

APPENDIX 1

CANADA WATER

HEADS OF TERMS

Subject to:

- 1. BL board approval**
- 2. Formal approval by the Council**

1. PARTIES

- 1.1 London Borough of Southwark of 160 Tooley Street, London SE1P 5LX (the "Council")
- 1.2 British Land ("BL") A wholly owned subsidiary of British Land Plc. The development obligations of any BL subsidiary will be guaranteed by British Land Plc subject to release on completion of defects and subject to an appropriate liability cap, or such obligations will be subject to alternative guarantees or security as the Council shall approve.

2. SITE

The masterplan area known as Canada Water, Southwark ("Site") shown edged red on the attached plan (Appendix 1). The Site is broadly divided into the following components, each demarcated as such on the attached plan:-

- 2.1 Surrey Quays shopping centre ("SQSC"):-
- 2.1.1 The vast majority of this site is currently held by BL on a lease with an unexpired term of 173 years where the Council is the freeholder.
- 2.1.2 Miscellaneous plots in the vicinity of the Shopping Centre owned by the Council.
- 2.2 Print Works ("PW") :-
- 2.2.1 The vast majority of the site is held by BL on a leasehold basis and the Council owns the freehold interest.
- 2.2.2 Roberts Close freehold owned by BL.
- 2.2.3 Car Park freehold owned by BL.
- 2.2.4 Miscellaneous plots in the vicinity of the Print Works owned by the Council.
- 2.3 Mast Leisure Centre ("MLC"):-
- The freehold interest is owned by BL and includes access rights across the orange land shown on the plan at Appendix 1.
- 2.4 The attached plan at Appendix 2 edged in blue ("The Estate Management Area") identifies land owned by the Council which will be subject to the estate management arrangements in accordance with the estate management agreement.

3. OVERVIEW OF TRANSACTION STRUCTURE

- 3.1 It is intended that BL will surrender its existing long leasehold interests and transfer its freehold interest in some or all of the sites referred to at paragraphs 2.2.2, 2.2.3 and 2.2.4 above to the Council and that the Council will grant two new long leases, broadly of (1) SQSC and (2) PW, although the exact extent will be worked up and agreed between the parties before the agreement is exchanged.

- 3.2 BL is in discussions in relation to the leasing of part of the Site for the creation of a new educational campus. It is an objective of the parties that educational use is brought into the Site through a transaction with a high quality educational establishment such as Kings College London or a similar higher educational organisation. If it is not possible to conclude such a transaction prior to the collapse of the existing leases, the parties will continue to seek to reach agreement with a higher educational establishment. The parties' intention is to create a campus educational environment and not one dominated by student accommodation.
- 3.3 The Council and BL will enter into
- 3.3.1 an overarching agreement regulating the relationship between them in relation to the Shopping Centre and the Print Works prior to the grant of the new headleases. This agreement will serve the same purpose as an agreement for lease(s) and will "fall away" once the two new headleases are completed.
- 3.3.2 BL and the Council will remain bound by the terms of the existing leases until their surrender.
- 3.3.3 an agreement ("**Collaboration Agreement**") in relation to MLC which will deliver a scheme consistent with the master plan and will cover:
- (a) planning - the need for a unified approach across the Site.
- (b) treatment of planning conditions and S106 provisions which jointly relate to MLC and the other components of the Site, how the cost/burden is to be shared, the equalisation of any costs/benefits between other components of the Site and MLC.
- (c) infrastructure costs that will be shared between MLC, SQSC and PW including, the delivery of the works, how the costs are to be apportioned and the recovery of the costs.
- 3.4 Proceeds from the scheme will be generated as a mix of capital receipts and rent as appropriate for the uses. On completion of each plot the proceeds (both capital and rent) will be apportioned between the landowners and the developer (BL is both a landowner and the developer)
- 3.4.1 The initial landowners' share is in accordance with the following percentages.
- (Subject to valuation and agreement on value and cost equalisation)
- SQSC**
- | | |
|-------------|-----|
| BL | 90% |
| The Council | 10% |
- PW**
- | | |
|-------------|-----|
| BL | 50% |
| The Council | 50% |
- 3.5 The Council shall have an option to contribute towards total development cost up to these initial percentages. If the Council do not contribute fully to development cost the percentages will be recalculated on completion of each plot. The landowners share is an appropriate amount of total receipts having regard to the initial valuation.

- 3.6 The developer's share (which the Council will participate in when contributing to development costs) is an appropriate amount of total receipts having regard to the total development cost excluding the land element.

4. **KEY ISSUES TO BE RESOLVED BEFORE EXCHANGE**

The following matters need to be agreed between the parties prior to exchange of the overarching agreement so that they can be included in or appended to the agreement as appropriate:-

- 4.1 Masterplan including phases and plots within the masterplan.
- 4.2 Historic costs (to exclude costs specifically associated with MLC) – are to be agreed and apportioned over the Site excluding MLC and injected into individual plot development accounts.
- 4.3 Build and development costs – agreed approach to demonstrating these costs. Treatment of cost overruns and costs arising from the developer's default. The Council to provide confirmation of its acceptance of the external consultants and the form of appointments and duties of care. The parties will rely on the advice provided by the professional team.
- 4.4 Finance – including agreed principles as to calculation of finance costs and allowable interest and the treatment of the development management account. Interest is to be rolled up on development costs at LIBOR + 3% subject to a minimum rate of 5.75% (compounded quarterly) on all expenditure which is not match funded (requirement for arrangements to vary the interest charge over time so that it remains appropriate).
- 4.5 Strategic financial model demonstrating deliverable and viable Masterplan and the projected returns to the Council (assuming various levels of the Council's financial contribution). The Council will require the model to be developed on the basis of (1) no contribution and (2) various levels of financial contribution, so that it can make an informed decision on investing.
- 4.6 Profit and fees – agreed principles as to calculation. BL to receive a 15% profit on all expenditure which is not match funded (in the relevant leasehold percentages). BL to provide a schedule of Development Management, Project Management and Property Management fees. The Council to receive an annual fee (to be agreed) to cover the time commitment of the Regeneration team (this is separate from the PPA fees).
- 4.7 Business plan and its role within the overarching agreement.
- 4.8 Council contribution of equity – the Council is to have the ability to contribute equity.
- 4.9 Timetables and milestones for delivery of new scheme in phases.
- 4.10 Pro-forma appraisal for plot developments based on a template for Phase 1.
- 4.11 BL to deliver affordable housing in accordance with the Council's planning policy.
- 4.11.1 The Council will have the first option to buy the social rented units. If the Council do not exercise this option BL will have the second option to acquire the units. BL will have the first option to acquire the intermediate rental units.
- 4.11.2 The Council will (on land owned freehold) have the option to acquire additional units which can be made available for social renting to take the scheme to an equivalent 35%. BL will have the first option to acquire the additional intermediate rented units.

- 4.12 The parties agree to explore a range of options for securing and managing the affordable homes for incorporation into the final agreement as an alternative delivery route to the one set out in 4.11.
- 4.13 Community facilities strategy including funding and phasing.
- 4.14 New leisure centre – basis for funding, delivery and treatment of the land interest of the site. Procurement issues to be discussed and agreed.
- 4.15 Site wide infrastructure costs – a strategy including principles and methodology for assessing the Site wide costs and repayment of these for all phases/plots.
- 4.16 Approach to identifying and securing an appropriate higher educational occupier on the Site.
- 4.17 Robust mechanism and formula for objectively settling PW rent review. The rent review will need to be settled before exchange of contracts.
- 4.18 The treatment of any remaining land that needs to be secured for the development to take place to include the use by the Council of its statutory powers.

5. **OVERARCHING AGREEMENT**

The following matters will be covered in the overarching agreement (this list is not exhaustive, but sets out some of the key points):-

- 5.1 The parties' agreed objectives for the scheme being:-
 - 5.1.1 creating a high quality mixed use development including uses such as retail leisure, offices, residential, cultural and public realm.
 - 5.1.2 the delivery of affordable housing in accordance with the Council's planning policy.
 - 5.1.3 the creation of an appropriate higher educational establishment.
 - 5.1.4 the delivery of the new Council leisure facility in phase 1.
 - 5.1.5 to make sure local people have the chance to directly benefit from the development by creating training and employment opportunities during the construction phase and exploring the viability of including business start up space and other support for small businesses as part of the finished scheme. BL's Corporate Policy is to pay the Living Wage (and therefore also the National Living Wage) to all staff directly employed by both British Land and Broadgate Estates, their wholly owned property management subsidiary. BL are already and will continue to explore ways in which they can promote the Living Wage amongst companies that they contract with as well as those companies further down the supply chain.
- 5.2 Agreement for:-
 - 5.2.1 surrender of existing leases.
 - 5.2.2 grant of two new 500 year headleases in the form attached to the overarching agreement.
 - 5.2.3 preconditions to the surrender and grant of the headleases.
- 5.3 Preconditions to the grant of plot subleases by BL.

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- 5.4 On-going cooperation obligations between the parties.
- 5.5 Financial principles and methodologies including:-
- 5.5.1 mechanisms for calculating land value, lease premium or geared rents.
 - 5.5.2 apportionment of land value.
 - 5.5.3 demonstration of overall masterplan viability. It is accepted that it may be necessary to develop some initial phases which generate profits below the target rate of return to establish Canada Water as a destination.
 - 5.5.4 principles for extraction of profit from scheme.
 - 5.5.5 Overage.
 - 5.5.6 viability target/hurdle rates for development plots etc.
 - 5.5.7 BL development return and management costs.
 - 5.5.8 BL provided finance rates. LIBOR + 3% subject to a minimum 5.75%. Provision for a periodic review of the finance rate.
- For the avoidance of doubt a number of the above items will be included in the development agreement annexed to the new headleases.
- 5.6 Delivery of the proposed new leisure centre for the Council including the financial and funding arrangements and ownership.
- 5.7 Provisions on development including:-
- 5.7.1 assurance for the Council on works to be carried out
 - 5.7.2 reporting on the carrying out of works including:-
 - (a) process for tendering of the works.
 - (b) ensuring that the works are carried out in a responsible manner.
 - (c) input into the construction documents and warranties including step in rights.
- 5.8 Planning strategy and obligations– timing for submission of planning application(s) and the process of approvals of applications.
- 5.9 A framework for decision making between the parties on an ongoing basis including:-
- 5.9.1 procedure for obtaining Council approval/sign off.
 - 5.9.2 dispute resolution as follows:-
 - (a) escalation to senior officers/representatives.
 - (b) third party dispute resolution where possible.
 - (c) process to be followed where there is a deadlock.
- 5.10 Provisions for remedying breaches.

- 5.11 Provisions that bind the agreement to each of the headleases such that breach of agreement will constitute a breach of the headleases, and vice versa but in a manner which means that an undertenant does not require sight of the agreement.
- 5.12 A prohibition on assignment or novation separately from the parties' respective legal interests in the Site. Upon any disposal of such legal interest the purchaser must enter into a deed of adherence in relation to the collaboration agreement.
- 5.13 A confidentiality provision and, for so long as this is applicable, an obligation on BL to co-operate at its own cost with any FOI request made of the Council.
- 5.14 Appropriate change of control provisions.
- 5.15 Treatment of copyright and intellectual property including designs and the business plan.

6. ARRANGEMENTS FOR GRANT OF NEW HEADLEASES

- 6.1 There will be two headleases (as identified on the plan at Appendix 1) as follows:-
 - 6.1.1 "SQSC".
 - 6.1.2 "PW".
- 6.2 The agreement will set out the following preconditions:-
 - 6.2.1 Masterplan and demonstration of masterplan viability/deliverability.
 - 6.2.2 Indicative infrastructure cost plan for whole scheme.
 - 6.2.3 Agreed programme for calculation of profit payments on extended schemes – staged distribution.
 - 6.2.4 Agreement as to the rent including the retention and distribution by the parties if income is unaffected by the development of individual plots. BL will fund a rental shortfall account of £3m. This is in relation to both SQSC and PW and will be put in place at the time of the grant of the new headlease of either SQSC or PW. This sum will be available for the Council to draw down once the existing lease or leases are collapsed up to a maximum total rent and rental shortfall equating to £1.3m pa.
 - 6.2.5 Business plan for whole scheme (including targeted revenue / capital split)
 - 6.2.6 Should the Council require additional income this can be drawn down from the development account subject to an interest charge which is to be rolled up at LIBOR + 3% subject to a minimum rate of 5.75% (compounded quarterly). This additional income is to be capped at £1.3m per annum across both SQSC and PW less the passing rents payable under the headleases. This additional income and rolled up interest will be included as a development cost within the relevant phases but will not attract a 15% priority return before the overage calculation.

- 6.2.7 Marketing strategy for the scheme to contain:-
- (a) controls on the marketing of residential units which will balance the need for local marketing and achieving an acceptable rate of sales.
 - (b) marketing strategy for any land disposals.
 - (c) marketing strategy for the higher educational facility.
- 6.2.8 Estate management strategy for whole scheme.
- 6.2.9 A reasonable level of certainty of delivery on the whole of phase 1 including agreements with a reasonable percentage of occupiers (or an agreed percentage of floorspace) and construction contract in place.
- 6.3 The agreement will set out the following SQSC Phase 1 conditions:-
- 6.3.1 Financial model for the phase 1 SQSC identifying departures to the model produced before exchange; the model to also show the cash cascade in terms of the priority of each item.
 - 6.3.2 Delivery of a substantive and material element of phase 1, including the new Council leisure centre.
 - 6.3.3 Receipt of satisfactory planning permission (outline for the Masterplan area and detailed for phase 1).
- 6.4 The agreement will set out the following "PW Phase 1 Conditions":-
- 6.4.1 BL will need to demonstrate that they have sought to reach an agreement with a higher educational establishment for the creation of an educational campus. If it has not been possible to conclude terms by the time of the grant of the new headlease BL will continue to endeavour to reach such an agreement until the Council and BL conclude that it is not possible to do so.
 - 6.4.2 The delivery of the first phase of PW to be a substantive and material element of the proposals for the whole of PW. The minimum phase which will trigger a collapse of the existing headlease is one which produces no less than £500,000 of head rent or combination of rent and decapitalised sales values. Additionally the first phase of PW cannot consist of wholly social rented accommodation.
 - 6.4.3 Receipt of satisfactory planning permission (outline for the Masterplan area and detailed for the first phase of PW)
 - 6.4.4 Certainty of likely delivery on the first phase of PW including a reasonable number of agreements with occupiers (or an agreed percentage) and construction contract in place

7. **ARRANGEMENTS FOR GRANT OF INDIVIDUAL PLOT SUBLEASES**

The agreement will set out the following preconditions for the grant of individual plot subleases and relate to the first development of the plots:-

- 7.1.1 Individual plot appraisal which must achieve an agreed minimum viability i.e. surplus hurdle.
- 7.1.2 Detailed planning permission.

7.1.3 Appropriate confidence that a buyer/investor/tenant can be secured in line with the appraisal assumptions.

7.1.4 Detail of land payments, profit split, fees etc. on individual plot.

8. KEY HEADLEASE TERMS

8.1 **Landlord:** the Council.

8.2 **Tenant:** BL plus guarantor where provided under the agreement.

8.3 **Term:** 500 years from the date of grant of the lease.

8.4 **Premium:** there will be no premium paid for initial grant of the lease but monies payable in accordance with the head lease.

8.5 **Initial rent and capital receipts:** in accordance with the following and subject to agreement and equalisation of base values:-

SQSC

BL: 90%

The Council: 10%

PW

BL: 50%

The council 50%

8.6 Tenant's covenants:-

8.6.1 obligation to pay rent.

8.6.2 restrictions on alienation:-

(a) no assignment of whole without assignee entering into deed of adherence to the "annexed" agreements and alongside an assignment of the other lease.

(b) no underletting of whole.

(c) no underlettings of part unless the tenant obtains either the Council's consent or a certificate from the Council to confirm that the underletting is in accordance with the terms of the agreement.

8.6.3 other links to the agreement, e.g. reporting on works to be carried out and payment of the monies due under the agreement/mechanism for rent increase.

8.7 Provisions for remedying breaches.

8.7.1 No cross default between the two headleases. Arrangements to be agreed to ensure that BL may not landbank and will proceed with development unless it is judged reasonable not to do so (force majeure, adverse market conditions etc).

8.8 BL to have pre-emption rights over the sale of the freehold or grant of overriding leases.

9. **TESCO**

The Council and BL acknowledge that Tesco retain the right to contribute 50% of BL's equity requirement on the Shopping Centre.

Appendices

1. Site plan.
2. Estate Management Area plan identifying the Council owned land which will be subject to the management arrangements.