model. Their values have been derived on a residual appraisal basis using Argus, with the resultant cashflows imported into Excel. The Argus .wcf files are submitted with the model and hard copies of each site appraisal (showing grown and ungrown values) are attached at Appendix A3.10.

Surplus site revenues are recycled into the overall development to minimise funding requirements. This is clearly identified on the Debt Balances graph below, which is extracted from the model and shows the Maximum Commitment, the financing requirements of the Council, the land receipts and the expected deficit.

The model is in line with the projected programme and incorporates the DM fees (including the discount subject to our planning and viability KPIs). It also allows the Council to identify the difference between our Base and Variant Bids and also the impact of value growth on surplus site value. The table below outlines the deficit sensitivity based on each scenario.

In calculating the costs and values, we have ignored any NPV savings associated with Olive Morris House, the £1m Wynne Road receipt, the savings in utilities and other costs that will benefit the Council and and the expected income that will be generated

On selection we would seek to ratify the model, subject to any Council requirements, to serve as a baseline tool for use throughout the development. We have included fees of £60k to allow for the model to be further developed, updated and audited throughout the process.



Debt balances

SECTION 3: FINANCIAL ROBUSTNESS
3.3 FINANCIAL OFFER AND VALUE

LAMBETH'S COMMERCIAL AND FINANCIAL RISKS

Our bid has been formulated to minimise the Council's commercial and financial risks. A Risk Register is attached in Section 2.2.5 detailing key project risks and how they will be mitigated.

Viability Risk

The viability of the scheme has always been a challenging aspect of the project. With the removal of International House from inclusion as a surplus site, the hurdle of cost neutrality will not be easily passed.

The Development Agreement has been drafted and agreed such that the Council is only committed to proceed with the development when they – exclusively – are satisfied that:

- The project is financially viable with sufficient committed surplus site receipts and a fixed price building contract; AND
- The project is sufficiently surveyed and designed to ensure all relevant risks can be transferred to the building contractor; AND
- The project is designed in line with the Council's brief through genuine co-production with stakeholders; AND
- All appropriate statutory consents have been obtained with all relevant conditions discharged and free of challenge; AND
- Financial due diligence relating to the selected building contractor is satisfactorily completed; AND
- Value for money is proven through a robust and transparent contractor tendering process.

Until all of these Conditions Precedent have been fulfilled, the Council retains the right to not proceed. The Council also retain the sole right to waive these Conditions Precedent if it is prudent and advantageous to do so.

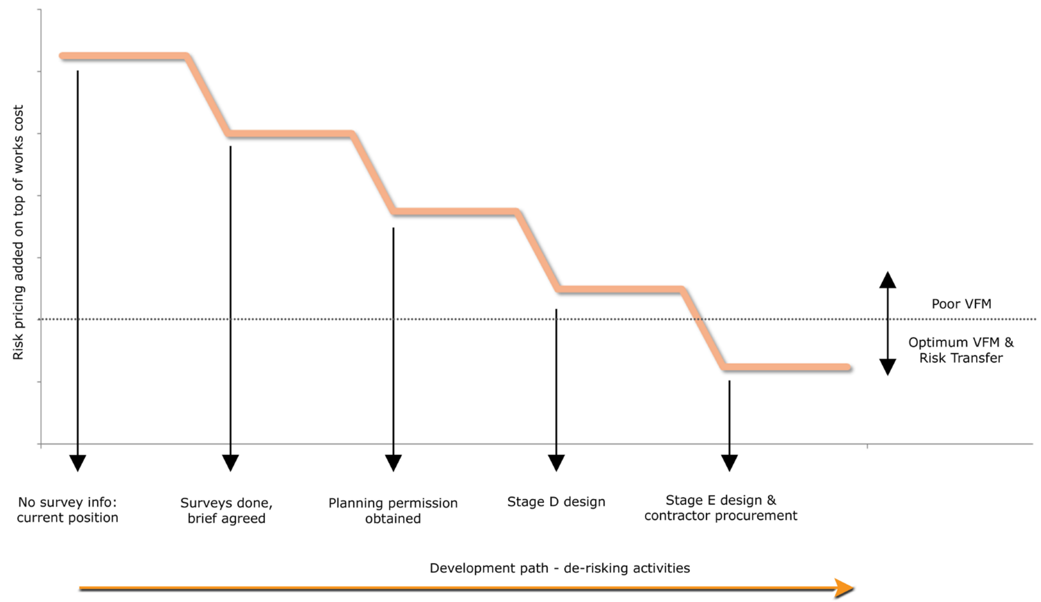
Surplus Land Value Risk

Throughout dialogue, Kajima have consistently promoted the inherent benefits to the Council of retaining control of surplus land sales, ensuring that maximum value capture is secured.

This principle creates a number of advantages and value enhancements:

- It permits each surplus site to be competitively tendered in the open market following a period of sustained growth (as outlined Section 3.2) thus capturing best value;
- It allows the Council to maintain flexibility and executive control of the sale process rather than being fettered by 'speculative' sale commitments made now at discounted values;
- Pricing is not discounted by purchaser hold costs and risk premium between partner selection and any third party on-sale, nor is Stamp Duty Land Tax levied twice;
- The Council will benefit from 100% of land value increases rather than be subject to opaque overage provisions or subjective valuation assumptions;
- Should Viability not be secured, or alternative sources of funding become available, the Council will retain complete control of the surplus land assets.

By committing to a price now, in a rising market, the Council will be crystallising a reduced surplus land value whilst limiting the full scope of opportunities to drive value. The biggest risk, in reality, is that insufficient capital receipts are captured between partner selection and the unconditional date, and our approach best mitigates this risk. The Council maintaining control at the outset reduces the risk of too great a shortfall whilst leaving current day value risk neutral.



Kajima's Value for Money Risk Mitigation Strategy

The model includes a dynamic scenario testing mechanism that allows the Council to test our inputs with and without growth. (See 'Summary' Tab Cell C6). The viability test heavily incentivises Kajima to deliver maximum value to the Council through these and any other available mechanisms.

Should an unexpected funding gap materialise, Kajima can work with the Council to seek acceptable ways to finance the shortfall. In principle options include project finance gap funding by Kajima on a basis to be agreed or through third party financing or institutional funding.

Build Cost Risk

As a core principle of our bid, Kajima is providing the Council with an effective 22.5% build cost increase guarantee over the Maximum Commitment.

As explored during dialogue, fixing the price at this stage of design in the absence of a fully scoped and specified project accompanied by, as a minimum, outline planning consent and full site and building survey information would be effectively meaningless. The nature of such an offer would materially restrict the Council's ability to subsequently flex and adapt the scheme and overall development to changing circumstances without adding to cost and, in the process, eroding value.

Kajima's proposal is to progress the design in detail, exhaustively check and study pre-existing ground and building conditions, secure planning consent and remove or quantify all reasonable risks prior to competitively tendering the construction contract to select the most suitable contractor for the project. As a result of this process, we are absolutely confident that we will be able to secure the most competitive price for the Council with a full market-leading level of risk transfer from a range of well covenanted and experienced contractors.

Davis Langdon have accurately priced the development based on known and expected risks and with an appropriate contingency for additional risk. We are also incentivised to identify all areas of cost savings for the Council's benefit. We outline this in more detail in Section 3.2. The whole project is undertaken on an open book basis.

Once the build cost is finalised following tender and agreement of the Maximum Commitment, Lambeth are protected from price increases and main contractor default by several layers. The construction cost will include appropriate contingencies against any unmitigated risk items.

Kajima's Out-turn Risk Return of 7.5% will remain subject to erosion against cost increases. After this has been exhausted, we are providing a wrap-around guarantee of 15% of the build contract. In monetary terms, Kajima is underwriting the Council's exposure to the extent of £13.3m.

Kajima is underwriting the Council's exposure to the extent of £13.3m

The basis of our bid is to simultaneously give the Council best cost and best value, as well as limit the risk of the Council against cost increases, which we believe to be the underlying principles of this process.

KAJIMA'S FEES AND RETURNS

Monies paid to Kajima by the Council project are split into two elements:

Development Management Fee

Kajima will receive a Development Management (DM) fee to cover Kajima's day to day resources in relation to the project. The total extent of the DM fee will be 2.5% of the actual main contract value for the Enterprise Centre project. However in dialogue we have agreed to incentivise the payment of this to align our interests with those of the Council.

Half of the DM fee is payable in the two years prior to starting on site, equivalent to 1.25% of the expected project value. This fee is paid monthly in equal instalments, discounted by 50% which is repaid on the grant of planning permission and once the Council confirms viability.

Should the pre-construction period extend beyond two years, an additional 0.625% is payable on a weekly basis subject to up to two periods of hiatus as dictated by the Council.

The remaining 1.25% of the DM fee (reconciled against actual build costs) is paid in equal monthly instalments over the programmed construction period.

In the event that works extends beyond the programmed construction period agreed at the unconditional date, the Council will not be required to pay any additional DM fee. This will be because either the contractor is at fault in which case our DM fee will form part of the agreed LADs or it is covered as part of Kajima's wrap-around guarantee of the build contract. The only exception to this is where the programme extends due to a Council Variation, whereby the agreed monthly rate will continue.

Our Development Management fee is competitive for a multi-site complex development such as this. We are also incentivised to successfully meet two Key Performance Indicators – receipt of planning permission and Council approval of viability – by way of discounting our fee by 50%, recoverable upon meeting each KPI. This demonstrates an aligning of interest and good value to the Council.

Based on the projected contract value, the Development Management Fee will amount to the sum of the following:

Fees received up to Planning	£220k
Planning catch up	£220k
Fees to Viability	£90k
Viability catch up	£90k

Kajima have invested £0.25m in this project thus far. This will not be recovered directly, but when discounted from the DM fee payable prior to viability it demonstrates that we do not materially benefit from our role until viability is proven. When added to internal costs incurred to date and going forward, Kajima remain at risk and our interests are fully aligned with the Council.

Legal fees associated with the negotiation and drafting of the Development Agreement form part of the project development costs and Kajima will submit an invoice to the Council for these costs upon signature of the Conditional Development Agreement, in accordance with Clause 4.1.4 of Schedule 7 of the Development Agreement.

Out-turn Risk Return

At the completion of the construction phase, Kajima are due a return equivalent to 7.5% of the total out-turn cost of the development including all construction and fees, but ignoring any finance costs and sales receipts (and associated sales costs), equivalent to £4.4m. This is in return for the 15% guarantee we are providing to protect the Council from cost over-run, delay and contractor default, worth £8.8m.

This return is fully at risk throughout the construction phase of the development and will erode on a 'pound for pound' basis in the event of cost overruns. With regard to surplus sites, we are managing pre-existing risks for the Council and therefore will take no return or overage from site sales. This also demonstrates a material alignment of interests with the Council.

We regard this to be a competitive return for the level of guarantee we are offering the Council.

STATEMENT OF CERTAINTY OF SURPLUS SITE REVENUE

Kajima have carefully considered our approach to surplus site values and undertaken primary research into the Brixton market. We are therefore as certain as we can be that the current day site values are achievable.

We have made some amendments between ISDS and ISFT submissions so that no stone is left unturned in predicting value. The biggest challenge has been to accurately portray the dynamic relationship between build costs, contractor over-costs and expected profits. We have considered how volume house builders will approach these opportunities and, whilst their bases of appraisal are opaque, we regard the reduction of profit to better reflect this dynamic relationship.

We have been more reluctant to reduce costs, or to remove contingencies, preliminaries etc, based upon the limited extent to which design has been developed, but we believe this will be a clear area where bidding parties will 'sharpen their pencils' in competitive tendering.

By advocating open market sales on a staggered basis we believe additional value will be captured. It will be better in design terms, with different developers interpreting the designs in different ways, but it also allows for each site to be secured by the keenest bidder, rather than once purchaser acquiring all and cherry picking.

The area of value that is the most difficult to state with certainty is growth and it is, in terms of forecasting, somewhat subjective. However, regardless of whether or not our view is shared by the Council, it is underpinned by forecasts by firms of agents, by government and economic data and by anecdotal evidence appearing almost daily in the news.

Kajima considers that the lack of growth for the past 5 years has resulted in pent-up pressure and will result in at least a similar length period of growth. This is well within the timetable for delivery of the Enterprise Centre, and our proposal allows for the Council to participate in this growth and benefit from 100% of the proceeds.

Even accounting for a cooling market, London has demonstrated remarkable resilience to the ills facing the remainder of the UK as a result of its established status as an international city. Brixton is part of this and we are therefore confident of our value forecasts.