

# Finance and Resources Committee

10.00 am, Thursday, 12 May 2016

## Additional Function Space and Offices Project - Investment Sale of Atria Offices

<b>Item number</b>	8.4
<b>Report number</b>	
<b>Executive/routine</b>	Routine
<b>Wards</b>	11 - City Centre

### Executive summary

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In June 2010, the Council approved the investment decision to proceed with the construction of the Additional Function Space (AFS) and Offices project, which involved the construction of an expansion to the Edinburgh International Conference Centre (EICC) and a speculative grade A office development. The approved funding model required that the office development was leased, and then sold, to repay the costs of construction and development.

This report asks Committee to note that the construction project has now been delivered on programme, and within budget, and that the office development (Atria) has been sold to Deka Immobilien GmbH for a gross price of £105.25m.

### Links

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<b>Coalition pledges</b>	<a href="#">P17</a>
<b>Council outcomes</b>	<a href="#">CO7</a> , <a href="#">CO8</a>
<b>Single Outcome Agreement</b>	<a href="#">SO1</a>

## Additional Function Space and Offices Project - Investment Sale of Atria Offices

### Recommendations

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That Committee:

- 1.1 Notes the successful completion of the Additional Function Space (AFS) and Offices construction project on time and within budget; and
- 1.2 Notes the investment sale of the offices (Atria One and Two) as shown outlined red on the attached plan, for a gross price of £105.25m.

### Background

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- 2.1 The original business plan for the expansion of the Edinburgh International Conference Centre (EICC) was predicated on the private sector delivering the project. However, in October 2007, after the sudden and unexpected withdrawal of the private developer Cala/AWG, the Council authorised EICC Ltd to initiate the procurement process for direct development of the Additional Function Space (AFS) and Offices project. Authority was granted to procure the professional team to allow the scheme to be fully developed and tenders sought for the construction contract.
- 2.2 Reports in March 2008 and January 2010, confirmed that the project was progressing within budget and programme and that the procurement for the principal contractor was ongoing.
- 2.3 In June 2010, the Council noted that a viable project business case and funding strategy were in place. Consequently, Council approved the investment decision to proceed with the project; approved the funding strategy and total development budget of £85m; and authorised EICC Ltd, as agent for the Council, to enter into a formal contract with Sir Robert McAlpine for the construction. In recognition of the need for the team to act promptly, and with strict confidentiality as commercial opportunities arose in relation to the letting and sale of the offices, the Council granted authority to the Director of City Development (in consultation with the Director of Finance and Head of Legal and Administrative Services) to enter into, amend or terminate legal agreements as required to achieve delivery of the project.
- 2.4 The project comprises the construction of two floors of subterranean multi-function space providing a total of approx 149,000 sq ft (13,844 sq m) of conference facilities, complete with a state of the art moving floor, and a seven storey grade A speculative office building comprising 202,000 sq ft (18,799 sq

m) (net) with three retail units and car parking including electric car charging points. Atria One comprises seven floors and sits above the AFS while Atria Two comprises two floors of offices above the EICC Atrium building (the main entrance at Morrison Street into the AFS). Once completed, the office was to be sold as an investment opportunity to repay borrowing costs, in accordance with the approved funding model. The innovative funding model comprised the use of remaining monies in the Lothian Road Income Trust Fund, a contribution from Scottish Enterprise (SE), proceeds of the investment sale from the completed offices and prudential borrowing supported by the EICC business case.

- 2.5 The final contribution from SE comprised a £10.1m consideration for the sale of Conference House and £5.9m capital loan. The capital loan plus interest was repayable to SE from any profit generated from the sale of the offices development or future EICC operating surpluses.

## Main report

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- 3.1 Construction began in July 2010 and was completed in March 2013, on time and within budget.
- 3.2 Throughout the construction and letting of the offices, the approved governance structure operated via the Project Board and Investment Steering Group. Both were chaired by the Council in recognition of the funding and risk structure.
- 3.3 Sectional completion of Atria One and Two and the AFS was granted on 28 March 2013 with practical completion granted on 25 April to coincide with the opening of the new pedestrian street, Ladyfield, which includes an art wall showing the skyline of Edinburgh and a quote from the renowned Scottish author, Alexander McCall Smith who opened Ladyfield in April 2013. Both Atria One and Two achieved BREEAM ratings of “Excellent” and “Very Good” for the AFS. The AFS held its first conference of the International Investigative Dermatology on 8 May 2013 and received its royal opening of the Lennox Suite, on 15 January 2015, by Her Royal Highness the Princess Royal.
- 3.4 Prior to completion, the office development secured its first pre-let to Brewin Dolphin, a private equity wealth management firm in January 2012, who took approx 47,500 sq ft (4,413 sq m) of space. Since then the building has continued to lease successfully to a variety of blue chip tenants including PwC, UK Green Investment Bank, Alliance Trust plc, AON, The Law Society of Scotland, EICC Ltd, Lothian Pension Fund, with Cafe Klaris (a local business) and The CO-OP taking two of the three retail units. The building is now just under 70% let, and has achieved some of the highest rents per sq ft in Edinburgh.
- 3.5 Atria has been positively received by the commercial market and is seen as one of the most successful grade A speculative office schemes in Edinburgh. It has won various industry awards including the Estates Gazette Property Company of the Year 2013; the Scottish Property Awards 2014 Judges Award of Merit; The

Royal Institution of Chartered Surveyors Award for Commercial Development of the Year 2014; and CoStar Deal of the Year for the letting to PwC.

- 3.6 The sale of the offices was always an integral part of the funding strategy for the project to recoup development and funding costs. When the project was approved in June 2010, it was anticipated that the investment sale would occur a year after completion and would bring in a gross consideration of approximately £83.2m. As the project progressed, it became clear that the timing of the sale was crucial to maximise returns. Although postponement of the sale would incur additional holding and funding costs, these would be more than offset by a higher consideration from a sale at the optimum time. Therefore, in June 2015, the retained investment agents Jones Lang LaSalle and Montagu Evans recommended that, due to exceptionally strong conditions in the investment market, the marketing of Atria for sale should commence in September 2015.
- 3.7 Consequently, in June 2015, the Project Board, in consultation with the Head of Property and Facilities Management and Head of Legal and Risk authorised the commencement of the sale process.
- 3.8 The marketing material was prepared along with a comprehensive package of due diligence material, which was placed in a virtual data room prior to the commencement of marketing.
- 3.9 In September 2015, a full open market campaign was launched covering local, national and international investors. Direct presentations were carried out by Jones Lang LaSalle and Montagu Evans as well as comprehensive and targeted mail shots issued to investors and agents.
- 3.10 Due to the strong interest received a closing date was set for 29 October 2015, when 5 bids were received. This was expected as the significant lot size restricts the range of investors that would bid for the investment. After detailed analysis, parties were asked to submit best and final offers at a second closing date on 3 November 2015. Three bids were received from European and American investors. After further detailed financial analysis, Deka Immobilien Investment GmbH, a global real estate investment company based in Germany, was identified as the highest financial offer. The main terms are as follows:
- Purchaser: Deka Immobilien GmbH;
  - Subjects: Atria office development comprising Atria One and Atria Two plus three retail units as shown outlined red on attached plan;
  - Price: £105.25m (gross), exclusive of VAT; based on full rental of the property
  - Funding: Cash funder; and
  - Fees: Each party to bear own legal and professional fees.
- 3.11 In line with the delegated authority granted to ensure prompt conclusion and commercial confidentiality, and to ensure the transaction could be concluded and money received by 31 March 2016, the Project Board, in consultation with

the Acting Executive Director of Resources, Acting Head of Property and Facilities Management and Head of Legal and Risk, and with the approval of the Convenor of Finance and Resources Committee, gave authority to conclude a contract for sale with Deka on the main terms outlined above.

- 3.12 Although overall project costs are still being finalised, the total development costs (before funding costs) are expected to amount to £79m compared to a budget of £85m, a saving of around £6m. Once funding costs are taken into account, including a repayment of £10.9m to SE, a surplus in the region of £13m is expected to be returned to the Council. This is considered to be a highly successful outcome bearing in mind the gross sale proceeds have also covered the repayment of the construction costs of the AFS of approximately £30m.
- 3.13 In summary, the AFS and Offices project has been completed on time and within budget, and has secured a significant net receipt for the Council. The award winning project is a highly successful example of public sector innovation. Its successful delivery now completes the regeneration of the Exchange district which has become Edinburgh's prime financial district and is home to some leading names in the business and finance sector and endorses the Council's decision to undertake a significant construction project and speculative commercial development to fulfil a key economic development objective.

## Measures of success

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- 4.1 The completion of construction of the AFS and Offices now completes the regeneration of The Exchange Financial District.
- 4.2 The AFS allows EICC to retain and enhance its competitive position in the global conference market and contribute economic impact to the Scottish economy.
- 4.3 The Atria office development provides much needed grade A office accommodation for Edinburgh.

## Financial impact

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- 5.1 The proceeds of sale will be used to repay development costs and funding costs to facilitate the development.
- 5.2 The net proceeds of sale will enhance the City's Strategic Investment Fund and help deliver the Transformation Programme.

## Risk, policy, compliance and governance impact

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- 6.1 There are no risk, policy, compliance or governance impacts as a result of this report.

## Equalities impact

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- 7.1 Generating a substantial capital receipt for the Council's Strategic Development Fund has the potential to enhance a variety of rights depending on where the money is focussed. This could include the rights to health, physical security, education and learning, standard of living and individual family and social life.

7.2 The Council has also enhanced its right to legal security by using a proportion of the capital receipt to reduce its financial borrowing.

## Sustainability impact

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8.1 There are no sustainability issues arising from the recommendations of this report.

## Consultation and engagement

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9.1 N/A

## Background reading/external references

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[City Of Edinburgh Council – 25 October 2007 – Edinburgh International Conference Centre Limited \(EICC\) – Requirement for Additional Function Space - Reports](#)

[City of Edinburgh Council – 13 March 2008 – Edinburgh International Conference Centre Limited \(EICC\) – Requirement for Additional Function Space \(AFS\)](#)

[City of Edinburgh Council – 28 January 2010 - Edinburgh International Conference Centre Limited \(EICC\) – Requirement for Additional Function Space \(AFS\)](#)

[City of Edinburgh Council – 24 June 2010 - Edinburgh International Conference Centre Limited \(EICC\) – Requirement for Additional Function Space \(AFS\)](#)

## Hugh Dunn

Acting Executive Director of Resources

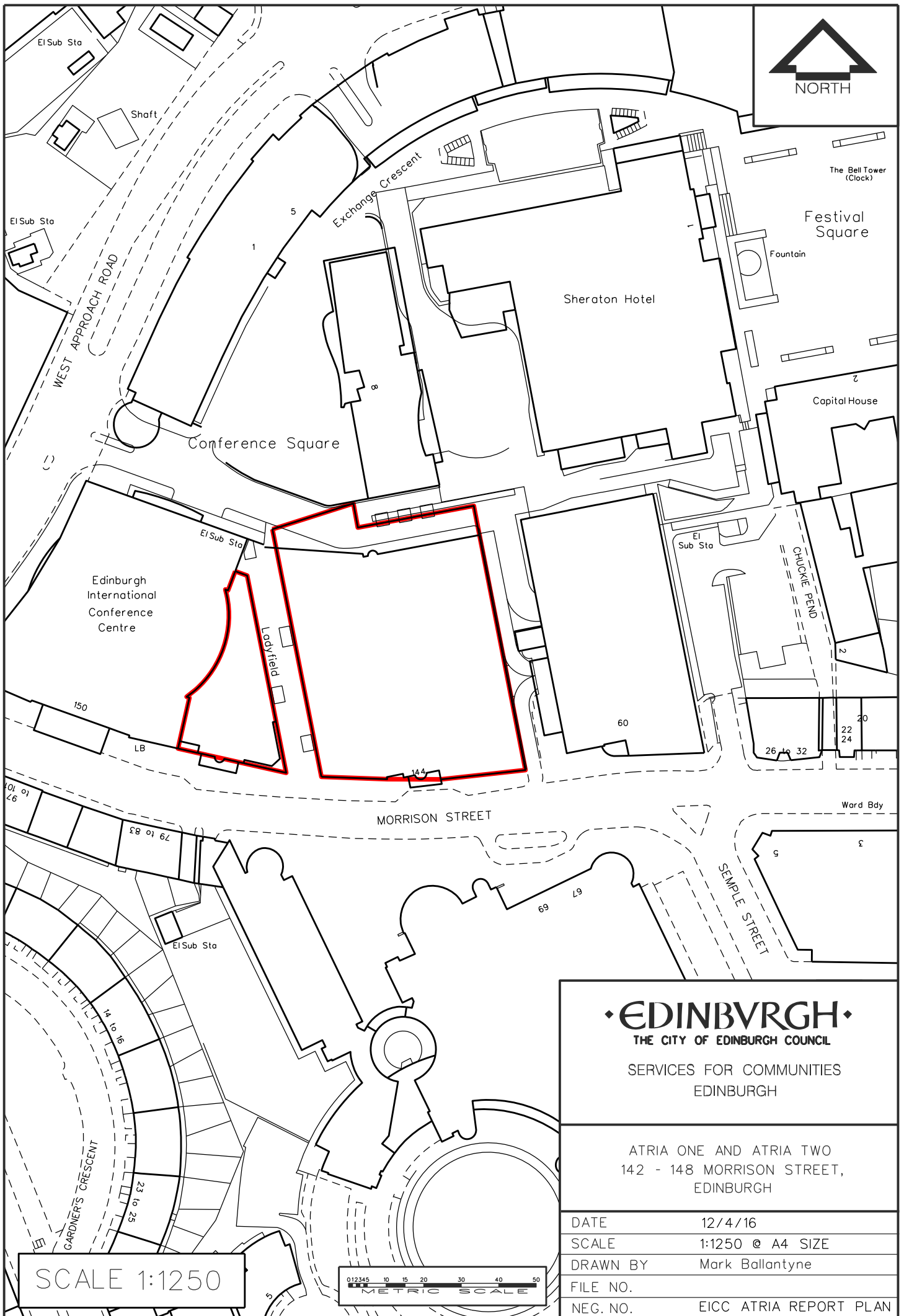
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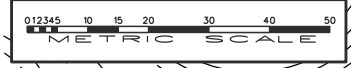
## Links

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<b>Coalition pledges</b>	P17 – Continue efforts to develop the city’s gap sites and encourage regeneration.
<b>Council outcomes</b>	CO7 – Edinburgh draws new investment in development and regeneration. CO8 – Edinburgh’s economy creates and sustains job opportunities.
<b>Single Outcome Agreement</b>	SO1 – Edinburgh’s Economy Delivers increased investment, jobs and opportunities for all.
<b>Appendices</b>	Location plan.



SCALE 1:1250



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 THE CITY OF EDINBURGH COUNCIL  
 SERVICES FOR COMMUNITIES  
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ATRIA ONE AND ATRIA TWO  
 142 - 148 MORRISON STREET,  
 EDINBURGH

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DATE	12/4/16
SCALE	1:1250 @ A4 SIZE
DRAWN BY	Mark Ballantyne
FILE NO.	
NEG. NO.	EICC ATRIA REPORT PLAN