

Yeovil Innovation Centre

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Purpose of the Report

This report has been prepared in response to a request from Scrutiny Committee. The report answers specific questions raised by the Committee in relation to the operation of the Yeovil Innovation Centre (YIC). The questions and the responses are detailed in the report.

Much of the detail included in this report is already in the public domain in separate reports or as part of SSDCs routine financial reporting procedures. For example the YIC Business Plan, The Business Plan for the YIC2 Extension and regular financial updates have all been reported and approved by District Executive and/or Full Council.

Report Background

1. Rationale and general background.

The original feasibility study for YIC (Ancer Spa 2005) had identified a twofold need for an innovation and business incubation centre based in Yeovil. Firstly there was a geographical 'gap' for a sub-regional innovation centre, with Yeovil ideally placed between the high-tech industry centres of Exeter and Bristol. Secondly there was a need to help reduce Yeovil's over-dependence on a small number of large employers within the local Aerospace Sector. The intention was to facilitate the growth of small business, ideally (but not exclusively) within the valuable high-tech sectors. This would begin the gradual shift away from our dependence on the major employers without reducing local GVA whilst helping to increase productivity in the local and wider economies.

YIC enables the establishment and growth of new businesses by providing a secure and supportive business environment that helps to de-risk business start-up and nurture businesses through their early years of development before releasing them into the wider business world. The centre assists tenants with business planning, creates opportunities to access specialist advice, helps them to make contacts to develop local business hubs and feed into supply chains.

The existing Yeovil Innovation Centre occupies a refurbished factory with a floor area of approx. 3,000 sq. m. The existing building comprises; approx. 800 sq. m. of 'anchor tenancy' space (this helps to financially underpin the whole operation); approx. 1,200 sq. m. of small and medium size units that form the wider tenancy space; approx. 1,000 sq. m. of shared facilities including a foyer, meeting rooms, administrative office space, kitchen, 'meet and greet' area, toilets and general access areas.

Yeovil Innovation Centre was officially opened in the spring of 2009 and South Somerset District Council (SSDC) became the operator by default when the procurement of an independent operator proved unsuccessful due to the prevailing national economic climate at that time. It should be noted that despite being opened at the height of a severe economic recession, the centre enjoyed both early and continuing demand and success.

2. The legal and statutory position

The YIC site was originally acquired and refurbished with capital grants from three funding partners:

Somerset County Council (SCC) -	£ 750,000
South Somerset District Council -	£1,200,000
South West of England Regional Development Agency (SWERDA).	£2,910,000

Note that the interests of the latter organisation passed to the Homes and Communities Agency (HCA) in 2012.

The resulting 'Funding Partnership' is bound by formal legal agreements that set out the agreed use of the building. These legal agreements include certain conditions:

- The terms of the SWERDA grant state that the funding was awarded for the development and running of an innovation and business incubation centre.
- There are 'claw-back' clauses in both the Funding Partners Contract and the Operating Contract to legally protect this position. These documents are signed and sealed by all parties and require contract variations even for minor changes.
- There is a charge (held by HCA as a contingent asset assigned to them on the demise of SWERDA) on the title deeds of the premises that prevent the use of the YIC for any other purpose than that of an Innovation and Business Incubation Centre. This means that whilst SSDC own the land and the building, the HCA can ensure the use of the site for its designated purpose.
- Cessation of the use of YIC for its intended purpose could result in a request to repay the original grants.
- Sale of the YIC would result in the financial proceeds being shared by the funding partners in proportion to the amount of capital they originally invested.
- HCA as the majority funder (and not SSDC) hold the 'step-in' rights if the original project is varied or abandoned.
- The use of the centre for its intended purpose is also governed by State Aid Exemption agreements.

Therefore the use of YIC for its current purpose is clearly defined and legally protected and cannot be varied by SSDC. The performance of YIC is monitored by the Funding Partners and this process is detailed at 3.14 below.

Report Detail

3 This section provides responses to specific questions and observations raised by the Scrutiny Committee. The questions are shown in bold italics and the responses in standard print.

3.1 It appears that the Innovation Centre may be required to broaden its original intended purpose and objectives to also generate income. In the commercialisation strategy it states the Income & Opportunity Development Manager will be tasked with overseeing and managing existing business units and developing them into self-contained and independent profit centres (such as the Yeovil Innovation Centre) and investigating new business and income opportunities and taking these projects forward to fruition on a similar basis of funding and development.

The Yeovil Innovation Centre is mentioned in the Commercial Strategy purely as a working example of a self-contained profit centre.

The strategy does not intend to infer that the YIC 'may be required to broaden its original intended purpose'. The purpose and scope of YIC cannot be changed and this is detailed in section 2 of this report.

Yeovil Innovation Centre was set up as a regeneration project and not an income generating project. Whilst we would not wish to sustain financial losses at the centre and making a profit is desirable, the primary function is to foster sound business growth for South Somerset (and further afield) and to benefit the wider economy.

3.2 *Members appreciate there is more pressure than before to make better returns on our assets but feel SSDC should prioritise as agreed previously the investment in growth of all sectors, to diversify its employment base, business support for all sectors is vital for the longer economic growth and prosperity of the district.*

The original and specific agreed aim of YIC was to help diversify the local economy away from its over-dependence on a small number of major employees operating in the aerospace and high tech sectors in Yeovil.

The YIC project is a way of helping absorb future shocks- particularly in the aerospace economy on which Yeovil is very dependent. Business start-up is accommodated at the centre to enable diversification, but we particularly encourage high tech start up because this sector will generate high levels of productivity and GVA (gross value added to the local economy). SSDC intervention in this sector will offer sound long-term benefit and value to the local economy. YIC also has a commitment to wider business start-ups and to companies from further afield wishing to test the local markets. Several tenants at YIC represent inward investment ventures into South Somerset from elsewhere in the country and Europe.

The wider Economic Development Service does not focus exclusively on the YIC and the service works on wider business support, infrastructure and employment land provision, town centre regeneration and 'softer regeneration projects' such as the organisation of specialist business events. Additionally the Economic Development Service has been responsible for delivering our Tourism activities. The service is responsible for providing business support across wide sections of the local economy.

3.3 *Members have expressed concern that phase 2 may not be required in terms of providing office space and alternative purposes should be considered, in particular with a focus on manufacturing diversifying the local economy and increasing employment and productivity.*

This concern has not been raised prior to this request from Scrutiny Committee. The YIC Business Plan (District Executive 2015) referred to the phase 2 extension and the full Business Case for the extension (Feb 2016) was agreed by the District Executive Committee and Full Council respectively- so there have been opportunities to air any concerns prior to this occasion.

The Business Case outlined the need for additional office space at YIC2- with a particular emphasis on the provision of small offices for small business start-up. Occupancy levels at YIC have generally held between 80% and 85% (with temporary extremes at 79% and 95%) over the last 3 years, which is as high as could be expected in any business centre with 'easy-in and easy-out' terms. Full centre occupancy would never be expected to be sustained in this type of operation. What is noticeable is the almost continual full occupancy of the smaller offices. There are rarely any small offices available even with reasonable tenant turnover. The vacancies invariably occur in the much larger offices. It has been tempting to consider converting the larger spaces into smaller offices, but larger offices are often needed to accommodate expanding businesses. One tenant slowly expanded their business over a period of years, moving progressively through the larger offices and is now occupying an anchor

tenant office. Additionally the larger vacant offices are well used for meetings and small conferences. YIC 2 aims to address the unmet demand for small offices and the new ground floor of YIC2 will almost exclusively comprise smaller office space.

It is also important to note that the YIC site has B1 planning use rather than the B2 planning use normally associated with manufacturing. Compatibility issues might also be created if manufacturing were to be permitted on a site that predominantly hosts office use.

3.4 What has been the performance of the Yeovil Innovation Centre since the last update to members in the business plan and Innovation Centre phase 2 project brief provided in 2015 Please provide:

- **Financial performance record from 2015 when the last business case was prepared.**
- **Levels of occupancy**
- **Turn Over – how long tenants have occupied the facility for**
- **How many business and organisations have gone on to expand and operate at alternative premises in South Somerset.**

Financial Performance Record:

The financial performance for YIC is reported as a profit and loss account as part of the monthly financial performance report to the District Executive Committee. Detailed narrative is provided on the Quarters if and when required. The table below shows performance since opening the operation with the minus (-) bottom line figures indicating profit.

	2007/8	2008/9	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17
	£	£	£	£	£	£	£			
Pay	0	93,452	127,636	88,522	103,572	126,650	155,338	152,408	144,978	145,234
Non Pay	48,764	89,170	115,024	134,281	151,998	200,593	204,402	202,614	236,792	190,854
Support Service	0	37,711	77,031	70,378	44,200	42,233	38,282	36,484	41,742	69,600
Income	-90,000	-20,557	-85,029	-159,319	-255,846	-352,734	-432,039	-429,704	-492,335	-434,314
	-41,236	199,776	234,662	133,862	43,924	16,742	-34,017	-38,198	-68,823	-28,626

* **The forecast for 2017/18 is approximately £35k net profit (forecast as of 31.12.17)**

Levels of Occupancy:

The tenant occupation level at YIC hit a peak of around 95% for a brief period in 2015/2016. As predicted, this was a temporary peak, but it drove the net income figures for the year towards £69k.

2016 saw the departure of some of our longer serving tenants and this impacted on the 2016/17 figures. The combined effect of this was to reduce the net income figure to around £29k – a position from which it has since recovered.

There has been a steady churn of tenants throughout 2017/18 with the current occupancy level now holding between 82% and 85%. The figures can vary on a monthly basis as tenants take up residency or vacate the building.

The following points are noted:

- Empty large suites tend to take longer to let and have greater financial impact when they become empty. They also attract NNDR even when empty. The vacant suites at YIC tend to be the larger suites, but they are nevertheless required for expanding companies and when vacant they do generate income as meeting spaces.

- The prevailing demand from business start-up is for smaller suites and this has been taken into consideration in the design of YIC2.
- The original feasibility studies for YIC suggested that occupancy would level off at around 85%. With occasional variations, this would seem to have been a reasonably accurate forecast and should remain the basis on which financial forecasts are made. 85% occupancy does not indicate lack of demand - it is the inevitable product of the 'churn' of tenants and very typical of the nature of these types of centre.
- It is believed that the break-even financial mark for YIC is around 60% occupancy. Higher occupancy rates produce disproportionately higher income levels because the overheads of the operation remain largely fixed regardless of the number of tenants.

Tenant Turn Over

The average length of occupation by the current tenants is currently 1.7 years with 10 tenants having been with us for less than a year. This does now indicate a reasonable 'churn' of tenants at YIC with some 30% of the total number of tenants turning over in 2017/18. In past years a far lower churn (a max 7 in any one year) has been the experience. Of the tenants at YIC only 2 currently exceed the 4 year Exit Strategy, but in both cases one or more of the exception points in that strategy are valid (see below).

Tenant turn-over tends to be largely natural but is also governed by the Exit Strategy as set out in the YIC Business Plan. The principle of a tenant moving-on after 4 years is explained to a tenant at the onset of a tenancy and the tenant's 'License of Occupation' makes specific reference to the 'exit strategy'.

The Exit Strategy advises:

It is not in the interest of any party to enforce the exit strategy before a business is capable of surviving outside the Centre. The Operator will establish the robustness of a business to move on before the exit strategy applies. Where possible, the Operator will support the exiting tenant to relocate within Somerset.

Exceptions to the four-year rule include:

- A company is deemed to be placed at undue risk if an exit is forced upon them.
- A company may be at a critical point of expansion or contraction and the exit is deemed to be inappropriately timed.
- A tenant has affected a move between suites within the Centre to accommodate the growth of a company and the company is deemed to be in a new phase of growth.
- Special consideration should also be given if a business is part of a wider cluster or collaboration within the Centre where the removal of that business will have a negative impact on the remaining tenants.
- A tenant may move to a full standard lease agreement and become an 'anchor tenant' at the Centre provided the amount of anchor tenancy space does not exceed approx. 8000 sq. ft. in total.
- In enforcing the exit strategy, the funding partners should not put the Operator in a position where overall financial operating losses may result.

Business Leaving the Centre and Business Expansion.

Business expansion and business growth are not synonymous and are difficult to measure - a business can expand in terms of premises or staff without growing its turnover or profit. Conversely a business can increase its turnover and profit considerably without the need to take on extra staff or take on larger premises. A business moving to larger premises is not necessarily an indicator that the business has grown.

We know that businesses leave the centre for a variety of reasons. Some are in growth mode and do need bigger premises- whilst some have simply moved their existing business elsewhere. We also know that some businesses do not experience the growth they expected with several returning to work from home – this in itself underlines the advantage of new businesses being able to use YIC without needing to commit to a long term lease.

Of the 31 businesses that we have tracked since 2013, we are able to break down accordingly:

Relocated to offices in Yeovil 29%
Relocated elsewhere in South Somerset 6%
Relocated outside South Somerset 6%
Reverted to home working 26%
Closed Regional Office 16%
Owner retired 6%
Ceased trading in existing form 10%

We are not readily able to measure the specific growth (or contraction) of businesses who leave the premises.

3.5 Please detail what level(s) of business support are currently available and if this is included in the tenancy package. Are there additional chargeable support packages?

SSDC has a Business Support Officer who is based either at Brympton Way or at the Yeovil Innovation Centre. Business support is offered to businesses from across the District and is generally carried out at that business or at YIC. We provide basic business support that will typically offer advice on Start-up, Business Planning, cash flow projections and marketing.

So far in 2017/18, 68 individual business supports on a 1:1 basis have been recorded and an additional 92 businesses have benefited from the Boost Networking sessions held at YIC (these are mainly guest speaker presentations on topics such as marketing, social media, business planning etc.) Additionally we respond to many more general business enquiries without recording these as a business support.

Business support from SSDC is free of charge and given without prejudice, but we are also able to signpost to additional and specialised assistance such as the Growth Hub (the national hub for business advice). We also advise on funding opportunities and funding sources, although it has been rare for a YIC tenant to request specialist funding advice.

Events have also been organised to showcase YIC tenants (and the services they provide) to overseas businesses.

3.6 In 2015 the business plan stated the criteria for tenancies will be widened but will maintain the central tenor of innovation. Has this remained? Please can you provide the latest criteria.

The original entry criteria for YIC tenants were based on SWERDA 'target sectors' (2009) and these were Aerospace/ Advanced Engineering, Creative Industries, Food and Drink, Marine Technology and Tourism. These sectors were deemed as business growth sectors for the South West, and the list was broadened for Yeovil Innovation Centre to include Medical, Information Technology and Finance.

The entry criteria were simplified for the 2015 revision of the Business Plan and remain current.

The published entry criteria (2015) states

- *The entry criteria had originally been based on the target sectors as previously identified by the South West Regional Development Agency. At this stage the criteria will be widened but will maintain the central tenor of innovation. It is intended that this position will be reviewed again in 2018 at the earliest, or at the latest in the next review of the business plan.*
- *If a tenant's ability to match the entry criteria is in doubt, then the matter will be referred to the Funding Partners for a view. A majority decision then prevails.*
- *These criteria will not apply to approximately 8000 sq. ft. designated as anchor tenancy space within the Centre, although the appropriateness of the anchor tenant should receive full and careful consideration.*

It is intended that the YIC2 extension should have a greater focus on high tech business where possible.

3.7 Please can you confirm if the objectives as detailed in the business plan remain unchanged?

The objectives for YIC remain unchanged from the 2015 Business Plan. These are best encapsulated in the YIC Visionary Statement as:

'Yeovil Innovation Centre exists to provide a dynamic and supportive incubation environment to accelerate the growth of ambitious, innovative firms in the South West region'.

The fundamental principles of the innovation centre are to provide:

- Flexible office space
- On-site support from a trained Centre team
- High speed broadband and excellent telephony
- A range of conference and meeting rooms
- Access to networking and collaboration opportunities

The Operator is also set specific objectives and these are to:

- Identify ways for the Innovation Centre to act as a catalyst for economic development.
- Market and promote the Centre. An annual marketing plan will be prepared and agreed by the funding partners.
- Provide flexible accommodation to support successive stages of tenant's development.
- Provide financial reports and other information as requested by the funding partners.
- Act as secretariat to the Funding Partners/Advisory Group.
- Identify and secure funding for provision of specialist services where possible.
- Provide an induction to new tenants re the facilities and technical services provided at the Centre.
- The assessment and vetting of prospective tenants.

- On-going administration of tenancies and front of house support services.
- In-house provision of some business advice for the Centre and the wider start-up community.
- Develop linkages with relevant knowledge bases including university and research establishments.
- Provide networking opportunities to enable businesses to learn from and do business with each other.
- Creation of links between finance and investment ready companies.

3.8 *If the objectives have changed please provide the revised list agreed by funding partners and confirm when and how they were last reviewed?*

There has been no change to the objectives, they were reviewed and accepted by the Financial Partners in 2015 and will be due for review in 2018/19, ideally once the YIC2 extension is operational. The Business Plan will be reviewed at that stage.

3.9 *Is there any intention to revise the objectives with regard to improving return / generate a greater income? (As suggested in the Commercial Strategy.)*

With reference to 3.1 and 3.2 above, there is no intention to revise the objectives with regard to generating greater income. The Commercial Strategy does not imply that this should be the case for the Innovation Centre. The term 'income generation' also encapsulates obtaining external grant funding and/or cost reduction in order to enhance services or to assist services in becoming self-financing.

The Business Case for YIC2 does however illustrate that YIC can expand without unduly increasing certain fixed costs such as staffing the centre. This will ultimately increase income without revising the objectives. The objectives will remain primarily focussed on tenant support and not income generation.

3.10 *We know SSDC has experienced problems recruiting the right calibre of staff in the Economic Development Team. Do we have enough staff resource to achieve the Business plan as detailed in 2015.*

The Economic Development Team has had no recruitment issues in recent years, although any vacancies that have occurred in the team in the last 12 months have been held over pending Transformation. These posts are now being filled through the Transformation process as the service is strengthened. The new Economy Lead Officer is already in place.

Under the new operating mode (as with all Commercial Services business units) YIC will also review any resource needs that it may have for the future as part of its ongoing business planning. The Commercial Services team will be responsible for the Operational Management of the Innovation Centre, and they will be supported by competent and capable staff as required.

The Economic Development team will be responsible for ensuring the YIC fulfils its core purpose and plays its part in the development of the South Somerset economy

3.11 *Members are still keen that Economic Development remains a high priority. We do not want to see the Innovation Centre and other related work around growth and business diversification suffer. Is there anything that can/needs to be done to prevent or reduce risks to achieving the objectives?*

Economic Development remains a top priority for South Somerset District Council and has no intention of diminishing our business support activities at YIC or in our activity to foster business growth and diversification within South Somerset and beyond. Transformation will expand the ED team with

additional resource available through the new Commercial Land and Property Development Team – see 3.10 above.

3.12 Are the current charges subsidised or at Market Value and regularly reviewed?

Charges at YIC are not subsidised. Rents were originally set by the Valuation Office and whilst first year tenants qualify for a small discount, the discounted rate is still equivalent to current Market Values in Yeovil. Business rates are a statutory charge and set by the Valuation Office and cannot be discounted. Service costs are set by wider commercial markets and these are not subsidised by the District Council

The charges are regularly reviewed, with adjustments likely to be made in 2018/19 with the opening of YIC2. Our tenants pay all charges at going market rates. In return they expect and receive a high value service from SSDC.

3.13 Are there conditions or commitments as part of the LEP funding?

The specific conditions associated with the LEP funding are for YIC to continue the operation for its intended purpose as an Innovation/Incubation Centre.

As is standard practice with LEP funding (and most public funding streams) there is also an agreed set of outputs and outcomes that the project will be measured against.

These outputs are based on job creation, business creation and ‘business safeguarded’ targets

Output/Description	Year 1*	Year 2**	Year 3	Year 4	Year 5	Total
Jobs in Construction Phase	25					
New Business Created by YIC2		7	7	7	7	28
Jobs created (indirect) at YIC2 (this includes jobs created by businesses growing whilst at YIC2)		17	19	23	29	88
Business Safeguarded (supply chains) using HCA recommended multiplier (Businesses created X 1.44)		10	10	10	10	40
Jobs safeguarded (supply chains) using HCA recommended multiplier (Businesses created X 1.44)		24	27	33	42	126
Business Supports incl. ex tenants		2	9	9	11	30

*Note: Year 1 will be 2017/18

**Note: Year 2 will be 2018/19 and will be the first year of operation for YIC2

3.14 The current governance, including the refreshed Terms of Reference, monitoring and reporting arrangements of the Innovation Centre – a copy of the latest quarterly report

The Governance arrangements are unchanged from the reported detail in the 2015 Business Plan

The Operator (SSDC) reports to the Funding Partners against an evaluation scheme based on the agreed project outputs.

The Funding partners Board comprises:

SSDC Portfolio Holder (Economic Development and Environment) - Chair
 SSDC Director (Commercial Services and Income Generation)
 SCC Portfolio Holder (Economic Development)
 SCC Lead Officer (Strategic Manager for Economy and Planning)
 HCA Specialist Advisory Officer

Other Officers can be requested to attend as required.

For SSDC, strategic decision making is vested in the District Executive Committee (or Full Council for projects with major financial implications) with monthly and quarterly financial reporting to that committee. The business support is reported through SSDC Council Plan monitoring.

The funding partners meet twice a year and agree the financial and operational decisions for the Centre.

However, quarterly financial reports are made to the Funding Partners. As the partners all have a financial interest at YIC that includes profit sharing, the accounting spreadsheets are forwarded electronically to them for transparency and they may interrogate the detail with SSDC financial officers if required. The spreadsheets themselves are quite extensive documents and do contain much commercially sensitive data (for example anchor-tenant rentals and commercial service charges) these and other data are covered by the Data Protection Act and for that reason are not public documents.

The accounts for YIC are covered by statutory financial regulations and are thus subject to regular internal and external audit to ensure compliance. The operation of YIC is also subject to regular external audit (there have been two in recent years) and these audits have provided considerable levels of assurance. The audits are published documents. Financial reporting is made at a headline level to the District Executive Committee as outlined in section 3.4 above.

Other performance measures are reported to the Funding Partners and are a record of an agreed set of outputs set by those partners. The key outputs recorded include:

Project Outputs	2014/15	2015/16	2016/17	Forecast 2017/18
Number of Tenants at YIC	28	32	31	c33
Businesses Created annually	2	2	7	6
Ratio of businesses created Indigenous: inward investment			2:1	2:1
Businesses created cumulative	25	27	34	40
Jobs created annually	4	8	14	10
Jobs created cumulative	124	132	146	156
Jobs safeguarded annually	120	132	135	135
Business supported annually	c75	c75	c75	100+
Number of new networks created	2	2	2	2
Recovery of temporary Operator costs	£34k	c£68k	c£29k	c.£45k

3.15 The latest version of the development plan

The link to the YIC2 Project Brief is provided below (background papers).

The final costings and output projections for the project remain unchanged, but the planning and design processes resulted in a minor reduction in overall footprint of the building (approx. -4%) without affecting the amount of office floorspace that will available in YIC2 for tenants.

3.16 A breakdown of the current tenants by service area:

This breakdown of current tenants by service area is:

Aerospace	8%
High Tech	45%
Service Provision	20%
Media and Comms	23%
Education	4%

The most notable change since 2015 has been an increase in High Tech, Media and Comms occupancy whilst other occupancy levels have fallen in relative terms.

A clearer distinction between high- tech and service provision would be useful in interpreting these figures. For example; should a website design company be classed as high-tech or a service provider? The next revision of the Business Plan will address this issue so that a more meaningful and consistent way of measuring sector take-up at YIC can be implemented.

Background Papers

- *YIC Business Plan 2015-2020 (District Executive Dec 2015)*
 - *YIC2 Project Brief (Full Council Feb 2016)*
<http://modgov.southsomerset.gov.uk/documents/g1513/Public%20reports%20pack%2004th-Feb-2016%2009.30%20District%20Executive.pdf?T=10>
page 84, 92, 93 and page 94-104
 - *Capital Budget details:*
<http://modgov.southsomerset.gov.uk/documents/g1830/Public%20reports%20pack%2001st-Feb-2017%2009.30%20District%20Executive.pdf?T=10>
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