

Treasury Chambers, Parliament Street, SW1P 3AG

Rt Hon Michael Heseltine MP
Secretary of State
Department of the Environment
2 Marsham Street
London SW1P 3 EB

5 March 1981

M. Heseltine

INTERNATIONAL CONFERENCE CENTRE

Thank you for your letter of ^{below.} 26 February. I am grateful to you for considering the alternatives I suggested to you. I still have the reservations I expressed in my letter of 11 February about the requirement for the Centre and the means of financing it that are likely to emerge, and may well wish to return to this question. I am however content to be guided by your view, based on professional advice, that the best means of assessing the market is to invite Healey and Baker to explore options for financing. ^{below}

As I understand it, the substance of the Cabinet decision was not that the project should proceed on the basis of private finance; but that it should not proceed unless it is privately financed. I accept however that in considering this question it will obviously be helpful to Cabinet to have a possible private sector financing package, or packages, in front of them.

I note that you will let me know the results of Healey and Baker's enquiries before reporting back to Cabinet. I am therefore content that you should proceed as you originally proposed in your letter of 31 December.

I am sending copies of this letter to the Prime Minister, Cabinet colleagues and to Sir Robert Armstrong.

Leon
Leon
LEON BRITTAN

CONFIDENTIAL

11th St
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97105
US

16 MAR 1981



*Sav
Buildings*

10 DOWNING STREET

PRIME MINISTER

Leon Brittan and Michael Heseltine are still at war over the International Conference Centre. You may like to glance at these recent exchanges: the issue could yet find its way back to Cabinet.

MA

MS.

20 March 1981



cc: PS/ma shanley
PS/ma Finberg
PS/sir R Cox
ma Delafons

File - Johnson

2 MARSHAM STREET
LONDON SW1P 3EB

My ref: H/PSO/11420/81

Your ref:

26 FEB 81

See below

INTERNATIONAL CONFERENCE CENTRE

Thank you for your letter of 11 February about the proposed International Conference Centre.

You will recall that the Cabinet approved the use of public funds for the substructure and decided that the superstructure could go ahead only if it could be financed from the private sector. To establish how best to achieve this we sought advice from four leading London firms of surveyors and also consulted David Young on their proposals. All the Agents independently offered very similar advice; one took a relatively more pessimistic view of the prospects of attracting investors, but David Young confirmed that there was likely to be no lack of interest, that we might hope to improve the terms in negotiation but that the method of financing proposed was appropriate in the circumstances.

I appreciate, of course, that what is proposed is an unusual method of financing Government building projects - although there has been plenty of experience of lease and leaseback office developments and pre-let developer's schemes that are not so very different in principle. The main innovation in the present case is that we are dealing separately with the financing and the construction of the project. The advice we have had is that the project is too big and too specialised for a single developer or contractor to finance, and that our best course is to approach the major investment institutions direct for the financing and to go for competitive tenders for the construction.

I note that your people have made the point that if one adopts a lower discount rate, it will show leasing to be more expensive than Crown-build. This comes as no surprise but the fact is that Cabinet decided that we should go for private financing and we have to get the best terms we can.

As regards the various alternative solutions that you suggest, I think we have been over these fairly thoroughly in the past, but as you have not been personally involved in those discussions it may be helpful if I explain the position in some detail.

- (1) I am not sure what you mean by "greater private sector involvement" on another site. The proposal is that private capital should fund the whole of the superstructure of the Broad Sanctuary scheme and the cost of interest during construction. If you had in mind that a developer might build on another site as a commercial proposition and rent it out to government from time to time, the answer is that there are now ample commercial conference facilities in London but they do not meet the special requirement of governmental and international conferences which are generally of a different character: the types of room required, security and accessibility are important factors, and so is the need to ensure ready availability (commercial facilities often have bookings for years ahead). In short, the type of building that the Government requires will not be built as a purely commercial proposition; but it should be possible to get private funds to finance it on reasonable terms.
- (2) You ask whether there is no way of obtaining private sector money "other than through the Healey and Baker route". Again I am not clear what you mean. We considered seeking advice from Merchant Bankers but we were told that leading London Estate Agents were the experts in seeking funds for major building projects and had access to all relevant investment institutions, pension funds etc. The Agents all produced very similar advice on the most likely sources of funds and differed only in detail on the kind of financing arrangements proposed - having considered other options such as mortgage and loan finance. David Young suggested going to Healey and Baker as they seemed to take the most positive approach. We have received enquiries about the project from major contractors and these will be referred to the Agents to take into account. But the fact of the matter is that contractors are chiefly interested in the building contract and would have to arrange financing with the institutions, which I believe would be on less favourable terms than we could get dealing direct.
- (3) Your third proposal is to incorporate an element of general purpose office development into the scheme by omitting the conference hall. If we are going for an all-purpose conference centre, this

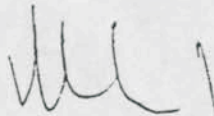
is an essential part of the scheme. It is certainly essential to have somewhere to hold plenary sessions and major press conferences, and there are some types of international conference (for which we cannot adequately cater at present) that need an auditorium of this kind. The only alternative for plenary sessions reasonably close to Broad Sanctuary is Church House, which is not always available and is somewhat confined and antiquated.

The Broad Sanctuary scheme has been in preparation for some years and on several occasions, when it has come to the point of decision, there has been a quest for alternatives. Feasibility studies have been done on adapting Somerset House, the United Services Club (before it was sold to the Institute of Directors) Richmond Yard, the Foreign Office courtyard etc. None has proved remotely satisfactory and all have been very expensive. If a Conference Centre of the kind proposed is wanted (and Cabinet decided that it was) then the Broad Sanctuary site is available and ready to start with a view to completion in 1986/87. Indeed I doubt if we could now provide adequate alternative facilities even on a temporary basis in time for the 1987 EC Presidency.

I do not think that we can do better than use what is the conventional route for obtaining finance for major commercial property developments. David Young confirmed that the project is likely to prove attractive to investors, given its location, its assured long-term occupant, prestige character and its link to office rentals in Victoria. The Agents also take this view and it means that we should be able to obtain finance on quite favourable terms. We cannot afford to delay longer if the Centre is to be ready by 1986/87; we need now to settle the financing in principle and appoint management contractors for the project if we are to keep to the timetable.

The Cabinet asked me to explore the possibilities of private finance and I think I should now do so by asking Healey and Baker to approach the institutions and other potential investors. I will ask them to let me have the results of their enquiries by the end of next month and I will then write to you again before reporting back to Cabinet.

Yours ever



MICHAEL HESELTINE

18 MAR 1981

12 1 2 3 4



Duty Clerk

With the Compliments
of the
Chief Secretary to the Treasury's
Private Secretary

As Requested

Treasury Chambers,
Parliament Street,
SW1P 3AG



Treasury Chambers, Parliament Street, SW1P 3AG

Rt Hon Michael Heseltine MP
Secretary of State
Department of the Environment
2 Marsham Street
London SW1P 3EB

11 February 1981

D. Milner,

INTERNATIONAL CONFERENCE CENTRE

I am sorry not to have replied sooner to your letter of 31 December. It took my officials a little time to discuss the details of the proposal with yours.

Your proposal was that, in the light of the discussions your officials have had with four leading London Estate Agents, from which clearer ideas emerged about the terms for financing the building of the proposed Centre from private finance, you should now invite Healey and Baker to seek offers from institutional investors on the lines proposed.

I must say that I have reservations about the proposals outlined in the annex to your letter. I am concerned about the potential costs to the Government and about the Government's involvement in the project.

On cost, my officials have had some discussion with yours about the assumptions to be used in the comparison between private finance and public finance. Calculations by my officials suggest that a more realistic assumption for the discount rate, given the estimated rental growth of 5 per cent a year, would be 7-8 per cent. This would make the option for private finance considerably more expensive than the public expenditure option, perhaps 2 or 3 times higher, contrary to the calculation shown in paragraph 8 of the annex to your letter.

As I understand the arrangements for Government involvement, the Government would continue to be responsible for construction of the building and would carry the risks that are inherent in building on such a prominent site to a tight timetable.

If we go ahead on the lines proposed, we shall be vulnerable to criticism that we are merely using leasing to evade public

expenditure controls. This could be embarrassing, particularly for your relations with local authorities, where you are proposing to score as public expenditure the capital value of leasing contracts. Moreover, the project could hardly be regarded as truly financed from the private sector at all.

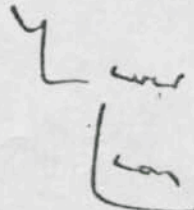
In view of these points I should be very reluctant indeed to agree to your proceeding even to the next stage (in view of the likely cost of the Agent's fees) unless we can find some way of securing a much greater private sector involvement in the construction of the Centre and its subsequent operation. Before giving you final comments and copying them more widely, I wonder if three alternatives could be examined.

The first would be to see whether greater private sector involvement would be possible on another site or in an existing building. I recognise that PSA have made every effort to identify alternatives that satisfy the FCO requirements. But are we sure that the FCO could not relax their requirements if the alternative is that no ICC would be built? I wonder for example whether there is any potential in existing or prospective developments in the Docklands area..

Second, we might consider whether there are alternative ways of injecting a private sector element into the project. Is there no way of obtaining private sector money other than through the Healey and Baker route? I expect this was a matter you considered at an earlier stage. But my fear is that Healey and Baker's ideas may now be set on the outline of the proposals and that we shall not get much movement in the terms now presented. Alternatively would it still be possible to give them a much wider-ranging remit to seek offers which would have a direct private sector involvement in the construction and later management of the building?

A third option relates to the design of the scheme. One of the reasons why the private sector cost is so high is the special nature of the project which makes it an unusual concept for the private sector to assess. Would it be possible even at this stage to contemplate an alternative which would incorporate more general-purpose office accommodation in the building at the expense of the large conference hall, which could be met elsewhere by perhaps temporary means? This should reduce the financing cost.

I should be glad of your views on this, and no doubt if you think it would be useful our officials can discuss the details. My concern is that, unless the terms of the proposed arrangements show a much greater element of private-sector risk-sharing, the Cabinet remit will not be satisfied. The alternative may well be to go back to the Cabinet with a report indicating that the private sector financing which was rightly required will only be possible if the scheme is substantially altered.


LEON BRITTAN

17 MAR 1984



Prime Minister

*In Heseltine reports
encouraging progress on
private funding for
the I.C.C.*

Carl Buildings²

2 MARSHAM STREET
LONDON SW1P 3EB

My ref:

Your ref:

31 DEC 80

Dear Chief Secretary

INTERNATIONAL CONFERENCE CENTRE

When Cabinet discussed the proposed International Conference Centre on 17 July it was agreed that the project could go ahead only if it could be financed from the private sector: I was asked to explore how that might be done.

I authorised my officials to consult four leading London Estate Agents, to explain the project in detail, and to invite their initial assessment of the prospects for private financing but without approaching the market at that stage. The Agents completed their reports in October. Three of them took a reasonably optimistic view of the prospects and two of those (Healey and Baker, and Richard Ellis) set out their proposals in very similar terms. I attach a note that summarises the approach that they recommend.

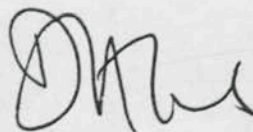
I have also sought the views of David Young on the Agents' proposals. He confirms that it is a financeable project by way of leaseback and that it is likely to be attractive to investment institutions because of its location. He was inclined to think that the development finance, reflected in the initial rent, could be got at the lower end of the 5½%-7½% range, depending on the selection of office buildings in Victoria to which future rent reviews would be geared. He also suggested that if we were starting from scratch it would be better to build the Conference Centre on a cheaper site elsewhere and to sell the Board Sanctuary site for commercial development with possibly some conference facilities provided free. But it would be unthinkable for this site to be sold for commercial development and if the Centre is to be ready by 1986, we must press on.

David Young also pointed out that the eventual rental commitment could be moderated if we carried out the development as a partnership between public and private capital. He suggested that the injection of public capital could be deferred until towards the latter half of the programme (possibly beyond the present PES period). There are attractions in the partnership concept and it would, of course, reduce the rent payable. But in terms of Net Present Value (discounting at 12% or less) it would be cheaper to meet the whole cost by private finance unless the initial rent was more than 6½%. We cannot form a view on this until we know what terms the market are prepared to offer. Meanwhile I suggest we leave this option open.

I now propose to appoint Healey and Baker (who David Young felt had taken the most positive view of the prospects) to seek offers from institutional investors on the lines proposed, and also to sound out what the attitude might be to joint public/private financing. The Government would not, of course, be committed to accepting any such offers and I will report to you on the response received.

We need to get this underway promptly as the programme requires a start on construction in the first half of 1982 and we need to open discussions soon with management contractors who will want the best part of a year for the preparatory work before inviting tenders.

I am copying this letter to the Prime Minister, Cabinet colleagues and Sir Robert Armstrong.

you see


for MICHAEL HESELTINE
(approved by the Secretary of State
and signed in his absence)

INTERNATIONAL CONFERENCE CENTRE - PRIVATE SECTOR FINANCE

1. PSA have had discussions with four firms of Chartered Surveyors (leading London Estate Agents) about the basis on which private finance for the superstructure of the International Conference Centre might be provided. Three of the firms took a reasonably optimistic view of the prospects and two presented their proposals in very similar terms (see paras 5 and 6 below).

The requirement

2. The requirement is that the building be completed in time for the UK Presidency of the EC in January 1987, in the location and to the design already agreed. The aim is to complete construction in January 1986 leaving time for contingencies and for fitting out before the EC Presidency begins.

3. The superstructure (£23.7m at September 1979 prices) is estimated to cost £32.1m at April 1982 prices (when construction should begin), spread as shown below (on the basis of a contract period of 45 months)

					£m April 1982 prices
81/2	82/3	83/4	84/5	85/6	Total
0.26	7.45	12.23	9.65	2.51	32.10

4. This cost increases to £39.6m when an allowance is made for inflation in building costs between April 1982 and January 1986; it excludes professional fees and the costs of furniture and equipment. Interest during construction at 10% to 12% brings the total cost to £51m - £54m at April 1986 prices. This is the amount that needs to be financed.

The proposals

5. The Agents advise that the approach most likely to succeed would be as follows:

- (a) A long lease of the site (125 years minimum) and leaseback of the completed building.

- (b) Funds provided by a syndicate of two or more institutions or pension funds.
- (c) Cost about £51m - £54m (including interest during construction and taking account of inflation in building costs).
- (d) Finance for construction at 10% to 12%.
- (e) Initial rent 6% to 7½%.
- (f) 5 yearly rent reviews linked to rental movements of prime offices in Victoria.

6. On this basis the initial rent starting in 1986 would be between £3m and £4m at 1986 price levels. A lower initial rent (possibly as low as 5% - 5½%) would imply a higher rate of rental growth and this would depend on the types of office building to which future rent reviews were geared.

Public/Private financing

7. The future rental payments could, of course, be reduced if the building were financed by a partnership between public and private finance - for example, with public funds meeting half the total capital cost and in the latter phase of the building programme. But at the discount rate of 12% used for this purpose the Net Present Value is less if private finance is used to meet the whole cost, unless the initial rent is more than 6½% (see para 8 below).

Comparative costings

8. On a common basis of total cost £51.5m over four years, 6% initial rent, rental growth at 5% per annum, reviews every five years, interest during construction at 10%, applying 12% discount rate the comparative Net Present Values are:

	£ million
a) Whole cost met by private finance	22.9
b) Half cost met by private finance, half by public funds in latter part of programme	24.4
c) Whole cost met by public funds	27.4

9. The apparent bias in favour of private finance reflects the fact that the market is likely to be willing to finance a development of this kind (linked to office rents in Victoria) at lower rates than apply to current Government borrowing. The high discount rate puts a much higher value on initial capital expenditure than on the long-term increase in rental costs.

PSA

December 1980

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