Northern Line Extension:

Enterprise Zone and borough s106/CIL contribution

1. INTRODUCTION

1.1 This paper summarises the key elements of TfL/GLA's proposal for funding and financing the Northern Line Extension (NLE), including an Enterprise Zone (EZ) and s106 and CIL contributions. Discussions are continuing on some of the details.

1.2 The Government confirmed in the 2012 Autumn Statement that borrowing of up to £1bn from the PWLB would be available to the Mayor, along with a supporting guarantee to be provided under the UK Guarantee Scheme. This is conditional on a binding agreement being reached in 2013 between TfL and the Battersea Power Station (BPS) developer. This will be based on the (non-binding) Heads of Terms signed before the Autumn Statement, which aims to see BPS and the NLE developed in parallel, with both opening around 2020.

1.3 NLE borrowing would be serviced by two revenue streams:

a. **Incremental business rates**[1], retained by the Mayor in a new Enterprise Zone (EZ), with a duration of at least 25 years in line with the Government's current EZ policy. **Section 1** of this paper covers the EZ proposals.

b. **Contributions from local developers,** collected by the two boroughs under the s106 and Community Infrastructure Levy (CIL) regimes. **Section 2** of this paper covers the commitment that each borough is being asked to make to pass a proportion of these revenues to the GLA for the NLE.

1.4 The Funding Statement that forms part of TfL's TWAO application in April will need to demonstrate that a robust funding package for the NLE, with support from key stakeholders, is in place. Proposals are being taken to borough cabinets in March. Thereafter, and at the latest before TfL makes a binding commitment to develop the NLE, each borough's political commitment will need to be developed into a binding agreement to pass developer contributions to the GLA on the agreed basis.

[1] ie growth in business rates above a defined baseline.

2. PROPOSED ENTERPRISE ZONE

EZ boundary

2.1 In order to mitigate risk and maximise income to support repayment of NLE debt within the available time, a wide EZ that includes sites in both Wandsworth and Lambeth has been accepted by HM Treasury. The VNEB EZ as a whole will be relatively small compared to EZs in other parts of the country, and will include sites where a material uplift in business rates is expected to occur following development. In Lambeth, this would bring both the new Sainsbury's store and the Vauxhall Square developments into the EZ. Further due diligence on the precise boundaries, to ensure that identified developments are accurately captured, is being undertaken.

Objectives of the EZ

2.2 The primary purpose of the EZ is to finance the NLE, but in a way that ensures that neither borough is financially disadvantaged as a result of the decision to 'widen' the EZ to sites beyond the core BPS site. Beyond this primary purpose, HMT have now orally agreed that EZ revenues will not be restricted solely to servicing NLE debt. Provided that the GLA is able <u>both</u> to meet its debt service each year <u>and</u> can reasonably forecast that it will have repaid NLE debt within 25 years, any surplus EZ income can be used to fund other economic priorities, as is permitted under EZ legislation.

2.3 The GLA's current policy is that the first priority for any 'surplus' would be the infrastructure requirements of the VNEB area that were identified in the DIFS, which would be determined in consultation with the boroughs. However, any 'surplus' is unlikely to be apparent before around 2030 (by when the quantity and value of commercial development across the EZ, and particularly at BPS, should be clearer). Both the boroughs and the GLA therefore have a strong interest in ensuring that commercial developments occur as expected, and that business rate revenues are maximised.

EZ Duration and Start Date

2.4 The GLA originally proposed that an EZ be maintained for as long as necessary to repay NLE debt. HMT did not agree to this request in full. Instead, it has agreed to a 25 year EZ, with the possibility of an extension of up to 5 years (linked to the guarantee), if required to repay debt.

2.5 The proposed start date for the EZ is 1 April 2016. Based on previous EZs, it is expected that the baseline would be fixed in October 2015, using each borough's forecast of business rates payable on sites within the EZ boundaries at 31 March 2016 (the day before the EZ comes into force). An April 2016 start should ensure that the vast majority of new developments within the EZ are captured as 'uplift' against the baseline. It is understood that the Government intends to bring forward regulations to establish the new EZ over the coming financial year.

2.6 Sensitivity analysis by KPMG currently shows scenarios ranging from 22 years (ie generating a surplus) to over 30 years in duration. Key variables include the quantity and value of new development, and the levels of interest rates and inflation. Should the EZ income over an extended 30 year period not enable full repayment of NLE debt, the GLA Group would be responsible for meeting any further repayment, up to the point at which the UK Guarantee can be exercised.

Disbursement of EZ revenues

2.7 HM Treasury has agreed that each borough, as the billing and collecting authority, will be statutorily required to pass 100% of the business rate uplift to the GLA.

2.8 While a wider EZ helps to spread risk across a number of developments, in the short term, it may adversely impact on the borough's retained income under Local Government Resource Review (LGRR). The GLA proposes to pass back to the relevant borough 30% of the retained uplift against the baseline (ie the level the boroughs would otherwise have received as part of their local share under the LGRR) on all EZ sites other than the BPS site, prior to the first reset (expected in March 2021). Beyond the first reset (or at any subsequent review of local government funding arrangements), we will need to revisit this principle, to ensure that the objectives set out in 2.2 are met.

3. BOROUGH S106/CIL CONTRIBUTION

3.1 Each borough is also being asked to commit an agreed sum to the NLE from income received from developers under the Section 106 and Community Infrastructure Levy (CIL) regimes, on an agreed profile. Actual payments in any given year will be capped at a percentage of the total s106/CIL income actually collected by that date, with unpaid amount rolling forward to future years (with additional indexation applied). This should mean that it should not score as debt. It is much closer to an income sharing arrangement: if no s106/CIL income is received, no payment is required.

3.2 The form of indexation proposed, ie using BCIS index, matches the indexation applied to the boroughs' income stream (s106/CIL). If sites developed and paid s106/CIL ahead of forecast, the boroughs could choose to pay the GLA ahead of the profile specified, in order to avoid indexation costs (which are likely to be higher than any income earned on deposit).

3.3 The key financing risks, such as an increase in interest rates, a reduction or delay in EZ revenues compared with the forecast or a reduction in construction inflation (as measured by BCIS index) without a corresponding fall in borrowing costs, would be borne by the GLA Group.

3.4 The proposed NLE contribution from each borough is summarised below. This represents 96% of the BPS contribution, about 22% of forecast s106/CIL in LBW, and about 17% of forecast s106/CIL in Lambeth.

Proposed NLE contribution

	£m, 2012/13 prices subject to BCIS indexation
Wandsworth (BPS)	200.1m[2]
Wandsworth (other sites)	59
Lambeth	7.3
Total NLE contribution	266.4

Profiling

3.5 Lambeth's contribution is needed over the period of NLE construction, to service debt and to avoid any issues from applying CIL revenues to debt service (which is currently prohibited in the CIL regulations). TfL has proposed that Lambeth's contribution of the £7.3m (plus indexation) be paid in equal instalments over the period to 2019/20. However, there are three developments due to start on site over the coming years (Sainsbury's, Vauxhall Square, Eastbury House) which could enable Lambeth to pay its NLE contribution ahead of this profile, thereby avoiding indexation costs.

3.6 If these developments do not come forward, then Lambeth's liability to contribute to the NLE would be capped at 72.2% of s106/CIL income actually collected by a given date. 72.2% represents the proportion of tariff income that was earmarked for the NLE in the 2010 Development Infrastructure Funding

[2] This represents a £203m NLE contribution, less £2.9m expenditure already incurred on the TWAO

Study (DIFS). If the cap applies in any given period, the NLE contribution due would roll forward to future periods (plus indexation), until the total NLE contribution has been paid to the GLA.

Non-NLE budget and prioritisation of NLE contributions

3.7 The approach set out above results in a total forecast budget for other infrastructure for both boroughs of £245m in 2012/13 prices, before administration costs. This is higher than the tariff-funded cost of other infrastructure of £217m in the DIFS, or £237m (updated figure used in BNPP's 2012 report, which included updated LBW healthcare costs).

3.8 Currently, a 28 year EZ is forecast to be required under the base case, compared with a 25 year base case maximum set by Government. There is therefore no scope at present for a lower borough allocation to the NLE than is proposed.

3.9 TfL does not envisage making a higher call on s106/CIL monies for any TfL-led project than was assumed in the DIFS, even if forecast project costs increase from DIFS assumptions. There may also be reductions compared with DIFS assumptions for certain projects, e.g. capacity works at Vauxhall tube station, which are being funded from TfL's core business plan.

Governance and monitoring

3.10 The set of financial arrangements described above will require active and ongoing monitoring and forecasting:

a. Each borough will need to report its actual s106 / CIL collected from developments across the VNEB Opportunity Area, and regularly update its forecast of future s106/CIL. These will need to be shared with the GLA, to enable the GLA to manage its NLE debt effectively, and the Nine Elms Vauxhall Delivery Partnership, to enable effective planning in other areas.
b. The GLA will need to forecast Enterprise Zone revenues and NLE debt repayment, to understand whether any surplus is likely to be available as described in para [2.3].
c. TfL will need to provide details of past ,programmed and forecast NLE payments.

3.11 It is proposed that this monitoring and reporting be undertaken through an officer level board of the relevant public authorities who will have two members each on the board. The forecast should be updated at least six monthly (or more frequently if significant variations are uncovered) and the proposed impact of the reviews and resulting Non NLE work programme will be reported to the VNEB strategy board whose views will be considered on any resultant re-phasing of the programme.

4. NEXT STEPS

4.1 Confirmation of agreement on these issues is needed before TfL can submit a TWAO application in April. It is understood that borough cabinets will be considering these matters in early March. TfL will be taking the proposed TWAO application, including detailed funding arrangements based on this proposal, to its Board in March. Thereafter, each borough's political commitment will need to be developed into a binding agreement to pass developer contributions to the GLA on the agreed basis.

Transport for London / GLA
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