

# **Report on an Urgent Decision taken by the Chief Executive in consultation with the Leader to Fit out the First Floor of Yeovil Innovation Centre (YIC)**

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## **Purpose of the Report**

1. The report sets out the details of an urgent decision taken by the Chief Executive in consultation with the Council Leader for approval for SSDC to fund fit-out works for the first floor at Yeovil Innovation Centre phase 2 (YIC2) three years ahead of forecast. This was with the objective of securing a letting of the floor to a single tenant who wish to be in occupation by September 2019, which will not be achieved without meeting the fit out costs. As well as supporting the YIC business plan the letting will secure and attract around 100 jobs for the local economy.

## **Decision Taken**

2. That the Chief Executive in consultation with Council Leader approved:
  - a. capital funding of up to £320,000 from the useable capital receipts reserve to meet the cost of fit-out works and furniture for First Floor at YIC2;
  - b. to add the revenue income stated in the confidential appendix to the Medium Term Financial Plan;
  - c. that expenditure shall only be committed if a legally binding agreement for lease has been concluded with GP Strategies on the basis set out in this report;
  - d. that prior confirmation shall be obtained from partners in YIC that SSDC may retain the full revenue impact of this letting to provide return on this capital and recovery of that capital until the full sum has been recovered, and thereafter revenue will accrue to YIC in the normal way; and
  - e. the Director of Commercial Services and Income Generation be authorised to approve the details of specification and lease terms, or to delegate as appropriate.

## **Reasons for an urgent decision**

3. The potential tenants are seeking occupation by 1 September 2019. Urgent decision making is therefore required to secure this opportunity for YIC and the jobs for the local economy. To successfully implement this will need the decision to be followed by rapid conclusion of the agreement for lease, specification and implementation of the works.
4. This decision would normally be dealt with by a District Executive report for members as it involves the use of capital receipts, but due to Elections the next meeting is not until June and the opportunity will be lost unless an urgent decision to proceed is made.

## Background

5. Yeovil Innovation Centre has been operating as an effective business incubation facility since 2009. A second phase – YIC2 was completed in autumn 2018. The Business Plan 2019-2024 for YIC recognised that introducing the additional space comprised in YIC2 would reduce overall occupancy levels for a period, projecting that it would take until 2022 at the earliest to return to 80-85% occupancy. The ground floor of the extension comprises a large number of smaller units, whilst the upper floor would be developed and fitted out according to demand. The first floor is currently only finished to shell specification. All occupiers would expect the landlord to meet the cost of a typical landlord's fit out (known as category A fit-out). It is then the norm for tenants to determine and fund their own fit-out (category B) and procure furniture but it is frequently the case that landlords grant a rent free period which contributes towards the costs.
6. No funding provision is already established to meet the capital costs. The revenue budget for YIC is based on the assumption this floor remains unused for at least three years. Without an occupier, there will be a service charge void to cover and expectation is that it will be assessed for business rates also, which will fall to YIC while the space is vacant acting as an additional cost to all YIC partners and adversely affecting YIC viability. Even if the tenant leaves at the three year break or the end of the six year term, the capital costs will have been paid, the work that we would have to complete to let the space will have been done, and we will have an enhanced asset that should be attractive to other potential tenants.
7. While there is a fair prospect of other enquiries from time to time, no prospective lessee will meet the category A costs. It is hypothetically possible that a new lessee might agree to a structure where a long rent free period is granted to equate to the cost, but that is quite unlikely. It is reasonable to conclude therefore that unless the landlord finds a means to finance the category A works cost, the space will remain unlet and leave YIC with ongoing void costs. The estimated budget for category A works is £250,000.
8. An enquiry has been received and nurtured at YIC about a potential letting of the whole first floor from a company who already have some space in Yeovil and need to expand. They are also considering the closure of an office out of area and centralising their business close to Yeovil in one location which will bring additional high quality employment and inward investment to the area, and support one of our largest private companies.
9. Outline terms for the letting of the whole first floor at YIC2 have been discussed as follows:
  - a. Net lettable area: 4,015 sq ft (estimate subject to check measurement)
  - b. Lease term: 6 years with tenant break option after 3 years
  - c. Break option: Tenant only on 6 months' notice. 6 months rent penalty if exercised
  - d. Rent: as stated in confidential appendix
  - e. Landlord works: Category A works plus creation of 2 glazed partitioned offices. The additional cost of those offices effectively funded by the lessee dropping normal expectation of 6 month rent free letting incentive.
  - f. Effective full repairing and insuring lease. Tenant would be responsible for internal repairs and pay a service charge for the external structure, common parts and insurance. Tenant responsible for business rates.
10. The tenant is effectively funding the cost of the category B works by foregoing the rent free period that might typically negotiate, and the costs of the furniture by paying a premium rent element. Ownership of the furniture will remain with SSDC until the payment period has been completed.
11. Implementation of the fit-out works adds to the value of the asset by creating additional accommodation capable of immediate occupation and use.

12. Achievement of this letting will continue the economic development of Yeovil by supporting additional jobs in the town.

### **Financial Implications and Business Case**

13. The financial implications and business case are stated in the confidential appendix.
14. Taking in to account the income and the void costs the Council would incur, the payback for the capital investment is 2.8 years.
15. The agreement to the funds will have economic benefits too, securing and attracting approximately 100 jobs within the district that are a key part of our local aviation industry. It also enhances the asset and the lettability of YIC2 should the tenants leave at the break clause.
16. If the recommendation to agree funding of £320,000 from useable capital receipts is agreed, this will leave approx. c£7m of useable capital receipts remaining unallocated.
17. Should the funding not be agreed, then the Council will be liable to pay business rates and lose out on recovery of potential service charge costs as stated in the confidential appendix. These void costs are taken into account when assessing the pay-back period for the capital investment and the agreement with YIC partners will need to ensure the full revenue impact is received by SSDC until the full capital contribution has been recovered.

### **Risk**

The following risks, and mitigation measures have been considered:

- A. Capital costs are incurred and the lease does not complete so income not received. No commitment to works or their costs will be made by SSDC until legally binding agreement for lease is in place.
- B. Full revenue impact not received by SSDC. The business plan for YIC includes the shares agreed for any surplus made by YIC. Specific agreement will be needed from partners to permit SSDC to receive full revenue impact until capital has been recovered.
- C. Tenant defaults on lease once granted. Appropriate due diligence will be carried out on the proposed lessee to enable reasonable confidence in the strength of their business. Tenant failure cannot be entirely ruled out but the impact of the capital works will have enduring value in the ability to lease this area.
- D. Capital costs are above the levels expected. A contingency of circa 5% has been built in to the budget cost assessment. If actual proposals are above budget, then specifications will be value engineered to achieve budget.

### **Council Plan Implications**

18. Economy – delivery of this proposal contributes to strengthening the local economy by facilitating growth in local employment and delivering more usable accommodation for businesses.
19. Protecting Core Services – accelerating the occupation of YIC2 will bring forward the clearing of the historical operating costs accumulated by SSDC and then improve the operating surplus which SSDC shares in.

### **Background Papers**

Specific reference has been made to the Yeovil Innovation Centre – Business Plan 2019-24.