

Cheshire and Warrington Local Enterprise Partnership

LEP Board Decision Paper

Subject:	Enterprise Zone Investment – Blocks 22-24, Alderley Park
Prepared by:	John Adlen
Date:	

1. Executive summary

Alderley Park Limited (APL) has applied for a total of £4m investment in respect of two projects to refurbish Block 22 and the basement of Blocks 23/24 at Alderley Park that will provide a total of 9,011 sqm (c.97,000 sq ft) of refurbished laboratory space. Both of these projects include a contribution towards the development of a new 2,247 space multi-storey car park (MSCP) on the site. The two projects could generate c.£401,500 per annum in retained business rates, generating up to £8.2m in retained business rates over the remaining lifetime of the EZ. On this basis the investment would pay back in 9.9 years. The applicant is seeking grant funding for the two projects on the basis of a gap in the overall financial viability of the schemes, which is exacerbated by abnormal infrastructure costs relating to the MSCP. Whilst these are two separate projects, they are being presented in a single business case for EZ investment due to MSCP element which is common to both projects.

At its September 2019 meeting, the EZ Board instructed the Growth Director to seek further clarifications regarding the MSCP and the financial split between the two projects. The EZ Board subsequently approved the two projects via correspondence subject to receipt of a satisfactory State Aid opinion and the LEP having the necessary funds available via the EZ Borrowing Facility.

The Performance & Investment Committee ratified the EZ Board's decision at its February meeting, subject to the receipt of the economic outputs associated with the project, which have been provided.

The applicant has provided a State Aid opinion, which the LEP's legal advisers (DWF) have stated is satisfactory.

2. Recommendations/actions/decisions required

it is recommended that the LEP Board ratifies the decision of the Enterprise Zone Board and the Performance & Investment Committee to approve the investment in the Block 22 and Blocks 23 & 24 projects at Alderley Park and delegates authority to the Chair of the Enterprise Zone Board to sign the legal agreement with the applicant.

3. Background

Bruntwood bought Alderley Park from Astra Zeneca in 2014 following Astra Zeneca's decision to relocate their R&D headquarters to Cambridge. Astra Zeneca are vacating the site much slower than originally expected and are still occupying a significant proportion of high quality floorspace. High levels of demand, compounded by limited space available, means that APL have been forced to bring forward more complex redevelopment schemes. A lot of the site that has been handed to back to Bruntwood is either physically inaccessible directly from public realm areas or is in a currently un-lettable state due to either the condition or current use of the space, which in turn has forced Bruntwood to bring Blocks 22 and Blocks 23-24 earlier than expected.

4. Scheme proposal

Alderley Park Limited (APL) has applied for a total of £4m investment in respect of two projects to refurbish Block 22 and the basement of Blocks 23/24 at Alderley Park that will provide a total of 9,011 sqm (c.97,000 sq ft) of refurbished laboratory space. Both of these projects include a contribution towards the development of a new 2,247 space multi-storey car park (MSCP) on the site.

The two projects to redevelop Block 22 and Blocks 23 & 24, will see the refurbishment of an ex-in-vivo space to modern laboratory facilities with the capacity to be either chemistry or biology. The initial scope of the project will see a comprehensive strip out of what is currently heavily cellurised buildings. Once this is complete, the intention is to fit out Block 22 to an enhanced shell and core to enable future customers to shape their own labs as they see appropriate. Blocks 23 & 24 would be completed to fully formed labs on a speculative basis.

The two projects will provide a mix of small, medium (2,000-5,000 sq ft units) in Blocks 23/24 and larger (10,000 sq ft) biology and chemistry labs and associated write up space in Block 22. Enquiries at Alderley Park range from 100 to 60,000 sq ft and around 40% could be accommodated within the space proposed within these two projects, supporting demand for the projects and the applicant's confidence that the space will let quickly.

The delivery of these projects is contingent of the delivery of a new Multi Storey Car Park (MSCP). The relocation of Royal London onto Alderley Park has meant a significant reduction in the number of available car parking spaces on site. The new multi storey car park will deliver 2,247 spaces. Without the car park, it is highly unlikely that the proposed schemes could be delivered successfully. The MSCP is required to facilitate anticipated employee growth at Alderley Park over the next three years. There are currently 2,500 spaces catering for 2,000 staff, but 6,000 employees are anticipated over the next 3-years. Without the new 2,247 space MSCP, the ability to attract and retain businesses and staff at Alderley Park, and continue its successful delivery of new space is severely constrained.

Completing these separate projects would significantly assist in delivery the objectives for the site, which primarily include assisting in the target of 75,000 sq ft of science lettings per annum. Block 22 will specifically deliver labs & write up space of c. 11,000 sq ft, whilst 23 & 24 will deliver small to medium biology labs from 2,000 sq ft to 5,000 sq ft.

5. Timescales

Construction of the two schemes and the MSCP will commence in 2020 and are due to complete in 2022.

6. Financial summary

Project Item	Block 22	Blocks 23-24	Total
Costs			
Construction Costs	9,254,798	7,140,223	16,395,021
MSCP Costs	1,200,000	900,000	2,100,000
Developer's Profit	1,529,698	1,012,387	2,542,085
Total Costs	11,984,496	9,052,610	21,037,106
Revenue			
Net Development Value	10,197,990	6,749,249	16,947,239
Surplus/Gap			
Gap	-1,786,507	-2,303,362	-4,089,869

The financial summary of the projects set out above shows a viability gap across the two projects of £4m. The initial financial appraisal of the schemes showed a 'gap' £5.97m, but this was reduced through negotiation with the applicant in order to meet the LEP's maximum 10-year payback period for EZ investments. The 'gap' is based on APL's requirement to meet its minimum internal rate of return of 15% (although this is now reduced due to the negotiation with the LEP). Cushman & Wakefield are satisfied with the cost and value assumptions provided by APL, although they note that further design work is required, which may push costs up. The LEP will cap its investment at £4m with any cost overruns being carried by APL.

The table below shows the estimated retained business rates from the two projects and the MSCP by Bruntwood and Cushman & Wakefield, which vary significantly. This was due to an overestimation on the uplifted rateable for Blocks 22-24, the inclusion of ineligible schemes such as Royal London, but also a significant variation in the estimation of retained business rates from the MSCP, with comparable MSCPs ranging from £135 per space to £600 per space. In addition, Cushman & Wakefield argued that only the car parking spaces directly attributed to Blocks 22-24 should be included in the estimation of retained business rates. Following negotiations between the LEP and Bruntwood and discussions with Cushman & Wakefield a revised estimation of retained business rates was agreed, which is shown in the final column.

Project	Bruntwood Estimate of Annual Retained Business Rates (£)	Cushman & Wakefield Annual Estimate of Retained Business Rates (£)	Agreed Estimate of Annual Retained Business Rates (£)
Block 22	270,000	252,000	252,000
Blocks 22-24	75,000	-	-
MSCP	750,000	19,200	149,549
Royal London	200,000	-	-
Total	1,295,000	271,200	401,549

Overall, we have taken Cushman & Wakefield's more conservative estimates of retained business rates, to err on the side of caution. However, we have agreed to include all of the retained business rates arising from the MSCP as the LEP investment will 'enable' the construction of the whole car park. On this basis the EZ investment of £4m would pay back in 9.9 years.

7. Value for money

Following negotiation, the 'ask' from APL has been reduced to from £6m to £4 million in order to ensure an acceptable payback period to the EZ and provide good value for money to the LEP. APL have confirmed that the remaining funding shortfall will be met from APL resources drawing on either its bank facilities or via additional shareholder equity, which will result in a lower Internal Rate of Return and demonstrates a genuine willingness to deliver the scheme on behalf of the applicant. Cushman & Wakefield report that the project provides medium to good value for money in terms of cost per job created following the reduction in the 'ask' from £6 to £4m. The project can also demonstrate delivery of wider benefits in the form of local spend, collaboration, skill development and enhanced market profile and confidence.

8. Benefits

The benefits associated with the investment case are set out in the table below.

Benefit	Quantum
New commercial floorspace (sq ft)	97,000
Brownfield land reclaimed (ha)	N/A
Number of new businesses attracted to the EZ	15-30
Number of new permanent jobs created	300
Number of temporary construction jobs	331
Gross Value Added (£)	18m

Annual retained business rates (£)	401,500
Total retained business rates (£)	8.3m
Private sector leverage (£)	15.8m

9. Risk analysis

The following key risks are associated with this proposal:

Risk		Impact	Likelihood	Mitigation
1.	Estimated level of retained business rates not achieved.	Impacts on LEP's ability to repay debt, could lead to default on loans and reputational damage.	Moderate	LEP policy of only investing half of estimated retained business rates provides headroom if retained business rates are lower than estimated. We have adopted Cushman & Wakefield's much lower estimates of retained business rates from the two projects.
2.	Developers do not deliver projects on time or on budget.	Delays in completion of schemes would impact on level of retained business rates, whilst budget overruns would further increase the viability gap on schemes.	Moderate	Bruntwood are an established national developer with a strong track record of developing at Alderley Park. They have recently entered into a new £350m joint venture with Legal & General. EZ investment is capped, any cost-overruns are met by the applicant. We build long-stop start and completion date into our legal agreements.
3.	Schemes do not achieve practical completion, which does not trigger the payment of business rates.	Would impact on the ability of the LEP to repay funding.	Moderate	Track record of the developer and a longstop completion date set within the legal agreement, with clawback penalties for under-performance.
4.	Developers deploy rate mitigation schemes to avoid empty rates.	Could reduce empty rates payable to 25%, would impact on the ability of the LEP to repay borrowing.	Low	A 'no rate mitigation' clause built into the EZ investment legal agreement, which means that developers cannot mitigate their empty rates liabilities.
5.	Schemes do not attract occupiers.	Limited impact as developers/landlords still have to pay empty rates	Moderate	Applicant has demonstrated that occupiers are currently being turned away or directed to unsuitable space due to the lack of existing supply.
6.	Investments are not deemed to be State Aid compliant.	Limited impact as the risk on State Aid sits with the developer	Moderate	Provision of a State Aid opinion as part of the legal agreement, which is assessed by the LEP's legal advisers. Clawback provisions in the legal agreement are triggered by any breach of State Aid.

10. Independent appraisal

Cushman & Wakefield have undertaken an independent technical appraisal of the proposed investment which notes that:

- (a) The projects demonstrate a good strategic fit with the overarching Cheshire Science Corridor Development and Investment Strategy, the site-specific Development Plan for Alderley Park and a number of wider local and national strategies for economic growth.
- (b) There is a clear demand for the projects, although market evidence is limited, the applicant has demonstrated that occupiers are currently being turned away or directed to unsuitable space due to the lack of existing supply. A vacancy schedule indicates c.50,000 sq ft of currently available space across Alderley Park is spread across a number of buildings and reported to be of low quality and therefore difficult to let. A schedule of enquires has been provided demonstrating interest from 51

businesses for c.330,000 sq ft of bioscience (laboratory and office) and tech/office space at Alderley Park over the next two years – over 6 times the existing available supply.

- (c) The applicant has over-estimated both the job and GVA outputs from both projects, applying higher job densities applicable to general office space to the projects. However, even when Cushman & Wakefield apply lower job densities for laboratories, the projects still represent medium to good value for money in terms of job creation and GVA relative to the EZ ask.
- (d) The applicant estimates that the projects would generate c.£1.3m per annum in retained business rates, which would provide a payback of 4.6 years. However, Cushman & Wakefield have tested this and found it to represent a significant overestimation including counting the retained business rates from Royal London. Cushman & Wakefield's estimate, when accounting for the whole of the MSCP is £401,500 per annum, which would increase the payback to 9.9 years (based on full occupancy). This is on the cusp of acceptable payback period for the LEP. Cushman & Wakefield note that this represents a risk to the investment and could limit the opportunity to invest in other 'better value' projects. However, it should be noted that it is difficult at this stage to estimate the likely Rateable Value of the MSCP. Cushman & Wakefield have based their assessment of the MSCP on a comparable from an MSCP in Macclesfield of £135 per space. The applicant has used a range of comparables from Wilmslow, Alderley Edge and Knutsford that range from £300-600 per space.
- (e) In terms of delivery, the site is in the freehold ownership of the applicant and is understood to have received planning consent for the proposed scheme and a clear and appropriate delivery strategy is in place. Bruntwood SciTech (the controlling entity of APL) is an established property developer and manager with extensive experience of refurbishment projects of a similar scale and value proposed, including early and ongoing projects at Alderley Park.
- (f) The State Aid legal opinion provided by Addleshaw Goddard (dated 20 May 2019) considers the funding request to be compliant under Article 26 of the GBER (Investment Aid for Local Infrastructure). Aid intensity is within the 50% allowance of eligible costs and a case is made for including the MSCP as critical to 'research infrastructure'. Cushman & Wakefield have raised concerns that the €20m per infrastructure project investment cap would be exceeded (totalling €22.9m) when the refurbishment of the two blocks and MSCP are considered together.

11. State Aid

Addleshaw Goddard have provided a State Aid opinion on behalf of Bruntwood, which has been reviewed by DWF, the LEP's legal advisers. DWF have stated that the State Aid opinion provided by Addleshaw Goddard, which is that the two projects are justifiable under Article 26 GBER (investment aid for research infrastructures) is satisfactory. However, they have also recommended that a "back-up" argument is also applied under Article 56 (aid for local infrastructures) GBER if there is any doubt as to whether the two projects actually qualify as research infrastructure. Bruntwood have confirmed via email that they will apply the Article 56 route as a back-up State Aid justification.

12. Investment agreement

An Investment Agreement has been drawn up by DWF acting for the LEP and Addleshaw Goddard acting for the applicant and a Term Sheet setting out the key commercial terms in the legal agreement is set out in **Appendix A**.

13. Funding

The investment will be funded through the EZ Borrowing Facility established with Cheshire East Council which will be repaid through the retained business rates generated.

14. Conclusions and recommendations

The two projects for Block 22 and Blocks 23 & 24 at Alderley Park approved by the EZ Board and the Performance & Investment Committee represents a good investment for the Enterprise Zone. The projects provides a clear fit with the vision, strategic objectives and investment priorities set out in the EZ Development and Investment Strategy and provides a good ROI in terms of retained business rates and wider economic benefits to the Cheshire Science Corridor and sub-region.

On this basis, it is recommended that the LEP Board ratifies the decision of the Enterprise Zone Board and the Performance & Investment Committee to approve the investment in the Block 22 and Blocks 23 & 24 projects at Alderley Park and delegates authority to the Chair of the Enterprise Zone Board to sign the legal agreement with the applicant.

15. Appendices

Appendix A – Investment Term Sheet

Appendix B – Business Case

Appendix C – Technical Appraisal

Appendix D – EZ Board Paper

Appendix E – EZ Board Clarifications Paper

Appendix A: Investment Term Sheet

Recipient:	Alderley Park Limited
Project Name:	Block 22 and Blocks 23-24
Amount of Investment:	£4,000,000
Purpose:	Development of 9,011 sqm (c.97,000 sq ft) of refurbished laboratory space and a new 2,247 space multi-storey car park (MSCP) at Alderley Park.
Funding:	Local Authority Borrowing
Repayment:	From Enterprise Zone Retained Business Rates in connection with the Project, with a restriction on the Recipient utilising any rate mitigation schemes.
Length of time site must be maintained to Approved Use:	10 years
Key Milestones:	The Recipient is obliged to adhere to the following key milestones within the project: (a) Longstop start date within 12 months (i.e. drawdown of first claim) (b) Practical Completion within 3 years of start date
Draw Down of the Claim:	Retrospective monthly/quarterly claims up to the agreed Investment level, against various pre-conditions, including: (a) Funder satisfaction with Project Costs at letting of construction contract (b) Funder satisfaction of the State Aid position (c) Funder satisfaction with any third party funding (d) Recipient has obtained the necessary consents (e) Funder satisfaction with the form of guarantee
Overage:	An overage payment is payable by the Recipient, which is calculated on the sale price or an independent valuation at an agreed calculation date as follows: (a) Parties agreed project costs (b) Parties agreed priority return to investor of 25% (c) The Funder then achieves 50% of the Overall Surplus after those deductions. (d) Overage is payable on the earlier of Disposal or at the end of the investment period.
Permitted Changes:	Any and all changes must be approved by the Funder via a Project Change Form.
Permitted Disposal:	The Recipient the right to dispose of part of/the site without triggering the overage clause for leases under 35 years
Security:	A guarantee is to be provided by Bruntwood Sci-Tech Limited.
Events of Default/Clawback:	The Recipient will be required to repay the monies in the following events: (a) Any finding of State Aid breach (b) Lack of progress towards Milestones and Targets (c) Material Changes to the Project (d) Usual insolvency provisions
State Aid:	The Recipient is responsible for ensuring that the Project is provided in accordance with State Aid Law.
Monitoring:	Recipient to submit monthly monitoring returns with any investment claims until the end of the Investment Period, after which they will submit an annual monitoring return for the remaining Project Duration (10-years).
Boilerplate:	The document contains the usual provisions and protections regarding Freedom of Information, Bribery Act and Confidentiality for this form of transaction.