

Report of the Cabinet Member for Finance, Performance and Customer Services

Leeds City Region – Revolving Investment Fund

Summary

- 1 This report seeks approval from the Cabinet 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 £1.632m, as the City of York Council agreed contribution to the setup of the Fund. It follows on from the report to May Cabinet which agreed in principle the contribution to the LCR RIF, subject to further detail which is included in this report. 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 City of York Council

Background

- 2 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.

- 3 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.

- 4 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).

- 5 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:

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

- 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 July 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.

Main issues

- 7 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.
- 8 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.
- 9 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.
- 10 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.

- 11 It is envisaged that if a Call for Projects is made later in the month, 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.
- 12 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

- 13 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.
- 14 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.
- 15 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.

- 16 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. It is recommended that the nominated officer in York is the Council's s.151 Officer.
- 17 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.
- 18 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.
- 19 As stated in paragraphs 14 and 15, 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. Investment monies will be drawn down from the Founder Members proportionate to their overall investment as funds are released.
- 20 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.

- 21 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 14 and 15), 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.

Council policies and City Priorities

- 22 The Revolving Investment Fund will contribute through collaborative resourcing and investment at LCR level to support Creating Jobs and Growing the Economy.

Implications

Financial Implications

- 23 Financial - The councils contribution to the fund was agreed in principle at Cabinet meeting (7th June) from the Economic Infrastructure Fund. The latest balance of the EIF is shown on the Capital Outturn report elsewhere on the agenda.
- 24 Human Resources - There are no human resources implications arising from this report.
- 25 Equalities - There are no equalities implications arising from this report.

- 26 Legal –Officers from legal services have been working with their colleagues from the other Councils in the City Region and external advisers to develop sound governance arrangements for the partnership which also ensure that no state aid issues will arise. Those arrangements are still being finalised. It is therefore proposed that the Director of Customer and Business Support Services be authorised to take any further action necessary to establish the Fund.
- 27 Crime and disorder - There are no crime and disorder implications arising from this report.
- 28 Information Technology - There are no information technology implications arising from this report.
- 29 Property - There are no property implications arising from this report.
- 30 Other - There are no other implications arising from this report.

Risk Management

- 31 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.

Recommendations

- 32 The Cabinet is requested to:
- Give authority to invest the £1.632m in the RIF, funding from the Economic Infrastructure Fund
 - Cabinet delegates authority to the Director of Customers and Business Support Services to take necessary actions required around the legal arrangements to allow Phase 1 to be launched.

Reason : To support the Council Plan priorities of creating jobs, growing the economy and investing in the city's economic future.

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	Report Approved	√	Date 4 July 2013
Wards Affected: <i>All</i>			
For further information please contact the authors of the report			

Appendices

Appendix 1: Heads of Terms and Investment Strategy

Background Papers

None