

ce BG
a return

070

2 MARSHAM STREET
LONDON SW1P 3EB
01-212 3434The Rt Hon John Moore MP
Department of Transport
2 Marsham Street
LONDON
SW1

My ref:

Your ref:

4 March 1987

Dear Secretary of State,

We were invited by colleagues at E(A) last week to report to them, against the background of a prospective strategy for Docklands and in the light of legal advice, on the question of continuing negotiations with Mr Travelstead and his Consortium for developing Canary Wharf.

We have now had Counsel's advice on the extent of my exposure to successful legal action in the event of negotiations coming to an end and on the handling of bringing them to an end if need be. In brief, it is that I should not be at risk of successful legal challenge if, after the present extension of the Option Agreement between them and the Consortium ends on March 6, I withdrew authority from LDDC to continue negotiating. There is no contract between me and the Consortium which the latter could seek to enforce. A claim against me for inducing a breach of contract by LDDC would depend upon the Consortium establishing that LDDC were themselves in breach of contract. I understand that they have been advised they have no contractual commitments to the Consortium provided they have made it clear their negotiations were "subject to contract". The only other basis for challenge would be to seek judicial review of the decision to terminate negotiations on the grounds that I had behaved irrationally or acted in bad faith. Counsel could see nothing in the relevant documents to suggest there was any serious risk of such a proceeding succeeding. We have consistently given notice to the Consortium of matters they have to satisfy us on. LDDC, in granting the most recent extension of the option agreement, gave clear notice that it was to be regarded as the last. I believe that Counsel's advice on your own Department's risk was similar.

Counsel advises, however, that it would be right if the Government decided that the expiry of the option agreement on 6 March was the time to signal the end of negotiations, to give the Consortium a brief period of notice and to be prepared to consider anything they had to say. Such a period need not be more than a week. Notwithstanding this advice, however, we have to recognise that, if negotiations are brought to an end, Mr Travelstead will use

every means at his disposal, including legal action, to preserve his position or recover damages.

Counsel further advised on the position that might arise if negotiations collapsed and the Government then, or subsequently, announced that it proposed to proceed with the City extension of the railway at public expense. He considered that any such decision should be deferred until after the negotiations with Mr Travelstead had broken down. LDDC have also, independently, taken legal advice. Their advice from leading Counsel is that the prospects of successful action for breach of contract against the Corporation in the event of negotiations being broken off were remote.

The basic question, of course, is whether we should now seek to end negotiations with Mr Travelstead. I have to say that I believe we should. Immediately after we met at E(A) to discuss the proposals, my Permanent Secretary again made clear to Mr Travelstead what we required by way of guarantees, and details supporting his claim to have substantial firms ready to take space in the development. Mr Travelstead promised that material by the end of last week, but nothing has been received. It follows that the conditions on which I was able to recommend to colleagues that LDDC should be authorised to agree the sale of the freehold of their land at Canary Wharf in advance of development have not been met. I have to conclude that Mr Travelstead has not been able to secure enough firm interest in taking space in the project to satisfy the banks whom he proposed as sureties. We are still in discussion with LDDC, and they with the Consortium, on the Master Building Agreement and its link with the proposed guarantees. We have not yet got a tight enough agreement. In any event, in the absence of either the guarantees or the evidence of space taken, I could not recommend that negotiations on the present scheme should continue. Unless I hear from him to satisfactory effect by March 6, I propose therefore that the Option Agreement should not be extended by LDDC and that Mr Travelstead should be given notice immediately after March 6 of our intention to withdraw support for LDDC's continued negotiations, giving him 7 days to make representations. If, against expectations, he brought forward substantial evidence within that time of having a firm deal to offer we should have to consider that.

If I do in fact hear from him before March 6 with what, prima facie, appears to be evidence that he can meet our requirements, I will have to consider, with legal advice, whether the option agreement should be extended, and for how long.

The collapse of this deal after such protracted negotiations would, of course, be a disappointment; I should warn colleagues, however, that to develop an alternative to Mr Travelstead's proposals may not be plain sailing. LDDC have been deeply committed to the success of his scheme and are not in a position

to bring forward a fully worked-up alternative at short notice. Mr Travelstead may be in a position to make life difficult for any successor through control over some key sites, or by spoiling litigation. It will be the more important therefore to present the achievements, and the remaining prospects, for Docklands in the most positive light.

The success of LDDC particularly in the last two years, in attracting private investment has been remarkable - and I acknowledge that the Canary Wharf negotiations have contributed to this. Officials have the further work in hand that will enable us to consider later this month (probably at an E(A) meeting on 23 March) firm proposals for a decision on the major commercial development for the Royal Docks and the construction of the Eastern extension of the DLR. It may well be that negotiations with Mr Travelstead will not have publicly collapsed by the time we are in a position to make a firm announcement about this. Whether or not a public rupture comes before we can announce a firm decision on the Royals, I believe we should offer a broad statement, of our strategic approach to Docklands. It would refer to:

- the striking progress made in Docklands (£1.5bn private investment);
- proposals under active consideration for development by major consortia in the Royals - worth £1.2bn;
- the Bill laid for the Eastern extension of the railway;
- our commitment to fund, through LDDC, a major East/West highway (provision made in this year's PE settlement);
- the opening of the central section of the railway in the summer;
- STOLport to become operational in the autumn;
- a number of other developers known to be keenly interested in the opportunity of development at Canary Wharf, perhaps on a slightly less grandiose scale: LDDC to open this up to a competitive process as a matter of urgency;
- as much as you feel able to say about alternative arrangements for the railway if the Canary Wharf Scheme does not go ahead.

I believe that a statement on these lines, which could also explain how far we have sought to accommodate Mr Travelstead's requirements, will be a good basis for maintaining confidence.

If you and colleagues agree, unless there is a dramatic development before the March 6 deadline, I propose to put Mr Travelstead on notice that we propose to terminate negotiations,

as set out above. I need to know that you, and others, are content by 10.00am on Friday 6th so that arrangements can be put in hand. I should be glad to know, also, if you are content with a statement on lines proposed above, to use in the event of a public rupture.

I am copying this letter to the Prime Minister and other members of E(A).

Yours sincerely

NH Leonard Private Secretary

PP.

NICHOLAS RIDLEY

(Approved in draft by the Secretary of State and signed in his absence)



The Rt Hon John Moore MP
Secretary of State
Department of Transport
2 Marsham Street
LONDON
SW1P 3EB

cc BG
2 MARSHAM STREET
LONDON SW1P 3EB
01-212 3434

My ref:

Your ref:

18 March 1987

Dear John

NBM

CANARY WHARF

I am writing to provide a further update on the position on the Canary Wharf negotiations.

Since I wrote to you on 11 March, with a copy of Mr Heiser's letter to Mr Travelstead, a meeting has been arranged between Mr Heiser and Mr Travelstead and his associates to take place today, 18 March. The outcome of that meeting, which is concerned with the question of guarantees for the infrastructure, is of great importance to the decision to be made about Canary Wharf, and about the handling of any decision, if the need arises, to break off negotiations.

I can also report that we have, since I last wrote, had replies from the firms mentioned by Mr Travelstead as being prepared to take space in the project. The overall picture is substantially less encouraging as to the prospect of firm commitment than Mr Travelstead suggested.

I will be putting to colleagues, for consideration at the meeting of E(A) on 25 March a paper on the substance and the handling of these matters, with legal advice - this will be together with the paper that we will be preparing on the Royal Docks. In the meantime, however, I see no alternative to extending the option agreement by a further week, which would take us to 26 March. We can take a considered view about next steps, including the vital presentational aspects, at our meeting.

I am copying this letter to the Prime Minister and other E(A) colleagues and to Sir Robert Armstrong.

Johnson

NBM

NICHOLAS RIDLEY

RECTORAL POLICY

DINNER CITIES



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CCBS



DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

JM/PSO/2846/87

The Rt Hon Nicholas Ridley MP
Secretary of State for the Environment
Department of the Environment
2 Marsham Street
LONDON SW1P 3EB

NRBM

13 MAR 1987

Dear Nicholas,

CANARY WHARF

Thank you for your letter of 11 March outlining the current position in your negotiations with Mr Travelstead. *FILE WITH DEN*

I agree that the evidence you have so far received from Mr Travelstead is very thin and I am content with the tactics you propose.

As regards the railway agreement, you will have seen a copy of my letter to John MacGregor of 9 March in which I reported that a meeting between my officials, LRT and Mr Travelstead on 6 March appeared to have cleared the way to an agreement. However, earlier this week LRT received a revised draft of the Agreement from the Consortium which appeared to take little or no account of the position we believed had been reached at the 6 March meeting. Subsequently, Mr Travelstead's representatives have been taking a more conciliatory line, alleging that their latest proposals reflect some misunderstandings of their lawyers.

All in all the most charitable interpretation of the Consortium's tactics is, I think, that they are still playing for time because they cannot yet deliver the assurances on the financing of their development that you have asked for. Nevertheless, LRT and my officials will of course continue in their efforts to secure an acceptable railway agreement until such time as we agree, in accordance with your proposed tactics, that the exercise has become futile.

I am copying this letter to the Prime Minister, to other members of E(A), and to Sir Robert Armstrong.

JOHN MOORE

CONFIDENTIAL

REGIONAL POLICY

INNER CITIES

PT 9



CONFIDENTIAL



Treasury Chambers, Parliament Street, SW1P 3AG

Brian Leonard Esq
 Private Secretary to the
 Secretary of State for the Environment
 Department of the Environment
 2 Marsham Street
 London
 SW1P 3EB

NBM

12 March 1987

Dear Brian,

CANARY WHARF

The Chief Secretary has seen a copy of your Secretary of State's letter of 11 March to the Secretary of State for Transport. The Chief Secretary discussed in the margins of Cabinet with your Secretary of State and the Secretary of State for Transport.

The Chief Secretary agrees the extension of the options agreement in the way you propose.

The Chief Secretary notes Mr Ridley's judgement that the absence of suitable guarantees and of other satisfactory evidence of commitment means that it will probably be impossible to reach an acceptable deal with Mr Travelstead. He considers that the case for ending negotiations with Mr Travelstead should be based primarily on these factors.

The Chief Secretary therefore considers that, in the absence of a significant improvement in the terms of the assurances provided by Mr Travelstead, we should not be prepared to contemplate further extensions beyond the date Mr Ridley has in mind except for the most compelling reasons.

I am copying this letter to David Norgrove at No. 10, the Private Secretaries to other members of E(A) and to Trevor Woolley in Sir Robert Armstrong's Office.

Yours,

Jin

JILL RUTTER
 Private Secretary

REGIONAL POLICY: Inner Cities: Pt 9





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2 MARSHAM STREET
LONDON SW1P 3EB
01-212 3434

The Rt Hon John Moore MP
Secretary of State
Department of Transport
2 Marsham Street
LONDON
SW1P 3EB

My ref:
Your ref:

Prime Minister²

Mr Ridley now looks to extend the deadline for Mr Travelstead beyond 25 March. 11 March 1987
Abt 11/3.

Dear John

Following our exchange of letters, and those of colleagues last week, a clear view emerged that we should continue to try to negotiate a deal with Mr Travelstead, if satisfactory terms could be reached; but in any case that it would be preferable for a final breakdown, if that is inevitable, not to occur before we are able, probably following E(A) on 25 March, to announce decisions on the strategy for the Royal Docks and the eastern extension.

Mr Travelstead in fact produced, late on 5 March, what purported to be the evidence we had been seeking about the commitments by his guarantors, and about taking space in the development. For that reason, as I had foreshadowed in my letter of 4 March, I authorised LDDC to extend the agreement to 12 March. There are, in any case, some points outstanding on the MBA, though these should be capable of resolution this week.

I attach copies of what Mr Travelstead provided, for the information of colleagues. It is evident that what he produced fell far short of what he had been told was required "well before" the MBA could be signed. As to guarantees, he argued that it was unreasonable to expect much better indications from his banking partners than the attached letters contain, in advance of every detail of the MBA, and the accompanying agreements, being available to them. I do not accept that. Final commitment must, of course, be held back until every detail is in place.

But the underlying principles have long been known to Mr Travelstead and should have been to his partners; almost all essentials of the agreement are in place. It would have been entirely reasonable for the banks to be much more specific about their commitment. That is what has now been made plain to him in a letter from my Permanent Secretary, a copy of which I am enclosing below. I attach much more significance to his banking partners than to the contractors who have, at a very late stage, been brought forward as guarantors.

Commitment to take space is secondary, but would provide the evidence we have been seeking of the probable pace of development on which the economic appraisal of the project turns. I am, as he invited us to do, having further checks made on what he has provided - vague though it is.

In view of the importance of ensuring that negotiations do not break down before we can take a considered view of the Royal Docks and the eastern extension, I propose that he should be given an extension of the options agreement, by letter, for a further seven days; and that we should be willing to contemplate one further, and probably final, extension next week to take us beyond 25 March. That seems to me to leave us with more flexibility than the alternative of a single extension now, with a firm warning of finality. That might unnecessarily provoke a rupture before we can be fully prepared.

I should be grateful for agreement to the course of action I propose by 10 am on Thursday 12 March.

Nicholas Ridley

NICHOLAS RIDLEY



Department of the Environment

2 Marsham Street London SW1P 3EB

01-212 8251

Permanent Secretary

Terry Hauser CB

G Ware Travelstead Esq
 The Canary Wharf Development Co Ltd
 9 Bishopsgate
 LONDON
 EC2N 4BQ

cc: Mr Goldman
 Mr McGuire
 Mr Wise
 Mr Freeman
 Mr Bradley
 PS/Secretary of State

10 March 1987

Dear Mr. Travelstead

CANARY WHARF

We have now had an opportunity to consider your letter of 5 March and the annexed document.

We are disappointed at the limited nature of the material you have now presented. As I pointed out when we met on 5 March, I made it clear as long ago as our meeting on 20 November what reassurances Ministers need to be satisfied that the immediate freehold transfer and public investment which you seek for your proposed Canary Wharf development were warranted; and that they would need them in good time.

I realise that the Bill to authorise the Docklands Light Railway extension did not receive Royal Assent until December and that you may face problems in getting a final commitment from guarantors or prospective occupiers without having a fully settled MBA or railway agreement. But what you have said in discussions with the Department has led us to believe that the banking groups whose letters you have copied to me are full members of the Consortium and have at all times been party to the negotiations and are fully informed about the stage reached.

As to the fundamental question of guarantees, it seems to me that we are in a situation in which the terms of the MBA and the railway agreement are sufficiently settled for any proposed guarantor to give a definitive, though still conditional view on the acceptability of the documentation. I consider that

Ministers can now reasonably conclude that if this project is going to get off the ground you ought to be able to provide very soon definite evidence that acceptable guarantors are committed to signing the proposed guarantee documents; of the availability of the money needed to build the proposed infrastructure and of commitments by the banks you are in partnership with to take a substantial quantity of office accommodation. We would expect prospective guarantors to say at this stage:

- (a) whether in principle they are prepared to give a joint and several guarantee for £340m for a specified period in connection with a project on the lines proposed;
- (b) whether or not the present documentation (subject to the outstanding points of which we are both aware) is essentially acceptable to them;
- (c) whether they would concurrently commit themselves to build office accommodation for themselves at the Wharf;
- (d) if so, how much and by when.

The letters you have produced are silent on these matters.

You will understand that Ministers cannot take a final view on this important proposal without having the material I have mentioned before them, with proper time to consider it. In any event, I believe that it would be desirable for us to meet senior representatives of the three banks next week. I and my colleagues would be available at short notice.

You told me there would be no objection to our approaching the undertakings you name about their intentions as potential occupiers. We are doing so confidentially.

I also note you have not offered any material about prospective contractors or building contracts beyond the letters from certain building and civil engineering companies expressing an interest

in participating and that you have not referred at all to your proposed funding arrangement with the Chemical Bank. You said at our meeting on 23 February that you were near arranging a facility with this bank and would copy the final agreement to the Department as soon as it was ready. I should be grateful if you would let me have information on these matters quickly.

Discussions between my people and the LDDC on Friday suggested rapid progress was being made to resolve the issues referred to in your letter and settling definitively the terms of an MBA and "guarantee" documents.

I am copying this to Christopher Benson.

Yours Sincerely
T M Heiser

T M HEISER

CONFIDENTIAL AND
COMMERCIAL-IN-CONFIDENCE

CC/9



Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Nicholas Ridley AMICE MP
 Secretary of State for the Environment
 Department of the Environment
 2 Marsham Street
 London
 SW1P 3EB

NRBM

6th March 1987

Dear Nicholas,

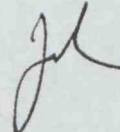
CANARY WHARF

Thank you for sending me a copy of your letter of 4th March to John Moore. *at-top*

I very much agree that the time has come to end the negotiations with Mr Travelstead's Consortium on the development of Canary Wharf and the western extension of the DLR. He has clearly failed to secure the necessary backers.

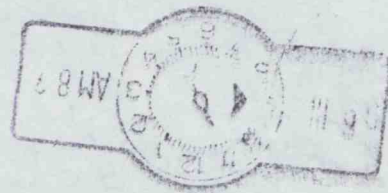
I am broadly content with your outline for a possible strategy statement on Docklands. Depending on timing you will need to be cautious about what you say on specific options for development of the Royals which have yet to be agreed. I also think it would be premature to say too much about the western extension of the DLR. I understand that LRT have identified several potential ways of linking the light railway to the underground system which are less costly than the Bank extension. It is not clear at this stage which alternative would be most cost-effective and the form of the rail link must of course depend on the scale and type of development eventually proposed for Canary Wharf. If necessary I suggest you limit comment on the western extension to a simple statement that options for linking the western end of the DLR to the rest of the public transport system are being looked at.

I am copying this letter to the Prime Minister, John Moore, other members of E(A) and to Sir Robert Armstrong.

Yours ever,


JOHN MacGREGOR

REG. POWER : Inner Cities





2 MARSHAM STREET
LONDON SW1P 3EB
01-212 3434

David Norgrove
Private Secretary to
The Prime Minister
10 Downing Street
LONDON
SW1A 2AA

My ref:

Your ref:

Prime Minister 2
DLN
6/3.

6 March 1987

mb

Dear David,

LONDON DOCKLANDS: CANARY WHARF

You will recall my Secretary of State's letter to the Secretary of State for Transport of 4 March, copied to the Prime Minister and other E(A) colleagues. This referred to today's expiry of the extended Option Agreement on Canary Wharf with Mr Travelstead and his Consortium.

Mr Travelstead came in to see my Permanent Secretary last evening, bringing with him various papers relating to the required guarantees and assurances on his proposed scheme. Officials here are now considering these, in consultation with colleagues in DTp and Treasury as necessary. In the light of this Mr Ridley has today authorised an extension of the option agreement until Thursday 12 March. I enclose a copy of the letter which Terry Heiser has sent to Mr Travelstead explaining this.

Mr Ridley is likely to write again to E(A) colleagues next week, in the light of the consideration of the papers that have now been submitted by Mr Travelstead.

I am copying this letter to Richard Allan and to the Private Secretaries of all members of E(A).

Yours sincerely
Brian Gual

B H LEONARD
Private Secretary

R12 34314



Department of the Environment
2 Marsham Street London SW1P 3EB
01-212 8051

Permanent Secretary
Terry Heiser CB

G Ware Travelstead, Esq
The Canary Wharf Development Company Ltd
9 Bishopsgate
LONDON
EC2N 4BQ

6 March 1987

Dear Mr. Travelstead

CANARY WHARF

I refer to your letter of 5 March and our meeting last night.

We obviously need to evaluate the papers which you handed me last night: and you tell me certain matters are still outstanding in connection with the settling both of the terms of an MBA which might be acceptable to all parties and of the terms of any agreement between you and LRT over the financing of the extension of the Docklands Light Railway.

The extension of the Option Agreement is for the LDDC: but the Government will not object to an extension until Thursday 12 March.

This concession should not be construed as in any way indicating that you have yet satisfied the Government on the matters on which they seek assurance.

Yours Sincerely

Terry Heiser

T M HEISER

*cc Ware
McQuinn
Goldman
Kearson
Rutman
Heiser
As/Secretary of
State*

Regional Pol; Inner Cities AT9



CC File

CONFIDENTIAL
COMMERCIAL IN CONFIDENCE

P 02558

From: J B UNWIN
6 March 1987

MR NORNGROVE - No 10

J B Unwin

Note at end.

DOCKLANDS

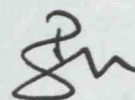
As you may have gathered, the situation reported in Mr Ridley's letter of 4 March has been overtaken by further developments.

2. Mr Travelstead delivered a bundle of new papers to DOE yesterday. While it seems most unlikely that these give the guarantees required, the legal advice is that they should not be dismissed summarily. Mr Ridley is still considering what action to take, but the likelihood is that he will reluctantly ask LDDC to extend the Option Agreement between them and the Consortium (otherwise due to expire today) for a further period (perhaps a week) while the Travelstead documents are studied.

3. If this course, which would be consistent with Mr Tebbit's approach, is followed, it will give a breathing space and avoid an immediate rupture. Mr Ridley is, however, anxious to bring matters to a head and not to let Mr Travelstead go on spinning things out. In the circumstances, I think the right tactical aim should probably be to avoid a public rupture before the E(A) discussion planned for 23 March. Ministers can then consider together how best to disengage with minimum exposure to legal redress. But it would be idle to believe that all the other issues - on the Royal Docks and on the City Extension - can be tied up on that occasion; and a break may be unavoidable before then. It may, therefore, prove necessary to arrange some further collective discussion at short notice before then (eg towards the end of next week).

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4. I understand that Mr Ridley will be writing round again before the weekend. We can consider further in the light of that.



J B UNWIN

Mr Unwin

Thank you.

The legal advice that no decision on the railway should be taken on the railway until negotiations have broken down may cause difficulty. It will remove one of the best elements of the face-saving package of announcements.

DLS

6/3.

pp's



CABINET OFFICE,
WHITEHALL, LONDON SW1A 2AS

Chancellor of the Duchy of Lancaster

Tel No: 270 0020
270 0296

5 March 1987

Brian Leonard Esq
Assistant Private Secretary to the
Secretary of State for the
Environment
Department of the Environment
2 Marsham Street
LONDON
SW1P 3EB

cc BGR
return

NBM

Dear Brian,

will request if
reg'd

The Chancellor of the Duchy was grateful for a copy of your Secretary of State's letter of 4 March to the Secretary of State for Transport.

The Chancellor would not wish the negotiations with the Consortium to be terminated until the proposals for the Royal Docks are firm, and ready to be made public. In view of the timetable for decisions on the latter, which your letter suggests would come forward to E(A) on 23 March, the proposal to give Mr Travelstead notice of the termination of negotiations would be premature, as being likely to increase the chances of a public rupture before the Royal Docks proposals are ready.

I am sending a copy of this letter to David Norgrove (No. 10), the private secretaries to other members of E(A), and to Trevor Woolley in Sir Robert Armstrong's office.

Yours Sincerely,
Andrew Lansley

ANDREW LANSLEY
Private Secretary

PPS. CC89



Department of Employment
 Caxton House Tothill Street London SW1H 9NF
 Telephone Direct Line 01-213 5949
 Switchboard 01-213 3000

The Rt Hon Nicholas Ridley AMICE MP
 Secretary of State for the Environment
 2 Marsham Street
 LONDON SW1P 3EB

5 March 1987

Dear Secretary of State,

WGM.

CANARY WHARF

I have read your letter of 4th March to John Moore. It is indeed disappointing to see that we are contemplating the failure of the project upon which the LDDC have been negotiating with Mr Travelstead's Consortium. However presented, I believe it will be seen as a serious setback to the development of our UDC policy and an embarrassment to the Government.

The tone of the letter rather suggested that we are now firmly on a course to end these negotiations and turn to the discussion of longer-term more modest proposals designed by your Department. I hope that everyone is in fact proceeding in the hope that we can still produce a satisfactory agreement within our time limit if at all possible. I trust that everyone will strive to avoid difficulties and to take a constructive view of this existing proposal to the end.

I take it that the LDDC are near to agreement with the Consortium on the Master Building Agreement. You say that in the absence of guarantees on the evidence of space taken, you still could not recommend that negotiations on the present scheme should continue. If the Consortium could come up with some guarantees and some evidence, will you be sending round to colleagues your comments on their adequacy before instructing LDDC to cease negotiations?

I am copying this letter to the recipients of yours.

Yours sincerely,

Seamus C. Clarke

PP KENNETH CLARKE
 Approved by the Paymaster General
 and signed in his absence.

2
PRIME MINISTER

cc Professor Griffiths

CANARY WHARF

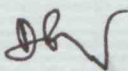
Mr. Ridley's letter below suggests that Mr. Ware Travelstead should be given a week from tomorrow to reach a specific agreement. Negotiations will then cease.

His legal advice is that this should not open the Government to a successful legal action.

I understand, however, that tonight Mr. Travelstead saw Terry Heiser and gave him a bundle of documents. The DOE view is that the proposals which they describe are not at all satisfactory. However, the DOE Solicitor believes that they must now be seriously considered and discussed with the consortium to reduce the legal risks. This is the advice going to Mr. Ridley overnight.

At this stage there seems no need for you to do anything other than note the position.

I would draw your attention to one further point. Counsel have advised that any decision to proceed with the city extension of the railway at public expense should be deferred until after the negotiations with Mr. Travelstead had broken down. This will, of course, make it more difficult to put together an attractive statement to put the best face on the breakdown of negotiations over Canary Wharf.


DAVID NORGROVE

5 March 1987

SLHAHW

CONFIDENTIAL

ce B&G
a

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DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

The Rt Hon Nicholas Ridley MP
Secretary of State for the Environment
Department of the Environment
2 Marsham Street
LONDON
SW1P 3EB

NBM

March 1987

Nicholas Ridley

CANARY WHARF AND DOCKLANDS LIGHT RAILWAY

Thank you for your letter of 4 March.

I agree that we should now bring matters to a head with the Canary Wharf Consortium and I am broadly content with your proposals for doing so. The evidence from LRT's negotiations with the Consortium is that they are simply playing for time by taking an unreasonable negotiating line, especially on the issue of revenue guarantees.

As regards the legal position of LRT and my Department, Counsel's advice is that the best course of action will be for me to put Mr Travelstead on notice of an intention to bring negotiations to end immediately after a similar communication to him from you. I would indicate that negotiations between LRT and the Consortium would have to cease since it is a condition that the Railway Agreement can only be signed if the Master Building Agreement is concluded.

You mention the need to be ready with an announcement about the future of Docklands when the talks collapse. I agree that it would be better if we could make a firm statement about the Eastern extension and related issues at the same time. This argues for a deadline which is slightly longer than the seven days you suggest to ensure that any breakdown occurs after we have been able to consider with colleagues at E(A) on 23 March the range of issues commissioned at the meeting on 23 February. But we cannot be sure that the breakdown will not occur earlier.

In that event I agree that an announcement of the kind you outlined would be necessary. We shall need urgently to prepare statements to cover both eventualities.

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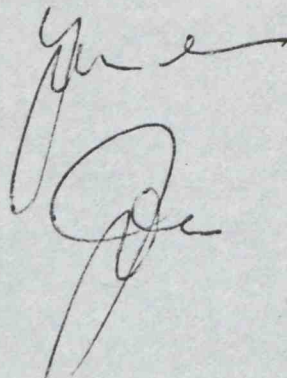
CONFIDENTIAL

The scheme for a Western DLR extension to Bank was the most expensive option (£130m), required of us in negotiation with the Consortium. If we are released from this we ought to look again at cheaper options. My officials have been discussing urgently with LRT the possibilities for a more modest but worthwhile Western extension of the railway which would link it more satisfactorily than at present with the rest of the Underground.

Whatever solution emerges for the Western terminus of the railway, a significant upgrading of the capacity of the Initial Railway will be required, costing some £45m to £50m. We shall also need to consider how we can attract private finance to meet any additional cost beyond the level of public contribution already planned. This points to a model of financing that LDDC are proposing for the Eastern extension of the railway, in this case based on enhanced land values at Canary Wharf as a result of the Western extension. I hope that you will be able to offer an assessment at our meeting on 23 March of the amount this approach could yield.

I will be in a position to describe the possibilities for a Western extension of the railway in more detail, together with their funding implications, at the 23 March meeting of E(A). In the meantime if we are forced into an early statement I suggest that we simply say on this subject that the Government is looking into the possibility of other ways of linking the initial section of the Docklands Light Railway to the Underground. That would not rule out going ahead with the Bank extension if we decided that that was sensible. But we will need to bear in mind that any announcement which implied that the Government were now prepared to contribute significantly more in public funds to a Western extension ought not to follow hard on a breakdown of negotiations with Mr Travelstead, as it could be used as evidence that the Government had acted unreasonably and in bad faith.

I am copying this letter to the Prime Minister, to other members of E(A), and to Sir Robert Armstrong.



JOHN MOORE

CONFIDENTIAL



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cc BG



Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon John Moore MP
Secretary of State for Transport
Department of Transport
2 Marsham Street
London
SW1P 3EB

NBPN.

23 February 1987

Dec JH,

DOCKLANDS LIGHT RAILWAY: CITY EXTENSION

Thank you for your letter of 20 February.

In the light of our discussions at E(A) this morning, I am content for you to authorise LRT to continue negotiations with the Consortium until 28 February on the basis you propose. At this stage it would seem premature to agree that the railway should proceed on the basis of LRT's appraisal. Whether this is acceptable depends on:

- (i) the outcome of LDDC's negotiations with the Consortium, and
- (ii) LRT's success in getting satisfactory revenue guaranties from the Consortium.

If the negotiations continue beyond 28 February, there is also the question of the Consortium's contribution to the higher capital costs which may result. We will also need to assess the overall outcome against the other options both for developing Canary Wharf and the funding of the City extension which are identified by the working group commissioned by E(A).

Finally, I note that on current projections, if the railway goes ahead, LRT will need increased resources to cover the higher capital cost of the project. I appreciate your decision to keep any additional costs in 1987-88 within LRT's existing EFL. For future years, the public expenditure implications will need to be considered in the 1987 IFR. My position remains unchanged from that in my letter of 21 April 1986 to Nicholas Ridley, namely that while I would not wish

Regional Policy

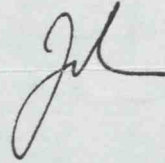
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to use this increase as a tool for an arbitrary squeeze on LRT's investment plans, equally I cannot agree in advance to increase LRT's EFL and future EFR's by the full amount of the additional costs of the DLR.

I am copying this letter to the Prime Minister, to other members of E(A), and to Sir Robert Armstrong.

Yours ever,



JOHN MacGREGOR



LONDON DOCKLANDS AND UDC'S

There are two issues:

- 1 How much further should Nicholas Ridley go in negotiations with Travelstead to financially support his expensive rail connection for Canary Wharf and the City.
- 2 How much further should Department of Environment go to develop new UDC proposals

1 Docklands: Canary Wharf and Royal Docks

The regeneration of London Docklands will be seen as one of the notable achievements of the Thatcher Governments of the 1980's. So far Ministers have rightly erred on the side of politicians in planning and funding the transport infrastructure.

However, we should be wary of getting drawn deeper and deeper into underwriting Travelstead's ambitious plans for a satellite of the City located at Canary Wharf. The project was conceived in the heady days before the City's Big Bang.

Today a dispassionate view of the case for a City satellite on this scale is questionable; indeed some of the investors are getting understandably edgy about the market outlook for such a big chunk of new office capacity. Responding to market pressures the City has relaxed its tight restrictions on new office capacity. Additional office space is becoming available in the Fleet Street area now that the newspapers are on the move. Some of the teams assembled in the pre-Big Bang scramble will

be pruned and others will be disbanded. Fierce competition is forcing rationalisation and a concentration of excessive manpower.

We would support a proposal to force negotiations with Travelstead's Consortium to a firm conclusion one way or the other by the end of February. The Government has already done more than enough to facilitate the Consortium's grand design for Canary Wharf. The risk investors must now make their judgement of whether there is a market for such a development.

The fallback of a less grandiose development may well be more in keeping with the existing character of Docklands. This should not be regarded as second best.

We continue to support strongly the Eastern extension of the Docklands Light Railway and the development of the Royal Docks area.

2 UDC's Generally

Officials at DoE have independently proposed an exciting scheme that coincides with the results of our research over the last 18 months. This is likely to be mentioned by Nicholas Ridley on Monday.

We aim:

- (i) to bring in Government deregulation and ^{from} freedom for local constraints where Local Government has totally failed to remove dereliction without saddling Central Government for direct responsibility for local housing;
- (ii) to reduce the cost of UDC's;

(iii) to enable us to tackle comparatively small pockets of dereliction, even as little as 30-40 acres, which nevertheless in the provincial context are very significant such as the Calder Valley or the site in Central Bradford that you may have seen.

Option No 1

We agree with one DoE option which achieves all three aims. This would enable a regional or sub-regional UDC to be created (similar to the Welsh Land Authority) which could apply full UDC powers to the derelict sites, some of them quite small. We could thus speedily overcome the land ownership mosaic problems by vesting all the land in one agency which has a duty to sell on at once. Because of the speedy sale envisaged this proposal would require little money, but needs to be fully costed. A variant on this proposal is:

Option No 2

Bring in regional UDC's as in No 1 but then charge the Development Agency with a variety of functions (a) cleaning up the site - clearing it and removing toxic and other waste, (b) building and developing all before sale. For financial reasons we are against this option, though on occasion we might remove toxic waste.

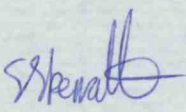
Option No 3

We also propose a bargain basement or "cashless" UDC. This would be little more than a super-simplified planning zone in a given area. In this the vesting powers of a UDC would be given to roving Commissioner (no big office blocks!). Instead of spending money in purchasing the property as in Options 1 and 2, the commissioner could facilitate the land

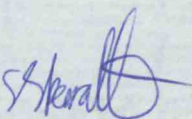
assembly of derelict sites and the onward sale to private sector developers who are currently hamstrung by regulation. The land would vest in the Commissioner for a notional five minutes in a series of transactions transferring land to a developer.

Conclusion

We are very cautious about further public money being put behind Travelstead. We recommend a committee be formed to consider new UDC options.

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JOHN WYBREW

pp 

HARTLEY BOOTH

cc B/G
cc Blup

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PRIME MINISTER

London Docklands

[E(A)(87) 4; Letter of 19 February from the Secretary of State for the Environment to the Secretary of State for Transport]

This is an extremely complex issue on which the papers circulated (apart from the map) are not the clearest. For convenience I have summarised the key issues on one side at Annex A attached. The remainder of this brief deals with them a little more fully.

DECISIONS

2. The issues for decision are:

i. whether negotiations with the consortium proposing to develop Canary Wharf should be broken off if they cannot produce substantial evidence to justify the scheme proceeding by 27 February;

ii. whether the Government should support the eastward extension of the Docklands Light railway to the Royal Docks.

These decisions must be taken in the light of the strategy for London Docklands and, for the UDC programme generally.

BACKGROUND

Canary Wharf

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OF THE PUBLIC RECORDS ACT

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THIS IS A COPY. THE ORIGINAL IS
RETAINED UNDER SECTION 3 (4)
OF THE PUBLIC RECORDS ACT

4. It was agreed earlier that in order to secure this major development LDDC might exceptionally be authorised to pass the freehold to the consortium in advance of development taking place, provided the consortium could satisfy the Environment Secretary on a number of points and give guarantees that the development would go ahead. The present 'option agreement' with the consortium (first signed in May 1985) expires on 6 March.

5. In parallel, London Regional Transport (LRT) are in negotiation about the construction of the westward extension of the Dockland Light Railway (DLR). This is important to the commercial viability of Canary Wharf, and the consortium have therefore agreed in principle to contribute £45 million in Net Present Value to the total cost, most recently estimated at £130 million cash. LRT also have to be satisfied about revenue guarantees in order to justify their part of the investment. The Bill authorising the westward extension received Royal Assent on 19 December. Tenders for the construction of the extension expire on 28 February, and there is a risk of cost-overrun if this date is passed.

Royal Docks

6. The 270 hectares of land around the Royal Albert Dock and King George Five Dock are the last major area for development. LDDC are negotiating with three consortia for an intensive commercial and housing development. A key feature will be the eastward extension of the DLR to provide access. E(A) agreed last November that LRT might deposit before Parliament the necessary Bill to authorise construction on the basis that the Government would consider its attitude towards the proposal before the second reading, now planned for mid-March. The Environment Secretary suggests (paragraph 11 of E(A)(87) 4) that he should indicate Government support for the Bill, provided LDDC can satisfy him the scheme is viable.

THE ISSUES

7. The central issue is the attitude which the Government should take to the proposals for the development of Canary Wharf and for the Royal Dock. These are both very substantial schemes, and significant amounts of public money are involved in providing associated infrastructure. If both go ahead, the scope for investment in other UDCs within present public expenditure plans will be substantially reduced. There is therefore at least a case for switching the emphasis of UDC development from Docklands to the Midlands and the North; and although Mr Ridley does not actually say this, it is clearly at the back of his mind. On the other hand, he recognises that LDDC has been a substantial success story and that there is a case for continuing to build on it.

8. The problem is also compounded by the fact that the position on the LDDC projects is continually changing as negotiations proceed. The potential developers are naturally reluctant to disclose all their cards at the outset, and information reaches the Departments concerned only through the LDDC and LRT, who have their own set of objectives. Decisions will therefore have to be subject to review as circumstances require

9. For the purposes of discussion, the Canary Wharf and Royal Docks decisions can be regarded as separate. If Canary Wharf does not proceed, and the westward extension of the railway is dropped, the land values around the Royal Docks will be slightly reduced, but (in the view of DOE) not so much as to change significantly the economic or financial case for the Royal development and the eastward extension of the railway (Row F of Annex A to E(A)(87) 4).

Canary Wharf

10. The immediate issue is whether the Government should now set a final deadline for negotiations, so that if Mr Travelstead cannot provide the evidence and guarantees required by 27 February and complete all the negotiations by 13 March his project will be dead. In this case LDDC will need to consider alternatives, and

Mr Ridley suggests (paragraph 9 of his paper) that there is a more modest fall back option.

11. The economic appraisal shows that the consortium scheme is marginally preferable to the fall back. But the fall back will require substantially less public expenditure. Over the three years to 1989/90 the Canary Wharf scheme (assuming the westward extension of the railway proceeds) will produce a surplus of £34 million, whereas the fall back scheme (without the railway) would produce a surplus of £63 million. These surpluses would be available through the urban block for investment in other UDCs, including the four which Mr Ridley announced at the last Party Conference.

12. I understand from DOE officials that Mr Travelstead is unlikely to be able to produce the necessary evidence by next Friday. The degree of commercial interest in taking up space in the development has been less than expected. The City of London has recently changed its planning policies (partly because of the threat from Canary Wharf) so there will be more space in the city itself, and the opportunity generated by the Big Bang may now have passed. So from Mr Travelstead's view point Canary Wharf it becoming less viable. Indeed, DOE officials believe it is possible that he will never be brought to the point of signing an agreement. But he will not want to appear to be responsible for the break. If the Government make the first move, he can be expected to be vocal in putting the blame on them.

The Royal Docks

13. LDDC are in negotiation with three consortia about various options. No firm proposals are yet on the table. But the current indications are that intensive commercial and housing development together with an eastward extension of the railway make sense in economic and financial terms. For that reason, Mr Ridley suggests that he should indicate support for the LRT Bill on second reading.

14. The Committee's agreement in November that the Bill might be deposited was on the basis that the Government would need to be satisfied before second reading that:

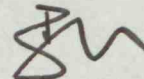
(i) the outstanding issues on the westward extension had been resolved;

(ii) there would be no significant risk that any of the costs of the eastward extension would fall as a burden on LRT.

As indicated above, it now appears that the westward extension is not a precondition for the viability for the eastward extension, and that, subject to that being confirmed, there is no direct link with the Canary Wharf negotiation. Mr Ridley reconfirms (paragraph 11) that he would need to be satisfied that the increased land values would be sufficient to avoid the need for additional public expenditure and that there would be no revenue risks on LRT. Subject to that, there appears no objection to the course now suggested.

HANDLING

15. You will wish to invite the Environment Secretary to introduce the discussion. The Transport Secretary will wish to speak on the negotiations between LRT and Mr Travelstead. The Chief Secretary, Treasury and other Ministers will also wish to contribute.



J B UNWIN

Cabinet Office
20 February 1987

LONDON DOCKLANDS DEVELOPMENT: ESSENTIAL POINTSCANARY WHARF

A decision is required next week on whether to break off negotiations with Mr Travelstead unless he can show satisfactory progress by 27 February

Arguments for breaking off are:-

- (i) DOE have identified a cheaper alternative (which saves £43m in net public expenditure and £70m for LRT on the Docklands Railway);
- (ii) the Consortium seem most unlikely to be able to show satisfactory progress in time.

Arguments for continuing negotiations are:-

- (i) the scheme is very imaginative and has received great publicity;
- (ii) the Government might well be blamed;
- (iii) there could be legal problems.

ROYAL DOCKS

A decision is not needed so quickly. The Bill authorising extension of the Docklands Railway to the Royal Docks is due for Second Reading in March. The Government will then have to declare its hand. This will depend on whether the extension will cost extra public expenditure. The DOE figures suggest not; but they need more examination. Treasury and DOE should be asked to arrange this.

OTHER UDCs

Mr Ridley's real motive in reducing the Docklands cost seems to be to spend more on UDC's outside London. 4 have been announced (Trafford Park, Black Country, Tyneside and Teeside); he wants to set up other "low budget" UDCs elsewhere. If he succeeds on Docklands, he can do this within his block. But he might still want extra provision. This should await PES. No decision is needed now. If Mr Ridley wants to press this, he should do so later on the basis of a proper paper.

CCB9

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

The Rt Hon John MacGregor OBE MP
Chief Secretary to the Treasury
HM Treasury
Treasury Chambers
Parliament Street
LONDON
SW1P 3AG

20 February 1987

This letter is intended to bring you and colleagues up to date with the position on the proposed extension of the Docklands Light Railway into the City and to highlight the decisions we need to make.

Appraisal of Scheme

My letter of 15 January to Nicholas Ridley mentioned that LRT had submitted a revised appraisal of the extension of DLR to Bank. We have now had an opportunity to carry out a detailed assessment of this paper and a copy of our analysis, which has been revised in the light of comments from your officials, is attached.

You will see from the analysis that the financial case for the project is no longer as robust as it appeared last March and it now seems unlikely, on the basis of a £45M NPV contribution from the Consortium, that it will achieve a 5% real return in financial terms. The project can however be justified if the quantifiable transport benefits to passengers are taken into account.

Given that the overall benefits from LRT's viewpoint are marginal the case for proceeding with the Extension is far from clear cut. Certainly we could not justify building the Extension if the Canary Wharf negotiations collapse since that would worsen the financial outcome at least to the extent of the Consortium's £45M NPV contribution, and the effect of lower revenues on the system. However, if we should collectively conclude that the Canary Wharf development proposal is still worth securing, and the development does in fact go ahead, then I believe the economics of the Extension are sufficiently sound to justify its approval.

Negotiations with Canary Wharf Consortium

Since my letter of 15 January, negotiations between LRT and the Consortium have resumed. It is still possible that a deal can be concluded by 28 February. LRT have not been able to secure an increase in the capital contribution of £45M NPV from the Consortium. However, the Consortium have agreed to drop their proposal that part of their contribution should be paid in the form of an annuity over 20 years. This will slightly improve LRT's cash flow as well as dispensing with the cumbersome and contentious annuity mechanism.

As at 13 February, LRT believed they had secured a breakthrough on the question of protection for their revenues in the event that development at Canary Wharf does not proceed at the pace or to the extent assumed in the railway appraisal. In recent discussions the Consortium's negotiators have conceded the principle that, insofar as development falls short of the levels assumed in the railway agreement, they should reimburse LRT for the consequent shortfall in revenue on an agreed formula. This would result in LRT receiving some £½M (March 1986 prices) each year for each 1M sq ft by which development falls short of their target. There would also be a cut off point (currently envisaged as the date on which building is due to be completed under the Master Building Agreement (MBA)) at which any remaining potential shortfall would be capitalised and paid to LRT as a lump sum. If final agreement could be reached on this, LRT would be protected from one of the most significant remaining areas of risk.

However LRT received a letter dated 17 February from the Consortium in which they attempt to renege on these crucial concessions on revenue guarantees. This may signal an attempt by the Consortium to pick a quarrel as a basis for breaking off negotiations. LRT are continuing to negotiate on the lines mapped out in the discussions but there must now be doubts about whether an acceptable agreement is attainable.

If revenue guarantees could be secured, the deal would offer LRT a high degree of certainty and protect them from risks associated with the Canary Wharf development. However, it would still be less than ideal in terms of the amount of capital on offer from the Consortium. The Consortium have consistently refused to increase their capital contribution and contend that LRT and Government have accepted the risk of capital cost overruns. If we were to try to insist on further capital contributions now they might well use this as an excuse to accuse us of bad faith and break off the deal. My conclusion is that to avoid giving the Consortium a pretext for accusing us of sabotaging the negotiations, LRT should continue to negotiate along current lines, at least up to 28 February.

Public Expenditure Implications

If the project goes ahead, the increase in estimated capital costs means that the resources earmarked in LRT's EFL and planning figures for the next three years will not cover their share of the cost of the extension. The appraisal sets out the extent of the likely shortfalls, taking into account the latest changes in the anticipated spending profile and the timing of the Consortium's payments. It has already been agreed that the shortfall in 1987/88 will have to be met from within the resources approved for LRT already during that year. But, without increased provision LRT will be unable to find the additional resources required in 1988/89 and 1989/90 without making cuts in their own investment programme. Your letter of 21 April 1986 accepted that their involvement in the City Extension project would not be used to impose an arbitrary squeeze on their investment programme. If we do agree that the Extension project should proceed, I shall therefore need to be in a position to assure LRT that we accept, in principle, that the deficit will be covered in the next IFR round.

Timing

The tenders received by LRT expire on 1 March and contractors will almost certainly increase their prices if LRT have to seek an extension. LRT have therefore put the Consortium on notice that they will expect them to meet any costs incurred due to delay in signing the MBA and Railway Agreements (assuming that the Agreements are in fact eventually signed.) However, if LRT are to be able to maintain this stance it will be important to be able to show that LDDC or the Government had not contributed to the delay. Otherwise, we could be faced with a need to find further public resources for the railway. The amount required will be affected by the length of any delay in finalising the agreements and it is important that LRT should have the clearest possible idea of when the agreements will be signed before asking contractors to extend their tenders or submit new ones.

Conclusions

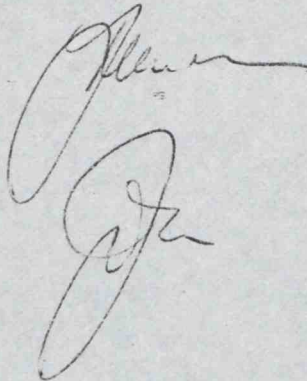
We are to have a discussion in E(A) on 23 February on the future of the Canary Wharf project and the tactics for bringing negotiations to a speedy conclusion. Subject to that I would welcome your agreement to the following course of action:

- (i) that I should inform LRT that we are prepared to see the railway proceed on the basis of the figures contained in the appraisal provided that an acceptable agreement can be reached with the Consortium;

(ii) that I should authorise LRT to continue negotiations with the Consortium on the basis I have outlined with a view to being in a position to sign an agreement by 28 February;

(iii) that I can inform LRT that should the project go ahead we will be prepared to agree that, other things being equal, the increased resources needed to cover the increased capital cost of the project will be taken into account in the 1987 IFR.

I am copying this letter to the Prime Minister, to other members of E(A), and to Sir Robert Armstrong.

A handwritten signature in dark ink, appearing to read 'John Moore', written in a cursive style.

JOHN MOORE

Introduction

1. Last March, on the basis of an outline appraisal, Ministers approved in principle a deal with the Canary Wharf Consortium on the funding of the City Extension to the Docklands Light Railway. This paper considers in detail LRT's latest appraisal of the project.

Development of the Proposal

2. When Ministers gave approval in principle to the project the proposal was for the City Extension to be built with sufficient capacity to serve a 10M square feet development at Canary Wharf at a capital cost of £103M (at outturn prices). To reduce their financial exposure should the Canary Wharf development not exceed 5M sq ft, LRT developed an option to build the railway in two phases: the first to serve 5M square feet by September 1990 at a capital cost of £93M; and a second phase to serve a further 5M square feet, should it be built, costing £16M, principally for additional rolling stock. The increased total cost of the phased option reflects the diseconomies of deferring part of the rolling stock order.

3. These proposals were prepared taking into account the traffic that would arise from 19,000 other jobs being created in other parts of the Isle of Dogs. However the promotion of Canary Wharf and the enactment of the City Extension Bill have already generated increased development interest and concrete plans for more intensive development than originally envisaged. LDDC have accordingly revised their assessment of the non-Canary Wharf jobs upward to 39,000. LRT have re-assessed the capacity requirement for the railway in the light of this employment forecast and they now propose that the first phase should provide similar capacity to that required to serve a 10M sq ft development at Canary Wharf with only 19,000 other jobs.

4. In the meantime the capital cost estimates for the project have increased by some £27M bringing the total estimated cost of the railway needed to serve the anticipated demand to £130M. A breakdown of the cost increases is given in Annex 1. They largely reflect additional unforeseen requirements arising from the nature of the site, problems identified during project design and negotiations with potential tenderers and higher costs for land and the settlement of Parliamentary Undertakings.

APPRAISAL

5. The financial appraisal has been based on the following:

- i. A discount rate of 5% real (the required rate of return) as previously agreed with HM Treasury, on the basis that a high proportion of the capital and revenue income from the project is to be guaranteed by the Consortium;
- ii. Appraisal over 50 years with due account being taken of renewal costs including the residual value of recently renewed assets at the end of the period;
- iii. Inflation taken to remain at 5% throughout the appraisal period;
- iv. Cash flows discounted to March 1986, the date of the agreement in principle with the Consortium on funding.

Capital Costs

6. The Net Present Value (NPV) of the capital costs on the above basis is £111M, towards which the Consortium have agreed to contribute £45M NPV. They originally proposed to provide this as a cash contribution of £45M during construction with the balance, to the value of £45M NPV, being provided as an annuity payable for 20 years after completion of the railway. They have now agreed instead to make their contribution wholly

during construction, on a pound-for-pound basis with LRT, and want to retain the option of a single cash payment. The revised payment schedule confers substantial advantages in reducing the immediate call on public expenditure but does not affect the appraisal. Asset renewals over the life of the project are assessed to cost an additional £12M NPV.

Operating Costs

7. LRT have established revised operating costs for the initial railway of £3.8M a year (1986 prices). The cost of operating the extension to Bank would add £2M by the time the service was operating at full capacity in January 1993, making a total operating cost of £5.8M (1986 prices) to service a 5M sq ft development at Canary Wharf, with 39,000 jobs elsewhere. The operating costs, over the life of the project, total £33.6M NPV.

Revenues

8. Assuming a 60% public transport modal share for all journeys to work in the Isle of Dogs and 80% for journeys to Canary Wharf, the maximum number of trips on the whole railway each year is expected to be 36.6M. Fares are assumed to be maintained at LRT levels throughout. The revenue from the railway, in the year of opening, 1989-90, is estimated on the basis of 3.2M sq ft of occupied space at Canary Wharf, to be £3.9M (1986 prices). This will grow to £9.6M (1986 prices) per annum when there is 5M sq ft of occupied space at Canary Wharf (from 1990-91) and, as well, all 39,000 non-Canary Wharf jobs are in place in the Isle of Dogs (from 1993-94). The discounted stream of revenues amounts to £96.4M NPV.

Network Benefits

9. LRT consider that the opening of the extension will not have a significant effect on the net revenue of the bus subsidiary. Losses caused by transfer of a significant number of bus passengers to the City Extension will be offset by

additional journeys generated by the development itself. The effects on the Underground are more difficult to assess. LRT estimate that increased patronage will produce additional gross revenue of £2-3M; but they believe this may amount to only £1M pa, net, when increased operating costs, through the need to increase service levels, are taken into account. This gives an NPV of £15.8M.

10. This is the weakest area of LRT's appraisal. It is possible that they have over-estimated the network benefits likely to accrue in practice. The LRT estimate assumes that all trips on the Underground resulting from the Canary Wharf development and the new jobs in the Isle of Dogs are completely new to the network; it makes no allowance for transfers from the rest of the network, nor does it include a detailed study of any additional costs which might be incurred to cope with increased demand on the network.

Summary of Financial Appraisal

11. The results of the financial appraisal, drawn together below, demonstrate that if the Canary Wharf development proceeds as planned (3.2M sq ft by September 1989 and 5M sq ft a year later) and the anticipated growth of jobs elsewhere on the Isle of Dogs materialises (39,000 by 1993-94), the project is at best marginally viable. Its justification in purely financial terms is weakened by the fact that little reliance can be placed on the assessed contribution of network benefits.

NPV - £M 1986 Prices

Capital Costs	(110.75)
Developers' Contribution During Construction	45.00
Asset Renewals	(12.02)
Operating Costs	(33.56)
Revenue	96.42
	<hr/>
	(14.91)
Network Benefits	15.80
	<hr/>
NPV Benefit to LRT	+ 0.89

Non-Financial Benefits

12. While the financial justification of the project is very weak LRT estimate it would yield significant non-financial benefits worth £31.85M in present value terms. Standard cost-benefit techniques have been used to assess the value to passengers of savings in their journey times which the City Extension will bring about. Benefits to passengers travelling to and from the new development at Canary Wharf have been excluded from this analysis as it can be argued that the Consortium's contribution is being paid to secure these benefits. If these non-financial benefits are taken into account the project can be justified even if the estimated network benefits are disregarded.

RISKS AND SENSITIVITIES

A. Discount Rate

13. For reasons explained above, the discount rate used in this appraisal is 5%. The effect of using the 7% discount rate, more usual in public transport appraisals, is to reduce the financial NPV of the project by some £12M, leaving it viable in cost-benefit terms.

B. Capital Costs

14. The cost estimates have been refined as the scheme has been developed. We believe the £130M estimate for the project is not now susceptible to large further increases for the following reasons:

- i. tenders have been received for the Tunnels and Banks Station contract, which are in line with the estimates.
- ii. the estimates include an amount for the upgrading costs (both civil, E&M systems and rolling stock) which is based on the latest offer from GEC/Mowlem;
- iii. the service pattern and rolling stock units provide 20% spare capacity over the predicted demand.
- iv. the sizeable contingency in the estimate - currently about 10% - provides a substantial cushion against the risk of overspending.

15. If costs were to increase by 10% spread evenly over the construction period the financial NPV of the project would worsen by some £11M. If the increases were concentrated at the end of the construction period the effect would be slightly smaller.

C. Operating Costs

16. The other element in the equation is operating costs. These are closely based on the operating costs identified for the Initial Railway, most of which are now becoming firm, and it is therefore unlikely that there will be serious overruns in these costs. These costs are in any case a relatively minor component in the appraisal; even if they were to increase by 10% over the whole life of the project, this would worsen the financial NPV by only some £3.4M.

D. Traffic and Revenues

17. This is the area of greatest potential uncertainty and risk. The case analysed above assumes 5M sq ft of development at Canary Wharf by September 1990 and 39,000 jobs in the Isle of Dogs by 1993. There are therefore two main components in the traffic figures which need to be considered separately.

18. Canary Wharf Traffic: The viability of the extension is heavily dependent on the size and timing of development at Canary Wharf. If, instead of proceeding to the timetable assumed in the appraisal (ie. 3.2M sq ft net occupiable space by September 1989 and 5M sq ft net by September 1990) the Consortium build at the rate envisaged in the draft Master Building Agreement (ie. 3.8M sq ft net by March 1992 and 4.3M sq ft net by September 1993) the NPV of the revenue lost to LRT would be some £12M. If nothing were ever built at Canary Wharf the lost revenue would be worth up to £43.5M NPV. The size of the potential revenue losses underlines the need to secure revenue guarantees from the Consortium sufficient to cover the NPV loss associated with shortfalls in development; and liquidated damages covering the whole loss in the event of total default.

19. Jobs Elsewhere on the Isle of Dogs: The forecast of 39,000 jobs elsewhere on the Isle of Dogs has been provided by LDDC and reflects the high level of interest being shown by developers in the Isle of Dogs. There are now firm proposals for most of the available sites, many of which are ready to proceed if the railway goes ahead. LDDC believe that construction of the railway rather than development at Canary Wharf is the key trigger to commitment by other developers. They are therefore confident that their estimate is robust. If it is not there would be a significant impact on the viability of the railway; a 20% reduction in non-Canary Wharf traffic would reduce revenue to the railway by some £10.6M (NPV).

IMPLICATIONS FOR PUBLIC EXPENDITURE

20. The increase in capital costs, means that the provision made in LRT's EFL and planning figures for the cost of the extension is insufficient, as demonstrated by the table at Annex 2. It can be seen there will be difficulties in all three IFR years. LRT have already been told that the shortfall in 1987/88 will have to be found from within their existing EFL. We believe they should be able to achieve this by deferring other capital investment schemes. However, without an adjustment to their planning figures, we do not believe they will be able to find the extra £10M needed in 1988/89 or £8M in 1989/90 without making damaging cuts in other major capital investment projects. Large cuts in these years were made in the 1986 IFR and we doubt that significant additional asset sales can be secured (beyond those allowed for in the IFR). They will be very resistant to making such cuts and will want an assurance of increased resources before committing themselves to build the City Extension.

FUTURE DEVELOPMENT

21. To allow for the possible future development of Canary Wharf to 10M sq ft (as envisaged in the Consortium's original scheme) the LRT appraisal also includes a case which assumes this level of development is reached by 1997 when there will

be 39,000 jobs elsewhere in the Isle of Dogs. This will necessitate a higher capacity railway and will consequently mean additional capital cost of about £6M for the strengthening of structure and platform extensions and £13M for extra rolling stock, a total of £19M at outturn prices including suitable contingencies. This results in the following financial appraisal, which does not include any allowance for network benefits nor LRT's estimated £31.85M NPV in passenger benefits:

	NPV - £M 1986 Prices	
	Incremental Effect of Further Phase	Total for Both Phases
Capital Costs	(12.97)	(123.72)
Developers' Contribution During Construction	-	45.00
Asset Renewals	(2.04)	(14.06)
Operating Costs	(5.51)	(39.07)
Revenue	32.17	129.13
	<hr/>	<hr/>
Net Financial NPV	12.19	(2.72)

22. It can be seen that the project would become much more financially viable, notwithstanding the need for additional expenditure, if the second phase of the Canary Wharf development were to take place.

SUMMARY OF CONCLUSIONS

23. The City Extension can be built to provide the capacity required by the Consortium and within the timetable specified by them at a likely maximum cost of £130M.
24. The projected financial performance of the project is now significantly less good than anticipated at the time the outline agreement on funding was struck with the Canary Wharf Consortium. The project's own internal cash flows would have a net present value of about -£15M on the most likely scenario. LRT estimate that this could be more than cancelled out by potential increases in net revenues on other LRT services but we do not believe their figures to be sufficiently robust to be relied on in justifying approval for the project.
25. The project can still be justified if non-financial transport benefits are taken into account and these are sufficiently large to provide a substantial buffer against downside risks.
26. The risks of a further worsening of the financial performance of the railway are limited, provided that guarantees on the development timetable for Canary Wharf can be secured from the Consortium.
27. There is one risk which it has not been possible to assess fully which is that the extension might generate capacity problems elsewhere on the network which would create a need for additional investment. While LRT do not believe this will occur, no detailed analysis has been carried out.
28. The provision in LRT's EFL is insufficient to cover the cost of the project, particularly in 1988/89.

DOCKLANDS LIGHT RAILWAY - CITY EXTENSION

SUMMARY OF COST INCREASES

	<u>£m</u>
Railway to serve 10m square feet Canary Wharf Development and 19,000 other jobs on Isle of Dogs, as approved in principle	103
1. <u>TUNNELS AND BANK STATION</u>	
(a) Improved interchange with District and Circle Line at Monument - to partially meet City Corporation's objections -	2.0
(b) Loss of Shorter St site - developer found to have planning consent for initially proposed tunnelling site, additional costs in only having one working site -	2.3
(c) Diversion of British Telecom cables - cables discovered to run directly across patch of new tunnel, LRT to reimburse BT's costs for raising cables -	2.5
(d) Underpinning adjacent GRE building - as part of agreed settlement of Parliamentary petition -	0.9
(e) Staff facilities etc at Bank Station -	0.9
	<hr/> 8.6
2. <u>UPGRADING - CIVIL WORKS</u>	
(a) Additional strengthening -	0.8
(b) Excess Mowlem tender price over LRT estimate -	1.2
	<hr/> 2.0
3. <u>UPGRADING - M & E WORK</u>	
(a) Additional cost of signalling	3.2
(b) Revised rolling stock requirements - 20 standard units instead of 13 extended units and 3 standard units modified to extended units	2.2
	<hr/> 5.4

£m

4. LAND AND ASSOCIATED COSTS

Shorter St - cost of changing foundations
of new development to make room for railway
tunnel -

2.5

GRE - additional cost of relocating telephone
exchange in basement of GRE building to allow
escalator link to be built -

3.0

Other increases in land costs and compensation
to third parties affected by the railway -

2.8

8.3

5. CONTINGENCIES

Pro rata increase -

2.8

27.0

RAILWAY TO SERVE 5m sq ft + 39,000

130.0

CITY EXTENSION TO DLR : EFL ALLOCATION

	TOTAL EXPENDITURE	CONSORTIUM CONTRIBUTION	NET COST TO LRT	EXISTING EFL PROVISION	ADJUSTMENT TO EFL
	£m	£m	£m	£m	£m
86/87	12	6	6		
87/88	52	26	26	13	+ 13
88/89	44	22	22	12	+ 10
89/90	19	-	19	11	+ 8
90/91	3	-	3	(outside) (IFR period)	
	<hr/> 130 <hr/>	<hr/> 54 <hr/>	<hr/> 76 <hr/>		

ESTIMATE AS AT 18.2.87. - PTL(d).

REGIONAL COUNCIL

ANNEX CITIES ●

P 79



CONFIDENTIAL

CCBG



DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

The Rt Hon Nicholas Ridley MP
Secretary of State for the Environment
Department of the Environment
2 Marsham Street
LONDON
SW1P 3EB

For E(A) follow,
Monday.

20 February 1987

NBM

Dear Nicholas,

CANARY WHARF NEGOTIATIONS

WITH DRN

Thank you for your letter of 19 February which we are to discuss with colleagues together with your paper E(A)(87)4 on 23 February.

I agree that we must now seek to bring matters rapidly to a head since prospects for an agreement with the Consortium do not look bright, and any further substantial delays are bound to drive up the cost of the DLR Bank extension. I cannot be sure that we could recover these costs from the Consortium.

If we are to extend the deadline for the railway negotiation, currently set at 28 February, it is important that I try to give LRT as much certainty as possible about the extended timescale. Your suggestion of an effective final deadline of some two weeks after the date of expiry of the extended option agreement, 6 March, would certainly achieve that.

I am copying this letter to the Prime Minister, to other members of E(A), and to Sir Robert Armstrong.

JOHN MOORE

CONFIDENTIAL



Receivable

Policy
Invoice card
PT 9

Blythe



BF // For E(A) on Sunday.

2 MARSHAM STREET
LONDON SW1P 3EB
01-212 3434

The Rt Hon John Moore MP
Department of Transport
2 Marsham Street
LONDON
SW1

My ref:

Your ref:

19 February 1987

Dear Secretary of State,

In my paper E(A)(87)4, to be discussed on Monday 23rd, I undertook to consult colleagues further about the handling of further negotiations with the Canary Wharf Consortium, the background to which was described in the paper.

I said then that the major question was whether the Consortium had secured enough firm takers of space to be willing to sign its commitments under the City rail extension and Master Building Agreements. I referred also to the agreements that negotiations could proceed on the basis of watertight and enforceable assurances by the banks themselves for the construction of "infrastructure" as a proxy for development - provided other aspects of the negotiations were satisfactorily concluded. The economic assessment to which I referred would justify a decision to approve the project at a level of 4.6m sq ft of development - though only marginally; and we would therefore need to be assured of at least that much development taking place on the timescale proposed.

The assurances by the banks were in themselves no more than a safety-net ensuring that in the last resort a mechanism was in place that would ensure that the infrastructure was completed. I attached more importance to our satisfying ourselves by evidence to be provided by the Consortium that the development was really likely to take place on the scale, and timescale proposed. In particular, we have asked the Consortium, and made it clear that we would need it well before approving the signature of the MBA, for evidence about:

- the guarantees (ie the assurances mentioned above) from the Consortium's international banking partners (the terms of these would have to be acceptable to us);
- the lending arrangements with the third party commercial banks;
- progress with construction and design contracts;
- letting arrangements with firms committed to taking a substantial volume of space.

The Consortium have, in the last four weeks, been negotiating vigorously, after an extended lull, on details of the Master Building Agreement, and on the form of assurances to be provided by the banks. It is still possible that agreement on the content of the MBA and the form of the assurances may be reached by 28 February - although I understand that the prospects of a satisfactory Railway Agreement by that time may be receding. However, the Consortium have produced nothing of substance on any of the points of evidence set out in paragraph 3 above, of which over-ridingly the most important are evidence of commitment by the sources of funding and guarantee.

I am tempted to conclude that the Consortium do not have the evidence that would justify us in authorising LDDC to continue negotiating for more than a very short further period. The original proposal by Mr Travelstead, to which we agreed, was that all the necessary agreements should be completed within 30 days of Royal Assent for the Rail Extension Bill, which took place on 19 December. The Consortium were given notice in mid-January that the extension of the "option agreement" to 6 March then agreed should be seen as the final one. The longer negotiations go on, the more risk there is of discredit both for LDDC and the Government; we must certainly avoid a series of inconclusive extensions. The last date of currency of the tenders for the City extension of the DLR is 28 February, and we have set this as the target for completing negotiation. I understand that there is a real risk of cost over-run if this date is passed.

I propose that Mr Travelstead (who is to meet my officials early next week) should be told that unless he can produce substantial evidence, on the matters mentioned above to demonstrate that there is a scheme which would justify us in proceeding, we must bring the negotiations to a close. I suggest that he is asked to produce this by the end of the coming week ie 27 February. We should need to evaluate what he produced by that date, and I will keep colleagues informed at that stage. If we cannot do so to our satisfaction by the date of expiry of the extended option agreement on 6 March, I would nevertheless make it clear to Mr Travelstead that we would not authorise any extension of the option agreement as such. We should, however, set a final deadline of not more than a further 2 weeks.

We may well expect that the Consortium will take legal action at whatever point negotiations break down. Our legal advisers are not in a position to be certain, but do not think that the Government is vulnerable to successful legal action if we proceed as I propose. We do not however fully know what LDDC's legal position is; they are taking Counsel's advice. I do not think, in any case, that these considerations should inhibit us from acting as I propose.

It will be important to maintain confidence in Docklands if these negotiations collapse, as I now expect - there are good

indications of substantial interest for alternative development at the Canary Wharf site. I would then urgently discuss the next steps with Christopher Benson, the Chairman of the LDDC.

I am copying this to the Prime Minister and other members of E(A).

Yours sincerely

BH Leonard 77.

(Private Secretary)

NICHOLAS RIDLEY

(Approved by the Secretary of State and signed in his absence)



CCB6
✓

CONFIDENTIAL

P 02516

From: J B UNWIN
17 February 1987

MR NORRGROVE

Mr Woolley
cc Mr Monger
Mr Roberts

LONDON DOCKLANDS: E(A)(87)4

ATTACHED

Mr Ridley has now circulated the above paper on strategic choices for London docklands and on UDCs generally. We must now decide how to handle this.

Issues

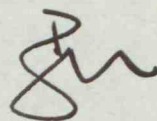
2. The paper is extremely complex, if not confusing. The immediate issue is the negotiations with the Canary Wharf Consortium which are due to be completed by 28 February unless an extension is agreed. Mr Ridley exposes a dilemma facing the Government. The Canary Wharf scheme is marginally preferable to other alternatives on economic grounds, and will be very prestigious; but it is more expensive in terms of public expenditure, and will limit what Mr Ridley can achieve with UDCs elsewhere in England. However the paper does not seek any decisions at this stage: it is presented as essential background reading. Negotiations between LDDC and the Consortium are currently in train and Mr Ridley promises a further paper on handling and tactics which we hope will be circulated tomorrow. Even this will not seek any final decisions, but Mr Ridley quite sensibly wants a steer from his colleagues on how hard the LDDC negotiators should be encouraged to try next week in seeking to secure the development. The urgency is the 28 February deadline referred to above. Beyond that, Mr Ridley appears to be trying to slip in some general presumption in favour of more resources for UDCs to strengthen his hand in the next Survey.

CONFIDENTIAL

Handling

3. There has been a thought that it might be possible to take this paper at the meeting of E(A) before Cabinet on Thursday. But I imagine the Prime Minister will want to concentrate this meeting on the main item in prospect (the Rover Group) and it seems unlikely in any case that Mr Ridley's further paper will be available in time. Moreover, the Chief Secretary, who is essential to this discussion, is unavailable (he has a prior commitment to appear at the press conference at Greenwich).

4. I therefore recommend that we should take the docklands paper at the E(A) meeting provisionally arranged for 11.30 next Monday (23 February). This is not ideal for many Ministers and we should not normally want to arrange a meeting like this for a single item. But we cannot go beyond Monday if E(A)'s views are going to be taken into account in next week's negotiations. I should be grateful to know if this is acceptable to the Prime Minister.



J B UNWIN

Cabinet Office

PRIME MINISTER

2

HOUSING IN THE DOCKS

I understand you were asking how much housing would be created by the docklands developments. The answer is some 25,000 in total by ^{the} early 1990s. East Docklands is expected to produce around 7,000 houses.

DN

ms

DAVID NORGROVE

5 February 1987

COMMERCIAL-IN-CONFIDENCE

pp's (only)

Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Nicholas Ridley AMICE MP
 Secretary of State for the Environment
 Department of the Environment
 2 Marsham Street
 London
 SW1P 3EB

3M
 3 February 1987

Dear Nicholas,

CANARY WHARF DEVELOPMENT

Thank you for your letter of 23 January from which I note that you and John Moore are strongly of the view that the two negotiations with the Consortium on the Canary Wharf development and the western extension of the DLR should remain separate.

I am prepared to accept this, though it is essential that your two Departments and LDDC and LRT ensure that the negotiations are closely co-ordinated so that the Consortium are left in no doubt at any stage as to what the Government's overall requirements on both projects are. If there is confusion, we will give the Consortium the opportunity to play one side off against the other, with the potential result of increased costs falling on the public sector.

On the question of your PES provision for all UDCs I am grateful for your confirmation that you will ensure that sufficient resources are made available for Canary Wharf in 1987-88. Any eventual agreement to the project would need to be on the expectation that you will also meet the associated public expenditure costs in future years from within the provision for UDCs that we agreed in last year's Survey, though there are, as you say, several other major issues to be resolved before we can decide whether the Canary Wharf project should go ahead.

I am copying this letter to the Prime Minister, John Biffen, Norman Tebbit, David Young, John Moore, John Wakeham and Sir Robert Armstrong.

Yours we,
Jul

JOHN MacGREGOR

REG POL: Inner cities pt 9



WJB

2 MARSHAM STREET
LONDON SW1P 3EB
01-212 3434

The Rt Hon John MacGregor OBE MP
Chief Secretary
HM Treasury
Parliament Street
LONDON
SW1

My ref:

Your ref:

23 January 1987

*Dear Chief Secretary,**NBM*

CANARY WHARF DEVELOPMENT

Thank you for your letter of 20 January in response to mine of 13 January to the Secretary of State for Transport.

The "freehold guarantee" route is now, as you say, the only practicable way forward and I am grateful for your agreement that negotiations should proceed on this basis. There are, as you point out, several major issues that will have to be resolved before any final proposal emerging from these negotiations can be approved and I will, of course, consult colleagues further before such approval is given.

As John Moore points out in his letter to me of 15 January, it is important that we co-ordinate our approach on the MBA with LRT's negotiations on the City extension of the London Docklands Railway. Officials in my Department already hold weekly meetings with LDDC with officials from Treasury and Transport represented as necessary to discuss progress on the MBA. Effective co-ordination between the two Departments does not, however, necessarily imply that the basis of the two deals, and the guarantees they offer, have to be identical. On the contrary, I, and I believe John Moore takes the same view that by taking the two sets of agreements separately we will be able to obtain guarantees from the Consortium, which are more clearly tailored to the particular needs of LDDC and LRT than we could by seeking a single blanket commitment. I have explained why the form of agreement set out in my previous letter is as strong a commitment to ensuring development as I believe is achievable. I understand also why John Moore and LRT believe that more specific, and in effect more stringent, requirements are needed to safeguard LRT's revenues. I think the important thing from John's point of view is to secure an effective assurance of sufficient revenues to ensure the required return on the Railway project. It may prove more sensible to express the requirement in these terms in the Railway Agreement, rather than explicitly in the form of a guarantees development timetable. But however it is expressed I would not wish him to relax his line, even if that means specifying different rates of development in the two agreements. Of course, in the final stages of negotiation, there is still hard bargaining to be done on both fronts.

I can confirm that I will remain within the agreed PESC provision for UDCs in 1987/88, although I am still determining the relative priority of the different elements under this heading. I will, of course, ensure that there are sufficient resources to cover potential expenditure under Canary Wharf, since without them the negotiations will collapse. So far as future years are concerned, it is too early for me to give the sort of commitment that you are seeking, although I will, of course, take what you say into account when putting together my Department's proposals for the next round.

I am copying this letter to the Prime Minister, John Biffen, Norman Tebbit, David Young, John Moore, John Wakeham and Sir Robert Armstrong.

Yours sincerely,

JH Leonard Private Secretary

PP.

NICHOLAS RIDLEY

(Approved by the Secretary of State and signed in his absence)

HESTONAL POLICY
ZINKER CITIES
PT 9





Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Nicholas Ridley MP
Secretary of State for the Environment
Department of the Environment
2 Marsham Street
London
SW1P 3EB

NRM

⁴⁴
20 January 1987

Dear Nicholas,

CANARY WHARF DEVELOPMENT

Thank you for sending me a copy of your letter of 13 January to John Moore. att:ap

From what you say, I am willing to accept that the development of the Canary Wharf by Mr Travelstead's Consortium is only likely to proceed if agreement can be reached with them using the "freehold/guarantee" approach you describe. I am also inclined to agree that alternative approaches such as leasehold must now be ruled out.

As you recognise, it is essential that the guarantees given by the Consortium's financial backers are watertight and I too would need to be satisfied on this point. Evidence of firm commitment from potential tenants of the office development, from contractors to construct the infrastructure and that the Consortium's financing arrangements are satisfactory must, as you say, also be obtained before the agreement is signed. You must also be clear yourself that the development of Canary Wharf can be successfully completed in the event of a default by the Consortium.

All that said, I still have a number of serious worries about your proposal which need to be resolved before I would be happy for the Government to approve the project. The first of these is the effect your proposed approach will have on the LRT's negotiations with the Consortium on the eastern extension of the Docklands Light Railway to which John Moore refers in his letter of 15 January. I agree with John that it is vital that our approaches to the separate negotiations on the MBA and the Railway be concerted.

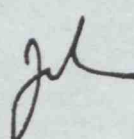
COMMERCIAL IN CONFIDENCE

I am concerned that what you are proposing is not consistent with what LRT will require to ensure the viability of the railway. While I have not yet seen the revised appraisal of the railway project, John's letter suggests that LRT will also need to negotiate separate, specific guarantees on the scale and pace of development or an increased capital contribution from the Consortium to ensure the viability of the railway. Given the likely objections by the Consortium to an increased capital contribution, surely it is giving the Consortium the wrong impression of HMG's overall requirement if you were to reduce your requirements concerning the occupancy of the development as you propose. Would it not be preferable to adopt an agreed approach to the negotiations whereby we seek similar commitments from the Consortium in the context both of the railway and the office development?

Second, the Government cannot of course approve the project until a satisfactory economic appraisal has been completed and we are all content that the project as a whole, including the railway extension is viable. I understand that there are problems with the methodology used by Peat's in the appraisal they have made. Our officials will be discussing these with Peat's shortly but I will need to be convinced about the methodology and the results of the appraisal before the project is finally approved.

Finally, I am concerned about the public expenditure aspects. It is not clear to me how you will fit all your proposed UDC activities into the increased baselines we agreed in the last Survey, given your current proposals not only for Canary Wharf but also for development of the Royal Docks and the eastern extension of the DLR and for the four new UDCs. I will need to know before you authorise LDDC to proceed with the Canary Wharf negotiations how you intend to fund all these activities within your agreed provision.

I am copying this letter to the Prime Minister, John Moore, John Biffen, Norman Tebbit, David Young, John Wakeham and Sir Robert Armstrong.

Yours ever,


JOHN MacGREGOR

CB35



DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

The Rt Hon Nicholas Ridley MP
Secretary of State for the Environment
Department of the Environment
2 Marsham Street
LONDON
SW1P 3EB

15 January 1987

Prime Minister²

mt

JRS

16/1

Nicholas Ridley

CANARY WHARF DEVELOPMENT

Thank you for your letter of 13 January about negotiations with the Canary Wharf Consortium. I note that you are proposing to authorise LDDC to negotiate an agreement on the basis of a freehold/guarantee arrangement. I see the force of arguments for this approach, but it has to be recognised that the absence of enforceable development guarantees in the MBA will make it harder to secure them in the railway agreement. It will be vital over the next few weeks for us to concert our approaches to these separate negotiations.

My concern is the risk to LRT's revenue if development at Canary Wharf is slower or to a lower level than assumed in the railway appraisal. So LRT still need to negotiate separate, specific guarantees on the scale and pace of development, significantly quicker than that included in the draft MBA, to provide the traffic LRT require to avoid serious revenue losses. If they cannot secure the development guarantees they are seeking, LRT may need, as an alternative, to seek an increased capital contribution from the Consortium to cope with the extra risk they would be running.

I am glad that you will insist on substantial letting commitments before you allow LDDC to sign the MBA. Obviously this is a matter of keen interest for us and I hope your officials will keep mine fully informed, since it could have an important bearing on LRT's tactics in the railway negotiations.

LRT have submitted a revised appraisal of the railway project which my Department is examining urgently. As I explained in my minute to the Prime Minister on 21 November there has been a substantial increase (now estimated at up to

CB35



DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

The Rt Hon Nicholas Ridley MP
Secretary of State for the Environment
Department of the Environment
2 Marsham Street
LONDON
SW1P 3EB

15 January 1987

Prime Minister²

mt

JWS

16/1

Dear Nicholas,

CANARY WHARF DEVELOPMENT

Thank you for your letter of 13 January about negotiations with the Canary Wharf Consortium. I note that you are proposing to authorise LDDC to negotiate an agreement on the basis of a freehold/guarantee arrangement. I see the force of arguments for this approach, but it has to be recognised that the absence of enforceable development guarantees in the MBA will make it harder to secure them in the railway agreement. It will be vital over the next few weeks for us to concert our approaches to these separate negotiations.

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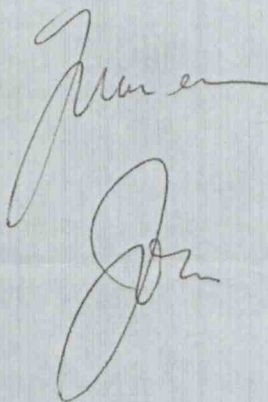
CONFIDENTIAL

£25m) in LRT's forecast cost of the railway since we agreed a provisional deal with the Consortium back in the spring. There seems little prospect of recouping this increase through a larger Consortium contribution since we took the risk of capital cost overruns. This means that the railway is by no means certain to be viable in purely financial terms. We shall need to satisfy ourselves before giving our collective approval for the railway project to go ahead that the likely benefits will outweigh the costs. If we do authorise the project that will require additional resources in 1988/89 onwards to finance it.

For these reasons I hope you will make clear that the Government's commitment to the project is still subject to the satisfactory conclusion of an agreement on the railway.

The Consortium are suggesting to LRT that the negotiations should resume next week and LRT will be pressing them to adhere to their latest target of the end of February for an agreement to be reached. This is an important target date since delay beyond then may mean that contractors increase the prices in the tenders LRT have obtained. It is important therefore that both sets of negotiations should adhere to this timetable.

I am copying this letter, as yours, to the Prime Minister, John Biffen, Norman Tebbit, David Young, John MacGregor, John Wakeham and Sir Robert Armstrong.



JOHN MOORE

CONFIDENTIAL

Regional Policy : Inner Cities Policy and Problems.



CCB/JS



CABINET OFFICE,
WHITEHALL, LONDON SW1A 2AS

Chancellor of the Duchy of Lancaster

Tel No: 270 0020
270 0296

15 January 1987

Robin Young Esq
Principal Private Secretary to the
Secretary of State for
the Environment
Department of the Environment
2 Marsham Street
LONDON
SW1P 3EB

NBPN

Dear Robin, at flap.
CANARY WHARF DEVELOPMENT

The Chancellor of the Duchy has seen your Secretary of State's letter of 13 January to the Secretary of State for Transport.

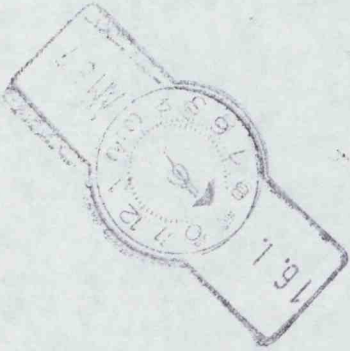
The Chancellor agrees with your Secretary of State's proposal that he should authorise LDDC to negotiate on the freehold/guarantee basis described in the letter.

I am sending a copy of this letter to the private secretaries to the Prime Minister, Lord Privy Seal, Secretaries of State for Employment and Transport, Chief Secretary, Chief Whip, and to Sir Robert Armstrong.

Yours Sincerely
Andrew Lansley

ANDREW LANSLEY
Private Secretary

REG POL: lanes cibis pt 9.



C/BG



The Rt Hon John Moore MP
 Department of Transport
 2 Marsham Street
 LONDON
 SW1

Prime Minister 2
 Mr Ridley proposes to
 transfer land to the
 consortium subject to
 various undertakings.

2 MARSHAM STREET
 LONDON SW1P 3EB
 01-212 3434

My ref:

Your ref:

The final paragraph
 suggests that the whole
 project may be losing
 momentum.

13 January 1987

Dear John

DLW

14/2 AT FLAP PT8

CANARY WHARF DEVELOPMENT

I last wrote to you and other colleagues about Canary Wharf on 9 July 1986 in advance of the meeting that you and I had with Mr Travelstead (on 23 July). This letter is to bring you and other colleagues up-to-date before I authorise LDDC, with your agreement, to move to the next stage of negotiations.

On that occasion we were ready to agree that in order to secure this major development LDDC might be allowed to pass the freehold of their land to the Consortium, in advance of development taking place, provided there were watertight assurances that the development would be completed as agreed. We were then talking about development of at least 5 million sq ft of office floorspace.

An alternative was also accepted - namely, for the freehold transfer to be supported by an undertaking that the Consortium would construct the whole of a defined infrastructure and for this to be supported by watertight "guarantees" from their financial backers. In effect, the latter - a "freehold/guarantee" approach for major infrastructure works estimated to cost about £300 million - would be relied upon to provide the necessary assurance that the Consortium and their backers would subsequently commit themselves to office development of a substantial enough volume to justify the investment of the public expenditure involved. This guaranteed infrastructure would include substantial car parking, shopping and other public space on a number of floor levels, as well as the usual service provisions for the site; and it would stand, in effect, as a proxy for the major office development which it would support.

The successful development of Canary Wharf on the scale envisaged by the Consortium - involving private investment of more than £1 billion - would undoubtedly be a success for us. But there are, inevitably, uncertainties in the market for development on this scale which we must recognise.

I have accepted - my advice from Christopher Benson and our external advisors is clear on that point - that for the land deal it would not now be realistic to try to secure guarantees of a specified volume of office development which would depend upon wider market conditions some years hence. But I am now assured that there is a form of undertaking for the freehold/guarantee -

as outlined above - which would be legally enforceable. It could also provide a satisfactory assurance against some of the principal risks which can arise after entering into a deal on this scale.

These principal risks are, first, that though the Consortium funds the infrastructure satisfactorily, an inadequate volume of office development takes place subsequently, or follows on an unacceptably long timescale. At the time that a deal is struck we will need to have evidence of substantial letting commitments for offices as well as of the infrastructure investment, so that we can be satisfied that the risk of a low level of development is minimal. We will then also need to reach the judgement that the Consortium and their backers will require a volume of office development which will not only be enough to remunerate their own investment but will also be enough to justify the Government's contribution.

Secondly, we shall ensure that the risk of abortive public expenditure is minimised. I do not anticipate too much difficulty in that: the level of financial commitment of many of those involved from the private sector will be high from the outset and that will reinforce their determination to see things through. But this will need to be kept under close scrutiny.

Thirdly, the risks of the Consortium's abandoning the project before completion of the infrastructure or, fourthly, of their selling off land at a substantial profit immediately on signing the Master Building Agreement must be guarded against. Here the undertaking given independently by the Consortium's financial members will be crucial. It will ensure that the £300m infrastructure will be funded - and that infrastructure will be a useful asset for the regeneration of the area.

Its main features and the other terms of the agreement which I propose should now be negotiated are for:

- (1) the Consortium to agree to build the infrastructure (within a set timetable), which would cost about £300 million and be sufficient to support 5m sq ft of office space;
- (2) the Consortium to agree to build (but not to guarantee to build) a minimum 5.4m sq ft of completed office development - with an expectation of final developed space in excess of that;
- (3) LDDC to sell the freehold of the greater part of the land required for the development;
- (4) LDDC to provide specific local roads and other infrastructure, in a phased programme, in support of the development. (The currently estimated cost of this is about £50 million - but details are still to be negotiated);
- (5) the agreement to be accompanied by a separate

undertaking by members of the Consortium (Credit Suisse First Boston, First Boston International and Morgan Stanley International). This would be to provide LDDC on the basis of independent documentary evidence of a breach of the agreement, such as a Surveyor's Certificate - with a sum of money sufficient to complete the guaranteed infrastructure; and for

(6) LDDC to retain a key parcel of land which would only be available to the Consortium on completion of the privately funded infrastructure and of a specified volume of building.

I am now satisfied that a structure of this kind, which would rest on undertakings from major banks, could be acceptable in principle, and which is as "watertight" as we could hope to negotiate with anyone.

A final deal will, of course, depend on Government's approval of the precise terms of the agreement and on a satisfactory result from the economic appraisal, which rests primarily on the increase in land values in the areas which are attributable to the project. This appraisal - which is currently being updated - is designed to answer Government's concern that wide economic benefits should arise from the development. This is a wider objective than meeting the more sectoral interests of our agents, LDDC and LRT. We shall, therefore, also need to reach a firm view here. It is not yet certain that the appraisal results will show these benefits to be sufficiently worthwhile - compared with those that might be obtained with less ambitious ideas for development but at a lower cost.

I would also not permit LDDC to proceed to signature until we have evidence of firm undertakings by bodies committed to taking a substantial volume of building (as noted above); and evidence of the contractors' commitments to construct the infrastructure and of the Consortium's own financing arrangements. Such a basis for confidence would be necessary for any project of this scale; but it is particularly important in this case.

You and other colleagues will be aware that the arrangement now proposed is novel particularly in its early release of the freehold to the Consortium. But the size and nature of this development is unprecedented in this country. So I am satisfied that LDDC's normal mechanism - of offering only a building licence to developers in the first instance - would not permit the Consortium to finance building on this scale. We also explored the possibility of entering into a leasehold arrangement, with an option of converting the leasehold to freehold on completion of the privately funded infrastructure. But it would not be feasible on the present timetable. It would be difficult to devise a structure satisfying both LDDC's obligations and those of the Consortium's lenders and lessees. It looks a less attractive arrangement than the one which, on firm advice, I now propose we should pursue. And it would put back the negotiations to square one.

Finally, I recognise that the project for the City extension of the Docklands Light Railway will need to be justified financially in its own right - although its cost is already taken into account in the economic appraisal. This will require assumptions to be made about traffic levels, and hence about the pace and scale of development, which may well have to be different from those in the land deal. You will also be seeking protection against a variety of risks - and I hope that our officials can remain closely in touch for the remaining stages of the negotiation to concert our approach. The public expenditure implications for that will be for you to consider.

The public expenditure bill to be met by LDDC specifically for the project - and more widely for the Roads programme in Docklands - has already been taken into account in the last PESC settlement. The basis of the present allocation is that LDDC would carry over sufficient resources including receipts from 1987/88 to enable them to fund their full programme.

In conclusion, I should welcome your, and other colleagues', agreement to my authorising LDDC to negotiate agreement on this - freehold/guarantee - basis. I shall make it quite clear that all of the precautions spelt out in this letter must be followed and that adequate safeguards against identified risks are taken.

I should welcome an early response. A letter ought to go to the Consortium by the end of this week to keep the negotiations moving. There are signs that they are flagging: it may be that Mr Travelstead is unable to secure sufficiently firm interest among potential occupiers to justify his yet going further. But he may also need some assurance of our good faith as well. I think that it may be difficult to strike a deal; but that we should keep trying with, perhaps, some more pressure on the timetable. When I have seen how far we get in this next period I will consider the position and be in touch with you again as need be.

I am copying this letter, as before, to the Prime Minister, John Biffen, Norman Tebbit, David Young, John MacGregor, John Wakeham and Sir Robert Armstrong.

*Yours
Nicolas*

NICHOLAS RIDLEY

Roa. Polict Unner Cotes PT9

