Council Cabinet
12 September 2023

ITEM 10

Derby City Council

Report sponsor: Cllr Nadine Peatfield (Cabinet Member City Centre, Regeneration, Culture and Tourism)
Report author: Catherine Williams (Head of Regeneration and Economic Growth)

Additional Capital Loan Request

Purpose

1.1 Great Northern Classics (GNC) will be a new purpose-built facility at a former Rolls Royce site on Osmaston Road, Derby. It will aim to facilitate the preservation and development of crucial skills for the classic vehicle industry.

1.2 In order to enable the redevelopment of the site, GNC have previously approached the Council to support the creation of this facility by granting a capital loan facility to help bridge the gap in funding required to redevelop the site. The loan amount approved was £1.25m repayable in full by the end of year 6, with a part amortisation and part bullet repayment profile.

1.3 GNC have now approached the Council for an additional capital loan of £0.250m in order that the site development can be completed, due to a change in previously assumed private funding sources. GNC's original loan ask of the Council was £1.5m which was not funded in full as £0.250m was for non-specified contingency purposes. This additional ask would bring us back into line with what was originally requested.

Recommendation(s)

2.1 To approve a further secured loan facility up to a value of £0.250m at a commercial rate of interest to the applicant on the basis detailed in para 7.1 (taking the total amount loaned to £1.5m).

2.2 Subject to 2.1 above, to approve the addition of £0.250m to the Other Regeneration Loan capital budget on the Council's 2023/24 capital programme for the capital loan advance, financed by a capital budget transfer from the Ascend capital budget on the Regeneration Capital Programme, and to amend the Capital Programme accordingly.

Reason(s)

3.1 To comply with Financial Procedure Rules.

3.2 To support other economic growth initiatives aimed at creating jobs, repurposing sites/buildings that are no longer in use, and generating foot flow and spend opportunities where appropriate.

3.3 Ability to support the council's ambition for 'The Derby Promise' for example through school visits, work experience, learning from local experts and apprenticeship opportunities.

Supporting information

4.1 **Company Background**

Derby City Council has been approached previously by the Directors of the company, for a loan of £1.25m to support the establishment of a new purpose-built facility, which was approved.

This is a business that aims to facilitate the preservation and development of crucial skills for their industry, by addressing the skills shortage in their sector. They will bring together multi-skilled artisans, trainees and traders into one venue and will serve as a centre of excellence. They have now approached the Council for additional funding support.

The original loan facility was approved by an Urgent Leader Council Cabinet Member meeting on 24 March 2022, subject to satisfactory due diligence and agreement of final terms, with a subsequent delegated approval in March 2022 which approved the final terms and to make the loan advance up to £1.25m. This was granted to help bridge the gap in funding required to redevelop the site.

The Council are now asked to consider a further loan of £0.250m which will enable them to complete the fit-out work and allow the building to open for business as close as possible to the original programme date of August 2023. This need has arisen due to a shortfall in a planned private investment raise, where the current climate sees investors wanting to see tangible completion of the facility, and/or contracted income streams secured prior to committing. This barrier to private investment was not anticipated at the time the original loan advance was approved. Work carried out on site to date is within acceptable parameters in terms of being on time and on budget.

As this is a start-up business, traditional high street funding is not an option for GNC. Banks will generally not support these businesses due to the inherent risks associated with start-ups, such as the unknown accuracy of the financial forecasts and the lack of a trading track record etc.

4.2 **Site**

As previously reported, the site (on Osmaston Road, Derby) will have a total lettable area of c. 56,000 sq ft. This is a mix of retail, workshop and office space, with the expectation that an occupation level of 85% will be seen by the end of year 2. The nature of the industry is such that most companies have less than 10 employees with a bias towards sole traders and small companies made up of 2 or 3 employees. The site is designed such that unit sizes can be flexed from as small as 400 sq ft up to 5,000 sq ft or more, and is highly configurable based on demand and growth. Typical units are anticipated to be c 1,500 sq ft, housing around 32 companies in total.

The site has been independently valued prior to works commencing at £2.25m (as at January 2021). Once the scheduled works have been carried out at the site, the value is expected to rise to somewhere in the region of £3-£3.5m.

We had a Council addressed valuation undertaken by Avison Young ahead of the original lend. Day 1 LTV re the original £1.25m loan was 55%, which will rise to 66% when adding in the potential extra £250k. Versus GDV this will be 46% should the additional advance be agreed. Given the headroom in the property values, the relatively short timeframe lapsed, and the fact that the building work undertaken since the project commenced will only have enhanced the day 1 value then not proposing a re-valuation at this time.

Without the additional funding proposed, the site rebuilding work would not be completed, and the opening would be delayed indefinitely. The delayed income streams would jeopardise the timely commencement of repayments to the existing element of the loan.

4.3 **New businesses / jobs into the City**

It is predicted that around 12 companies will relocate. These will be local (<20 miles) and it is expected that at least half will come from outside the city (Nottingham suburbs, Derbyshire villages etc).

126 new jobs are expected to be created by year 6, with the expectation that circa 27 will be existing jobs just relocating. These numbers relate to those physically employed on the site and do not take into account any potential local supply chain benefits.

The overall position/expected outcomes are the same as they were in the original cabinet report.

4.4 **GVA**

Whilst this has not been assessed by external consultants, the anticipated GVA output is c£4m pa. This figure is based on the jobs on site and could potentially be higher when including visitors to the site and related spend in the locality. It is anticipated that the site will become a tourist attraction once completed, with a café and viewing area incorporated into the development.

4.5 **Due Diligence**

External Due Diligence (DD) was undertaken prior to the original loan being sanctioned, and various points were raised by the DD provider relating to the start - up/speculative nature of the business and being unable to take a firm view on the likelihood of forecasted trading income being achieved given the lack of comparable business models.

These were put to GNC to which they responded accordingly, and ultimately the Council was satisfied with the position.

It is not proposed to undertake additional due diligence at this time, given the above risk profile remains as assessed at the outset and the appropriate loan margin will be applied as before. There remains no trading business to assess, and this was the case at the time the original report was done. This remains a start-up business with the associated risks, and this was accepted at the time that the original £1.250m loan was approved. The strength of the security position is and remains a major positive, with the value only having been enhanced by the work carried out on the building to date.

4.6 **Further considerations**

This is a very bespoke and unproven business proposition, with very few comparable operations either nationally or in Europe. The job creation, ambitious proposals for the development of the site, and the potential to generate tourist foot flow into the City make this additional ask worthy of our consideration. The scheme also has heritage and engineering at its core, which are both things that the City is keen to promote.

It is also worth noting in the context of the wider Osmaston Regeneration programme that the Council has supported over a number of years e.g. Marble Hall, Keepmoat's development on Main Works site, relocation of Castleward businesses to site adjacent to GNC etc.

In terms of security, we hold a first legal charge over the Osmaston Road site which provides a very good level of cover. Based on the original site value of £2.25m and a fully drawn loan of £1.5m, then the Loan To Value (LTV) will be circa 67%. Upon completion of the works, and using the lower £3m figure as advised by the valuer, LTV will fall to 50%. In summary, the risk of loss to the Council is very low.

The total project costs are estimated to be c.£2.5m of which the Council has contributed £1.25m to date with an additional ask of £0.250m meaning GNC have directly contributed c.£1m to the project via shareholder/equity investment.

The further loan advance, if approved, would be on commercial lending terms, ensuring that no Subsidy Control considerations are required. The Council will also charge an appropriate arrangement fee payable on drawdown.

Public/stakeholder engagement

5.1 The Council have had a series of constructive dialogue sessions with the Directors of the business in the development of this report.

Other options

6.1 Do nothing and risk the building not being completed, and therefore unable to generate any income from trading to repay the existing loan. Record the loss of prospective jobs and GVA to the City as referred to in the report.

Financial and value for money issues

7.1 The capital loan request is for an additional £0.250m and the proposed loan terms are as follows:

- New loan term to align with existing loan i.e. 6 years from date of initial drawdown of the existing loan (therefore full repayment due in February 2029).
- Repayments to be on an interest only basis until January 2024, followed by repayment of interest and principal from February 2024 to February 2029 with a final bullet payment of the principal at the end of year 6 (February 2029).
- A fixed interest rate to be applied to the loan on a daily basis, set on commercial terms.
- An arrangement fee to be applied to the loan at drawdown, in line with usual commercial lending terms.
- No 'Investor exit' to be allowed at year 5, unless the Council's total £1.5m loan has been repaid in full, to provide further assurance for loan repayments (as per the original agreement).
- For loan security purposes the legal charge over the site will be increased to £1.5m and a debenture will remain in place. Any legal costs associated with the new loan to be met by GNC.

7.2 Cabinet approval is also sought to add the £0.250m to the Other Regeneration Loan capital budget on the Council's 2023/24 capital programme for the capital loan advance, financed by a transfer of £0.250m capital budget from the Ascend Capital budget on the Regeneration Capital Programme. The capital programme will then be updated accordingly.

7.3 In line with proper accounting practices, capital loan repayments are treated as capital receipts. The Ascend capital budget was set up to provide capital loans on a recyclable basis as loans were repaid, with the capital receipts re-invested in Ascend capital and the interest credited to the Ascend revenue budget to support delivery of the programme. It is proposed that this treatment will apply to this £0.250m advance.

Legal implications

8.1 The loan advance will be made under the general power of competence (GPC) in the Localism Act 2011, sections 1 to 8 but is also permitted under the power to invest granted by section 12 of the Local Government Act 2003. The statutory guidance on local government investments will apply to the loan.

8.2 At this stage there are not considered to be any subsidy control implications associated with the proposed loan arrangements, as they will be subject to a commercial rate of interest.

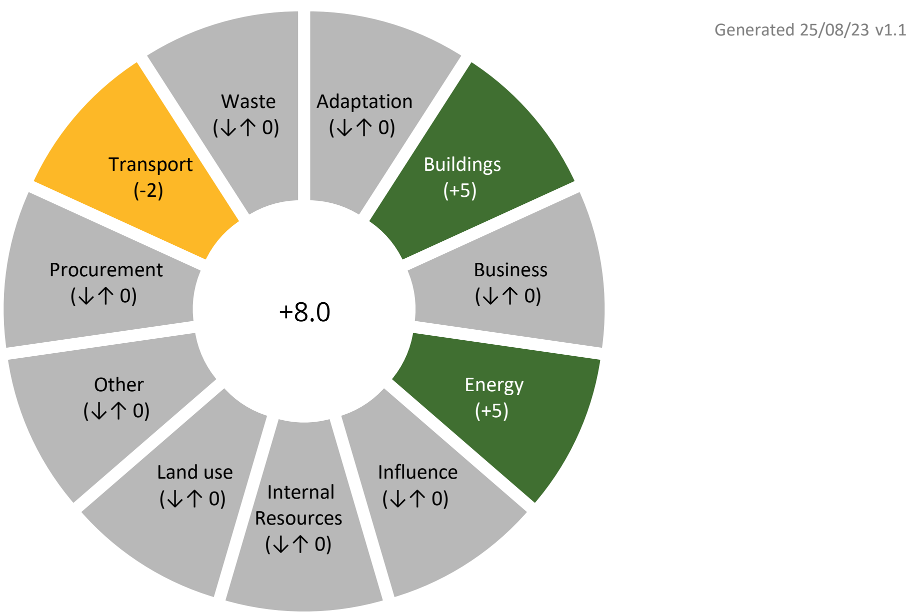
8.3 Currently our initial charge is not registered against the site and we are not able to confirm that there are no other charges against the land. If there are other charges, consent will need to be obtained from these other charge holders prior to granting the further advance, in order to comply with anti-tacking provisions of the Land Registration Act 2003.

8.4 The loan agreement and associated documentation will be drafted by Legal Services or external legal advisers appointed by the Council for this matter.

Climate implications

9.1 The City of Derby has declared its ambition to become the UK's centre of excellence for future fuel technologies. The University of Derby (UoD) will work with existing experts to revolutionise low-carbon energy to power buildings and transport. GNC will tap into this with a project at UoD researching green options for classic vehicles, benchmarking the green footprint of all known vehicle propulsion technologies, and considering the impacts of manufacture, re-engineering, fuel supply and emissions. GNC will look to combine the University's research and expertise in future fuels with the carbon-from-production free benefit of classic cars. This crucial collaboration will pioneer carbon-neutral classic motoring, with the aim of being at the forefront of sustainable classic motoring.

9.2 By co-locating so many specialists, substantial emission gains are automatic. The building is intrinsically more energy efficient than the small dispersed locations their industry currently occupies.



Other significant implications

10.1 The key risks and mitigations are outlined below;

Risk description	Effect	Mitigation
Loan default	Advance not repaid leading to loss of future capital receipts, to replace funding used for initial advance, and interest	Future interest receipts have not been included in the MTFP. Loan security as outlined at paragraph 7.1
Legal charge – Land Registry have not registered transfer of site ownership.	If the site transfer is not affected at Land Registry than our legal charge isn't valid or registered.	Solicitors dealing have confirmed paperwork has been lodged and issue is down to Land Registry backlogs. Expectation is this will be resolved by end of August 2023 and will confirm this ahead of any additional drawdown.

This report has been approved by the following people:

Role	Name	Date of sign-off
Legal	Simon Brown	19/07/2023
Finance	Amanda Fletcher	24/08/2023
Service Director(s)		
Report sponsor	Cllr Nadine Peatfield	24/08/2023
Other(s)	Catherine Williams (HoS)	24/08/2023

Background papers:
List of appendices: