

Manufacturing & Materials Research & Development Centre Project Change Request and Revised Business Plan

To: Business Board

Meeting Date: 12 May 2021

Public report: Yes

Appendices 2 and 3 to this report are exempt from publication because they contain information relating to the financial or business affairs of any particular person (including the authority holding that information) under paragraph 3 of Part 1 of Schedule 12A of the Local Government Act. It is considered that the public interest in maintaining the exemption would outweigh the public interest in disclosing the information.

Lead Member: Chair of the Business Board, Austen Adams

From: Director of Business & Skills, John T Hills

Key decision: Key Decision to be made by Mayoral Decision Notice

Forward Plan ref: Key Decision 2021/027

Recommendations: The Business Board is recommended to:

- (a) Recommend that the Mayor approves the project change request at Appendix 3 for the Manufacturing & Materials Research & Development Centre;
- (b) Recommend the Mayor approve the revised Business Plan for the Peterborough R&D Property Company Ltd at Appendix 1;
- (c) Recommend the Mayor delegate authority to the Director of Business and Skills, in consultation with the Lead Member for Economic Growth, the Section 73 and the Monitoring Officer, to finalise and complete the necessary legal documentation for the Peterborough R&D Property Company Limited; and
- (d) Recommend the Mayor approves the allocation of the balance of the £13.773m Getting Building Fund monies to Phase 2 of the

University of Peterborough project and releases the balance of the funding based on the amendment to the Business Plan.

1. Purpose

- 1.1 To seek approval for a change to the project Business Model, to enable the Peterborough R&D Property Company Limited ("the Company") to manage the Manufacturing & Materials Research & Development Centre ("the Centre") itself instead of procuring a commercial operator to do so.
- 1.2 To seek approval for a number of changes to the project Business Plan, to enable the Company to take on this role and the reduced capital contribution to the build from Photocentric Ltd.

2. Background

Manufacturing & Materials Research & Development Centre

- 2.1 At its meeting on 12th January 2021, the Business Board considered a report on the incorporation of the Company and made recommendations to the Combined Authority Board on the delegation of authority to officers to prepare legal documentation and on the approval of the Business Plan for the Company. The recommendations were adopted by the Combined Authority Board at its meeting on 27th January 2021. At that time, it was the intention that a commercial operator for the Centre would be procured by the Company and the Business Board also recommended that consent be given for the Company to enter into a contract with the successful contractor in the procurement.
- 2.2 Subsequently, advice has been received that the proposed Business Model, of having a contractor to operate the Centre (by taking a lease of the premises with right to sub-let to the tenants), would result in the Company being unable to recover VAT on the construction costs which would have reduced the build budget by circa £3m. A solution has been developed that would allow VAT to be reclaimed but will require the Company itself to manage the building. The Company, as previously planned and approved by the Business Board and CA Board, will be a Special Purpose Joint Venture, between the Combined Authority and Photocentric. However, to protect the Combined Authority from the risk of having to inject further share capital into the Company to cover potential losses arising from operation of the Centre, Photocentric have agreed to fund the additional cashflow requirements of the Company and any losses resulting from the Company's operation of the Centre. This revised arrangement will be enshrined within the suite of legal documents describing the shareholder and lease arrangements for the building, between Photocentric and the Combined Authority. These will allow the Director of Skills and Business in conjunction with the Section 73 and the Monitoring Officers, to finalise and complete the necessary legal documentation to secure the commitment from Photocentric to inject further share capital into the company to cover its cashflow needs and potential losses.
- 2.3 The project was first approved by the Business Board in October 2020 and ratified by Mayoral Decision Notice in November 2020. Then in January 2021 a change request was approved by the Combined Authority for the joint venture partner Photocentric to increase their investment for the construction of the Centre from £1.5m to £3m, to enlarge it to 3,283m²

across 3 floors, facilitating a mix of high-quality technical laboratory and office space for incubations and start-ups.

- 2.4 However, to help provision for the need to inject further share capital into the Company, to cover potential operating losses, Photocentric have now requested that they reduce their investment in the building by £800,000 to £2.2m
- 2.5 Hence, this change request also proposes a reduction in the size of the Centre back to the original plans approved by Business Board in October 2020 and ratified by Mayoral Decision Notice in November 2020. The building will now be 2,954m² across 3 floors, in line with the original Getting Building Fund application approved by Government, and whilst this reduces the overall lettable space to 1,657m², the original total job outputs agreed as part of the award of Getting Building Funding remain unchanged.
- 2.6 While the number of jobs is in line with the original application, this change request also outlines a 3-month delay in the build programme as the revised building scope must be resubmitted for planning permission in June reflecting the revised design and reduced size of the building. This delay gives a revised expected completion and opening date in December 2022.
- 2.7 The revised Business Plan, which includes this revised proposal for the delivery of the Centre building, forms Appendix 1 to this report and the Business Board is invited to recommend that the Mayor, through a Mayoral Decision Notice, approves the release of the remaining funding to the Company, to enable contracts to be placed with MACE, the project consultants by the 3rd June 2021, to commence the redesign and resubmission of the planning application for the smaller building, in order to meet the revised December 2022 completion date. Therefore, to expedite the process it is intended to seek approval through Mayoral Decision Notice. This notice will follow the Business Board approval on 12th May.

Getting Building Fund Implications

- 2.8 The Combined Authority element of the budget for the project is made up of £14.6m Getting Building Fund (GBF). The award of the funding followed a formal joint application process by the Combined Authority and its partner Photocentric, which was approved by Mayoral Decision Notice on 5 November 2020. Of this £14.6m, £827k was ring-fenced for the associated car park and £300k was top sliced to cover staff, leaving £13.47m for the build itself.
- 2.9 Given the proposed revisions to the Business Plan, and the underpinning Economic Appraisal, it was necessary to confirm that the revised proposals would not impact upon the outcomes and conditions agreed as part of the award of the GBF from Government. Discussions have therefore taken place with the Cities and Local Growth Unit (CLGU) and a Project Change Request has been approved and confirmed in writing on 27th April 2021, The change request approval confirms that the GBF spend conditions set out in the Grant Offer Letter from the MHCLG Secretary of State, remain unaffected.
- 2.10 An independent re-evaluation of the GBF application has been carried out by the same independent evaluators that conducted the original application's appraisal in October 2020 . Their independent report on this revised business plan and revised project investment is attached as not for publication Appendix 2.

Commercial Appraisal, State Aid and VAT

- 2.11 The original independent evaluator's report of October 2020, set out a number of reports which were required to be produced before the project was confirmed for funding, which the funding decision was therefore made subject to. These have now been repeated for the new Business Plan and are provided in Appendix 2. Of particular importance were the requirements to validate that the Commercial Model (Business Plan) for the project, provide confirmation that state aid regulations had been met, and that VAT could be recovered.
- The Business Plan for the revised project scope has been completed.
 - The commercial model underpinning the plan has been validated by Carter Jonas as viable and comparable to market conditions.
 - State aid advice has been received from Pinsent Mason and provides a positive view on compliance of the new business plan and commercial model.
 - Deloitte have produced new VAT advice which confirms that the Company will be able to reclaim VAT on its construction costs and the Company is now applying to be registered for VAT.

2.12 Summary of material changes to the project

The two key changes to the business plan are:

- I. The move from procurement of a commercial operator for the Centre, to the Company operating the Centre and associated reconfiguration of commercial and business plan.
 - II. Reduction in capital investment by Photocentric from £3m to £2.2m.
- 2.13 The business model is now based on the Company taking on the operation of the Centre itself once complete. Direct operation allows the company to reclaim VAT on expenditure in relation to the build cost. The Company takes on the operation of the Centre itself, collecting rents direct from the tenants and providing services in return. Photocentric will agree to underpin the operating risk of the Centre and will provide further capital investment as may be required in order to ensure that the Company remains able to pay its debts as and when they fall due. As a result, Photocentric will be provided in the Shareholders Agreement with a veto at Board level in terms of matters relating to the operation of the Centre by the Company so that it is able to retain a measure of control over the costs which it will be underwriting. As a result of its agreeing to underpin the Company's cashflow requirements, Photocentric will reconfigure its investment and reduce its initial capital contribution of £3m by £800k to £2.2m.
- 2.14 The removal of £800k from the construction budget results in a reduction of the 14% in Gross Internal Area (GIA) and a Net lettable area of 17%. The Combined Authority has worked closely with an independent consultant (Carter Jonas) to review and revise the commercial model, which is now included within the revised business plan at Appendix 1, and they have confirmed that they consider the model to be financially viable.

Significant Implications

3. Financial Implications

- 3.1 The allocation of shares in the Company will be proportional to the financial investment made by each shareholder in the creation of the Phase 2 Research Building. Photocentric's share allocation of 13.7% of the shares in the Company will be subject to the change request being approved.
- 3.2 As the investment is made by acquiring shares in a limited liability company, and the total value of the shares that the Combined Authority is purchasing is not changing, the total financial liability to the Combined Authority is unchanged by this request – capped at the value of the Combined Authority's shareholding (£13.8m). The funding for this is entirely from the Getting Building Fund, which is ringfenced for this project and could not be spent elsewhere without approval from Government if the project were not to proceed.
- 3.3 While the Combined Authority will own a greater percentage of the Company than under the previous plan, the value of the building will be lowered by the scope change so the overall value of the building attributed to the Combined Authority is likely to be similar.
- 3.4 As Photocentric are underwriting the operating costs of the Centre via its commitment to purchase additional shares in the Company, and the Company is likely to run a cash deficit in its early years, the Combined Authority's ownership of the Company is likely to be diluted to some extent. This will result in the Combined Authority being entitled to a smaller share of the Company's operating profits, or sale revenues. However in return, Photocentric are de-risking the early years of operation of the Company. The amount of additional investment by Photocentric is expected to be in the order of £100k's so is not expected to create a change in majority control of the Company (which would need a further c. £11m investment from Photocentric).

4. Legal Implications

- 4.1 The revisions to the Business Plan will be taken into account in the construction of the Shareholder Agreement between the Combined Authority and Photocentric Limited, the Articles of Association of the Company and the Agreement for Lease and Lease of the premises between the Company and Photocentric Limited.

5. Other Significant Implications

- 5.1 None.

6. Appendices

- 6.1 Appendix 1 – Revised Business Plan for the Peterborough R&D Property Company Limited

- 6.2 Appendix 2 (Exempt) – Independent Appraisal Report on the Revised Project and Business Plan
- 6.3 Appendix 3 (Exempt) – Project Change Request for the Manufacturing & Materials Research & Development Centre

7. Background Papers

- 7.1 'University of Peterborough: Incorporation of PropCo2' (Agenda Item 2.4, Business Board Meeting held on 12th January 2021)
<https://cambridgeshirepeterboroughcagov.cmis.uk.com/Meetings/tabid/70/ctl/ViewMeetingPublic/mid/397/Meeting/2001/Committee/69/Default.aspx>
- 7.2 Minutes of the Business Board meeting held on 9th July 2020
<https://cambridgeshirepeterboroughcagov.cmis.uk.com/Document.ashx?czJKcaeAi5tUFL1DTL2UE4zNRBcoShgo=C3fN6hk%2f1pGVfRRTedlg3soLtreUx8kX3zGbsHN0QOg0qVdtttdGjkq%3d%3d&rUzwRPf%2bZ3zd4E7lkn8Lyw%3d%3d=pwRE6AGJFLDNih225F5QMaQW CtPHwdhUfCZ%2fLUQzgA2uL5jNRG4jdQ%3d%3d&mCTIbCubSFfXsDGW9IXnlq%3d%3d=hFflUdN3100%3d&kCx1AnS9%2fpWZQ40DXFvdEw%3d%3d=hFflUdN3100%3d&uJovDxwdjMPoYv%2bAJvYtyA%3d%3d=ctNJFf55vVA%3d&FgPIIEJYlotS%2bYGoBi5olA%3d%3d=NHdURQburHA%3d&d9Qjj0ag1Pd993jsyOJqFvmyB7X0CSQK=ctNJFf55vVA%3d&WGe wmoAfeNR9xqBux0r1Q8Za60lavYmz=ctNJFf55vVA%3d&WGewmoAfeNQ16B2MHu CpMRKZMwaG1PaO=ctNJFf55vVA%3d>
- 7.3 Getting Building Fund Project Proposal – October 2020 (Agenda Item 2.1, Business Board meeting held on 19th October 2020)
<https://cambridgeshirepeterboroughcagov.cmis.uk.com/Meetings/tabid/70/ctl/ViewMeetingPublic/mid/397/Meeting/2011/Committee/69/Default.aspx>
- 7.4 Mayoral Decision Notice (5th November 2020)
<https://mk0cpcamainsitehdbtm.kinstacdn.com/wp-content/uploads/documents/governance/transparency/mayoral-decision-notice/MDN28-2020-Award-getting-building-funding-GBF-to-Uni-of-Pb.pdf>