

Report of Chief Officer Public Private Partnerships and Procurement Unit

Report to Executive Board

Date: 19th June 2013

Subject: Design & Cost Report for the City Region Revolving Investment Fund

Capital Scheme Number: 16500/ RIF

Are specific electoral Wards affected? If relevant, name(s) of Ward(s):	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No
Are there implications for equality and diversity and cohesion and integration?	<input checked="" type="checkbox"/> Yes	<input type="checkbox"/> No
Is the decision eligible for Call-In?	<input checked="" type="checkbox"/> Yes	<input type="checkbox"/> No
Does the report contain confidential or exempt information? If relevant, Access to Information Procedure Rule number: Appendix number:	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No

Summary of main issues

1. The Revolving Investment Fund (RIF) is being established to address identified market failures in the provision of commercial finance to support the acceleration of economic growth and job creation in the Leeds City Region. The long term objective is to grow the Fund, however it will be initially capitalised by authorities. Leeds, Bradford, Kirklees, Wakefield, York, Harrogate and Calderdale have expressed an interest in becoming "Founder Members" in the Fund. The Leeds City Council investment is £6.440m.
2. The Fund will be launched in two phases, a Phase 1 launch and Call for Projects at the end of June 2013 and a Phase 2 launch expected later in the year. The approach will allow the Fund to concentrate on areas of high need, apply lessons learned to the second phase, create an investment track record and allow for further information gathering to inform the Phase 2 Fund development.
3. The Phase 1 launch will target asset based construction and housing projects that require short term loans that are over £1m. The loans will be made on a commercial basis at state aid compliant rates with a maximum target return period of 5 years. The

investments would have a minimum public/private funding ratio of 25/75. Returns from investments made will be reinvested in the Fund (unless otherwise agreed unanimously by the Founder Members in due course).

4. The precise legal structure of the Fund is still being formulated, however in line with the recommendation of the Legal Advisors for the project, the RIF is anticipated to be a Limited Partner (LP) structure, with each authority or “Founder Member” being a Limited Partner and a General Partner (being a special purpose company formed by Leeds City Council) to manage the Fund.
5. An outline Investment and Monitoring Process has been developed incorporating two main decision points. The first decision point is a high level decision, at Member level through a Joint Committee arrangement (most likely a sub-committee of the Leaders Board comprising Members from the Founder Authorities), to identify if the project fits with the Investment Strategy, what economic benefits it is likely to generate and if it is capable of providing a commercial return on investment by the Fund, and whether it is therefore recommended for consideration at the detailed due diligence stage.
6. Supported by appropriate external advisors, LCR officers will undertake detailed due diligence and be responsible for negotiating commercial terms on behalf of the Founder Members. In order to enable the fund to operate on a commercial basis, the final decision as to whether to make an investment will be taken by the Director of Resources of Leeds City Council in consultation with the Chief Financial Officers of each of the Founder Members.
7. Investments will be drawn down from member authorities in proportion to where the economic benefit is identified to accrue. Member authorities will retain funds until either a) investments are approved which benefit their local area; or b) once all funds provided by a single member authority have been drawn down, and a further investment is to be made in that authority’s area, funds would be drawn down proportionately from the other member authorities to fund the investment.
8. Founder Members are required to enter into legal agreements and gain the required authority to invest in the RIF prior to the establishment of the Fund. Each authority is anticipated to formally approve their commitment during June or early July.
9. This report and the recommended arrangements should be considered in conjunction with agenda item 25 “Review of Governance Arrangements in West Yorkshire” (June Executive Board). It should however be acknowledged that these two bodies have separate memberships. See paragraph 4.1.2 for further detail.

Recommendations

10. The Executive Board is requested to:

1. Give authority to invest the £6.440m in the RIF, in accordance with capital scheme number 16500 RIF
2. Authorise the Director of Resources to take any necessary further action to establish a Leeds City Region Revolving Investment Fund including the approval of any necessary agreements (in accordance with the Principles as defined in paragraph 3.1 of this report), and any necessary decision making arrangements in relation to the making of investments by the RIF, to enable Leeds City Council to become a Founder Member of the Fund.
3. Authorise Leeds City Council to act as administrator of the RIF (including, if necessary, the establishment of a “General Partner” for the RIF).

1 Purpose of this report

1.1 This report seeks approval from the City Council's Executive Board to enter into a limited partnership with partner local authorities to establish a Leeds City Region Revolving Investment Fund (RIF), and give authority to invest £6.440m in accordance with capital scheme number 16500RIF, as the Leeds City Council agreed contribution to the setup of the Fund The report covers the following;

- The strategic context for the RIF
- The First Phase Launch
- How the Fund will operate
- The requirements of Founder Member Authorities
- Capital Investment from Leeds City Council

2 Background information

The Strategic Context for the RIF

- 2.1 The Leeds City Region ("LCR") is working to deliver a single Investment Strategy and Investment Plan that sets out its strategic priorities and how it can support the generation of economic growth within LCR. An Investment Framework to support the delivery of the Investment Plan is also being developed which utilises a number of funding sources and supports a more strategic approach to investment across the LCR. It is intended that the Investment Framework will act as 'a single door' where projects can apply for funding and, depending on the nature and terms of the opportunity can be allocated for consideration within the RIF or other funding source within the Investment Framework. Those projects that as both delivering economic growth returns and are commercial in nature can be considered for investment by the RIF.
- 2.2 In July 2012 the City Region agreed its 'City Deal' with government to help boost jobs, increase productivity and create the conditions for economic growth in the City Region. A key component of the City Deal is the creation of a RIF to help facilitate economic growth by supporting commercially viable projects that due to the current difficult conditions in the financial markets, cannot secure appropriate finance to proceed. By investing in commercial development or expansion projects, that would otherwise be stalled because conventional sources of finance are insufficient or unavailable, both direct and indirect jobs can be created, and a catalyst to support the regional economy achieved.
- 2.3 A high level market needs review undertaken by PwC identified a number of areas where there is a range of supporting evidence that suggests future economic growth in the region could be hampered by a lack of access to finance. In the study the key investment sectors which had a stronger evidence base in relation to the lack of 'access to finance' as an issue were Construction (a broad range of investment potential falling within large scale commercial infrastructure), Housing (including private rented) and Low Carbon (mainly renewable energy).

2.4 The long term objective is to grow the fund as envisaged in the City Deal through a mixture of both public and private investment. Initially it is envisaged that the RIF will be capitalised at Phase 1 with seed funding provided by Founder Member Authorities. The table below sets out the capital contribution to be made by each authority that has expressed an interest in becoming a Founder Member of the Fund:

2.5

Authority	£m
Leeds	6.440
Bradford	4.133
Kirklees	3.304
Wakefield	2.625
York	1.632
Harrogate	0.320
Calderdale	1.632
Less Project Development Costs:	(0.450)
Total	19.636

2.6 To implement the RIF a two stage implementation plan has been developed with a Phase 1 launch with initially £10m of the above Local Authority seed funding planned for the end of June 2013. Phase 2 targeted for later in the year, to encompass further sources of public and private investment. This approach will allow the Fund to concentrate on areas of high need, apply lessons learned to the second phase, create an investment track record and allow for further information gathering to inform the Phase 2 development. This report concentrates on the Phase 1 Launch of the fund.

3 Main issues

The Phase 1 Launch

- 3.1 Heads of terms are attached at **Appendix 1** to this report. The principles outlined in the Heads of Terms as to governance, the decision making process and the role of Leeds as administrator of the fund (the “Principles”), are agreed between the parties. The precise legal structure of the Fund (in particular whether a Limited Partnership is the most appropriate structure), is still to be finalised between all the parties, however this will not materially impact on these agreed principles. The Investment Strategy for the RIF is detailed as part of the Heads of Terms document at **Appendix 1** of this report. The Strategy positions the Fund in relation to purpose and approach and sets out the criteria which must be met by any investment by the Fund. The Investment Strategy has been considered by all the participating authorities to ensure it meets their needs.
- 3.2 The Phase 1 launch will seek to promote the fund to projects within the LCR that will grow the economy, in relation to job creation and increased GVA, with Expressions of Interest sought from projects that are seeking investments over £1m.

- 3.3 At this stage it is intended to target asset based construction and housing projects requiring short term or mezzanine based loans. These loans will be provided on a commercial basis lending at state aid compliant rates, with a maximum target return period of 5 years. A leverage ratio of public to private funding of at least 25/75 will be required. For example, a £5m public sector investment will require a further £15m of private monies as a minimum.
- 3.4 Returns generated by investments will be reinvested in the fund to enable it to grow and support economic growth going forward. Provision will be made in the Legal Agreement to accommodate the payment of a dividend if the partner authorities are in unanimous agreement.
- 3.5 It is envisaged that if a Call for Projects is made on 28th June, the likely timeframe for first investments would be late 2013, however, the process will be sufficiently flexible to accommodate projects that are ready to access funding sooner.
- 3.6 The findings of the Phase 1 launch in terms of demand for investment, aligned to further work to understand the needs of the market, will inform the Phase 2 plan. As this will involve private investment it will be necessary to refine processes further including the appointment of an independent fund management arrangement.

How the Fund Will Operate

- 3.7 As noted above the precise legal structure has not been finalised, however this will not materially impact on the Principles agreed in the Heads of Terms and as detailed below. The Heads of Terms reflect the recommendation of the Legal Advisors for the project to structure the RIF as a Limited Partnership (LP), under the Limited Partnership Act 1907, which will provide the formal vehicle to provide loan finance to qualifying projects. The LP structure will comprise each authority or “Founder Member” being a Limited Partner, together with a General Partner, which will be a private limited company and controlled wholly by Leeds City Council, to manage and administer the Fund
- 3.8 Projects will be assessed at the feasibility stage for economic and commercial viability by the LCR. A summary assessment will be presented to an LCR Joint Committee with representation from each Founder Member, with a clear recommendation as to whether the project fits with the Investment Strategy and demonstrates sufficient potential to be able to access the funding.
- 3.9 An interim appraisal process has been developed which provides the structure for the strategic and economic assessment of projects in line with the aims and objectives of the RIF (the “Feasibility Stage”). The assessment will identify the economic impact that the project will have in the short and long term in relation to direct and indirect jobs created and gross value added (GVA), in the region as a whole and at individual authority level. This information will be considered alongside the initial assessment that the project is commercially viable, financially sound and demonstrates that it is deliverable.
- 3.10 If the project is approved for investment in principle then detailed due diligence will be undertaken and commercial terms negotiated. It is envisaged that as the principle of investment in the project will have been approved at a prior stage, and in order to

operate in a more commercial way, the decision to invest will be made by Leeds City Council's Director of Resources, following consultation with the nominated officer representing each Founder Member.

- 3.11 Leeds City Council (in its administration capacity), supported by LCR officers and expert external advisors (legal, financial and technical), will be responsible for undertaking due diligence on behalf of the Founder Members. It is intended that the costs of the due diligence will (to the extent possible) be re-charged to applicants for investment. The objective of the due diligence process is to understand and assess the risks of any investments made and to mitigate these risks and safeguard the lenders interests as far as possible.
- 3.12 Whilst the economic impact can be taken into account at the Feasibility Stage, the terms sought and final investment decision must be taken on an objective commercial basis. If the RIF is not perceived either by potential investors or borrowers to be operating on this basis it could potentially have an adverse impact on the perception and effectiveness of the fund.
- 3.13 As stated in paragraphs 3.8 and 3.9, the Feasibility Stage appraisal process is able to identify for each project the proportionate economic benefit that it is estimated could be generated in each of the geographical areas of the Founder Members. In order, in the first instance, to align the financial investment in the project to the estimated economic return for each Founder Member, investment monies will be drawn down from those Founder Members proportionate to their economic return. Once all the funds provided by a single Member Authority have been drawn down, funds will be drawn down proportionately from the other Member Authorities.

4 Corporate Considerations

4.1 Consultation and Engagement

The Requirements of Founder Member Authorities

- 4.1.1 In order to achieve the target Phase 1 launch of the Fund by the end of June, full approval to utilise this money to make investments will be required. The proposed Founder Members will need to enter into legal agreements prior to establishing the fund to commit the funding when required, and to formalise the governance arrangements around the investment and monitoring process including when decisions can be taken. External legal advisers have been engaged to develop the agreements in accordance with the principles set out in the Heads of Terms attached at **Appendix 1** of this report; however delegated authority will be required to enter into these agreements in advance of the Phase 1 launch.
- 4.1.2 While the success of the Fund will be dependent on ensuring that the process for providing loans (while being diligent) is prompt, efficient and familiar to borrowers and other investors, it is intended that there will be wider LCR involvement at a) the Feasibility Stage (see paragraphs 3.8 and 3.9), and b) in an overview capacity, assessing the effectiveness of the Fund and making recommendations to the Founder Members as to how the Fund should evolve. It is envisaged that such involvement would in the first instance be by way of a specially established group of relevant elected authority representatives, however it is considered that in due

course there would be scope for this role to link in with the proposed Combined Authority (referred to in Agenda Item 25) potentially via a joint committee which would provide the broader regional framework and appropriate linkages to support and facilitate this role.

4.2 Equality and Diversity / Cohesion and Integration

- 4.2.1 A screening document is attached at **appendix 2**, which documents how the impacts on equality, diversity, cohesion and integration have been considered.

4.3 Council policies and City Priorities

- 4.3.1 The Revolving Investment Fund will contribute through collaborative resourcing and investment at LCR level to the Leeds City Vision that the economy will be prosperous and sustainable, and the City Priorities to be Best City for Business and Best City to Live.

4.4 Resources and value for money

- 4.4.1 Capital Funding and Cash Flow.

Funding Approval :	Capital Section Reference Number :-		16500				
Previous total Authority to Spend on this scheme	TOTAL £000's	TO MARCH 2011 £000's	FORECAST				
			2011/12 £000's	2012/13 £000's	2013/14 £000's	2014/15 £000's	2015 on £000's
LAND (1)	0.0						
CONSTRUCTION (3)	0.0						
FURN & EQPT (5)	0.0						
DESIGN FEES (6)	0.0						
OTHER COSTS (7)	0.0						
TOTALS	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Authority to Spend required for this Approval	TOTAL £000's	TO MARCH 2011 £000's	FORECAST				
			2011/12 £000's	2012/13 £000's	2013/14 £000's	2014/15 £000's	2015 on £000's
LAND (1)	0.0						
CONSTRUCTION (3)	0.0						
FURN & EQPT (5)	0.0						
DESIGN FEES (6)	0.0						
OTHER COSTS (7)	6440.0				6440.0		
TOTALS	6440.0	0.0	0.0	0.0	6440.0	0.0	0.0
Total overall Funding (As per latest Capital Programme)	TOTAL £000's	TO MARCH 2011 £000's	FORECAST				
			2011/12 £000's	2012/13 £000's	2013/14 £000's	2014/15 £000's	2015 on £000's
LCC Supported Borrowing	6440.0				6440.0		
Revenue Contribution	0.0						
Capital Receipt	0.0						
Insurance Receipt	0.0						
Lottery	0.0						
Gifts / Bequests / Trusts	0.0						
European Grant	0.0						
Health Authority	0.0						
School Fundraising	0.0						
Private Sector	0.0						
Section 106 / 278	0.0						
Government Grant	0.0						
SCE (C)	0.0						
SCE (R)	0.0						
Departmental USB	0.0						
Corporate USB	0.0						
Any Other Income (Specify)	0.0						
Total Funding	6440.0	0.0	0.0	0.0	6440.0	0.0	0.0
Balance / Shortfall =	0.0	0.0	0.0	0.0	0.0	0.0	0.0

Parent Scheme Number : 16500
Title : Leeds City Region Revolving Investment Fund

4.4.2 Revenue Effects

4.4.3 The borrowing costs for the scheme are included in the 2013/14 approved Revenue Budget.

4.5 Legal Implications, Access to Information and Call In

- 4.5.1 This report is subject to Call In.
- 4.5.2 This Project has accessed legal advice from officers within the City Council's Public Private Partnerships Unit, Corporate Governance and Squire Sanders.
- 4.5.3 The decisions set out at recommendations 6 are Key Decisions and any subsequent decisions that are required to establish a Leeds City Region Revolving Investment Fund will be Administrative Decisions provided that the Project remains within the parameters agreed by Executive Board.
- 4.5.4 The finalisation of the legal arrangements to establish the Fund and incorporate Leeds as a Founder Member and administrator of the RIF will be undertaken after this Executive Board meeting. It is therefore proposed the Director of Resources is given authority to undertake any further action necessary to establish the RIF at Phase 1.

4.6 Risk Management

- 4.6.1 As with any project of this scale, there are a number of issues and risks to be managed in moving towards launch and formal legal agreement. The main risks at this point relate to gaining agreement to the governance arrangements and legal agreements between the Founder Members. Consultation and briefings have been undertaken to ensure Founder Members are comfortable with the commercial implications of the different components which will require approval and signature when required. These are reflected in the Heads of Terms attached at Appendix 1.
- 4.6.2 New and on-going risks will be addressed by risk management procedures.

5 Conclusions

- 5.1 The Revolving Investment Fund (RIF) is being established to address market failures in the provision of commercial finance to support the acceleration of economic growth and job creation in the City Region. The long term objective is to grow the Fund and a two phase approach is being taken incorporating a Phase 1 launch and Call for Projects by the end of June 2013. The initial capitalization will be from Founder Members in the LCR in order to pool resources to take a strategic approach and maximise impact.
- 5.2 The budget envelope for the project is £6.440m (Capital Scheme number 16500 RIF). Subject to appropriate approvals being sought from the partner authorities, the Council will enter into legal arrangements with partner local authorities to be a Founder Member and act as administrator of the RIF.

6 Recommendations

- 6.1 The Executive Board is requested to:

1. Give authority to invest the £6.440m in the RIF, in accordance with capital scheme number 16500 RIF
2. Authorise the Director of Resources to take any necessary further action to establish a Leeds City Region Revolving Investment Fund including the approval of any necessary agreements (in accordance with the Principles as defined in paragraph 3.1 of this report), and any necessary decision making arrangements in relation to the making of investments by the RIF, to enable Leeds City Council to become a Founder Member of the Fund.
3. Authorise Leeds City Council to act as administrator of the RIF (including, if necessary, the establishment of a “General Partner” for the RIF).

7 Background documents¹

7.1 None

Appendices

Appendix 1: Heads of Terms and Investment Strategy

Appendix 2: EIA screening document

¹ The background documents listed in this section are available to download from the Council's website, unless they contain confidential or exempt information. The list of background documents does not include published works.