



Leicester
City Council

**WARDS AFFECTED
CASTLE WARD**

**Cabinet Briefing
OSMB
Cabinet**

**22nd November 2010
7th December 2010
13th December 2010**

82 – 86 RUTLAND STREET – CREATIVE INDUSTRIES WORKSPACE

Report of the Strategic Director Development, Culture and Regeneration

1. Purpose of Report

This report seeks Cabinet approval for conversion of Council owned buildings at 82 - 86 Rutland Street to workspaces for the creative industries sector.

2. Recommendations

- 2.1 Cabinet is recommended to note the report, and to approve the conversion of 82 – 86 Rutland Street to workspaces for the creative industries sector, and to:
- i. authorise the Strategic Director Development, Culture and Regeneration to agree and sign off the funding agreement with emda for ERDF capital support;
 - ii. approve capital expenditure on the project in line with the funding profile included in the report (para 5.1.3)
 - iii. approve the use of £426k WNF funds to support the project

3. Summary

- 3.1 The ambition for the Cultural Quarter is to see it thrive and develop as a vibrant attractive and sustainable focus for Leicester's cultural and creative sectors. Key to this ambition is to bring unoccupied and under-occupied buildings and sites back into economic use. This includes providing affordable workspace for cultural and creative businesses to enhance the investment already made in this area and to stimulate new growth in cultural and creative business activity.
- 3.2 82 - 86 Rutland Street is located in the heart of the Cultural Quarter. The building is Grade II listed property owned by the Council and currently unoccupied. The property is in a very poor state of repair and requires significant remedial works and investment to prevent continuing structural deterioration. The proposed refurbishment is an opportunity to bring an at-risk historic building back into economic use and meet a need and demand for expansion space for creative businesses within the area.

- 3.3 Funding for the first phase essential repair works (£246,000) has been committed from the Working Neighborhoods Fund (WNF). The cost of the second phase conversion works will be met by an approved ERDF grant of £646,000 matched by a further WNF commitment of £162,000. If not secured by the end of December the ERDF grant option will be lost. Significant ongoing maintenance costs will have to be incurred on this building if this project is not implemented. Once completed the historic building will no longer be at risk and will have appreciated significantly as an asset.

4. Report

4.1 Historical Context

The property comprises three separate linked buildings (with a total internal area of 9,000 sq ft) and is a textbook example of a mid 19th century integrated hosiery factory and warehouse. It is believed to be the oldest surviving example of a small purpose built factory where a number of knitters would work together for the manufacturer and warehouse owner rather than working individually at home.

It survives in an area of the City where large and significant factories and warehouses often replaced such earlier examples later in the 19th century. The properties form part of a very significant group of historic buildings including the Pfizer and Vogel building adjacent which dates from the early 20th century. The visual relationship is particularly important showing the contrast in scale between mid 19th century and early 20th century warehouses, one for hosiery, the other for leather.

4.2 Recent Context

The Council acquired the freehold of the then fully occupied properties in 1982. Subsequently the properties became part vacant in 1989 and then completely unoccupied in 2002 and have since remained so. The properties were Grade 2 listed in 2006. The Council last fully marketed the properties in August 2009 with a freehold guide price of £400,000. Two offers were subsequently received; however, both were significantly less than the guide price (under £200,000) and consequently not progressed.

The listed properties are at risk and are currently in a very poor state of repair. There are a number of areas of the buildings where works would be required to prevent further significant deterioration and structural damage.

4.3 Creative Industries Workspaces

- 4.3.1 The proposed scheme would involve the Council undertaking first phase essential preventative maintenance work and then secondly refurbishing the properties to a standard and configuration which would make them attractive as grow-on space for SMEs; in this case in the creative industries sector. It is proposed to convert the properties into five workspace units with a total area of 8,245 sq ft. The characteristics of the units and the overall development will be such that their size and quality will make them an attractive proposition to creative businesses seeking grow-on space. The location of the Rutland Street properties, in the heart of the cultural quarter, provides the potential for a market for such units drawn from businesses incubated at the LCB Depot and Phoenix Square.

- 4.3.2 A property strategy for the Cultural Quarter prepared by Lathams and commissioned by the Council, Blueprint and Prospect Leicestershire (October 2010) proposes a number of actions to develop and consolidate the Cultural Quarter. The Rutland Street property is specifically cited as a flagship workspace project supporting and complementing the development of a cultural cluster within the area. Delivering the strategy will be co-ordinated by LCC in conjunction with other stakeholders in the area including Curve, Phoenix Square and DMU
- 4.3.3 Indications from both LCB Depot and Phoenix Square support a demand for grow-on space for units within a range of 1,000 sq ft to 2,500 sq ft; floor areas which could be readily accommodated within the Rutland Street properties while largely retaining its original internal layout and features as a former factory and warehouse. The Depot's units range from 160 sq ft up to around 800 sq ft. (currently enjoying near 100% occupancy); similarly Phoenix Square's offer is from 200 sq ft up to 900 sq ft with the majority of units being at the smaller end. The marketing strategies for the three facilities (LCB Depot, Phoenix Square, Rutland Street) would be aligned to ensure consistency for the overall property offer within the Cultural Quarter and to facilitate growth and retention of businesses in the creative sector. All three facilities will be marketed and managed by the same team.
- 4.3.4 As the above shows the new workspace will be a discrete, new offer that doesn't duplicate existing facilities. The LCB Depot is designed to offer incubation and start-up units and is populated by IT businesses, graphic designers, web designers, arts and creative sector support organisations. Similarly the Phoenix Square workspace offer is for start-up incubation sized units targeted particularly at the Digital Media sector.
- 4.3.5 The new facility will offer grow-on space which could suit expanding companies from either of the above. Two potential tenants are already in discussion with the LCB Depot management team. The space could also support designer/maker uses such as ceramics, fashion, jewellery etc for which there is a shortage of appropriate premises in the city at present. These organisations need workspaces that can house specialist production equipment and machinery, and the Rutland Street site lends itself to 'light industrial' activities of this nature. These uses would also be complementary to the Grade 2 listing of the building as a previous hosiery factory. The site could also provide grow-on space for start up and graduate businesses emerging from the DMU Innovation Centre and specialist faculties and courses at DMU. The existing DMU Innovation Centre is based on the DMU campus but like LCB Depot offers small start up spaces and is an 'office' offer that doesn't support the designer/maker space offered by Rutland Street.
- 4.3.6 There are other existing workspace facilities in the city such as the Leicester Business Centre (LBC) in Belgrave which is also managed by LCC. However they do not serve the same creative sector market, being more generic business facilities and community based. The attraction of the Rutland Street facility for creative businesses is precisely the location and the consequent easy access to the network of other creative businesses and the city centre.
- 4.3.7 A glass atrium covering the courtyard and external passenger lift housed in a glass shaft within the courtyard, will provide the scheme with an architectural focal point. This will

set the project apart from a standard refurbishment and reflects and recognises the historical significance of the building, its location and potential function within the cultural quarter. The chosen design option retains and preserves the listed buildings original architectural features and functions.

- 4.3.8 The cost estimates have allowed for a BREEAM rating of 'Very Good' to be achieved which is in line with the rating level expected for conversion of existing properties.
- 4.3.9 The building will create more than 8,000 sq ft of floor space. As a marker the LCB Depot currently support 190 jobs with 22,000 sq ft. We would therefore hope that the new facility could support in the order of 50+ new jobs and we would anticipate that (like with LCB Depot and Phoenix Square) many of these will be graduate level jobs, helping us with our objective of retaining and encouraging graduate employment in the city.

5. Funding & Income / Cost Appraisal

5.1 Capital Funding

- 5.1.1 The total estimated budget costs for the scheme is £1,054,000. The key issue relating to assembling a funding package is the restrictive regulations governing ERDF assistance. Taking these regulations into account, together with the Euro exchange rate and ERDF intervention rate, results in ERDF support of £646,000, leaving a balance to be funded on the proposed total cost of the scheme of £408,000.
- 5.1.2 The WNF will allow first phase essential maintenance and repair works to be completed in advance of the letting of the main contract and will not count such costs against the substantive project application. This approach maximises the ERDF grant received. Given the current condition of the building, the Council would complete, as a first phase, elements of the overall project which address and remediate the deterioration and damage to the core structure of the buildings.
- 5.1.3 Works to the value of £246,000 would be required to be completed in advance of the main contract and would be funded by Working Neighbourhoods' Fund. This leaves a funding gap of £162,000 which represents 20% match of to the ERDF's 80% contribution.

Two options were considered to meet this £162,000 funding gap as shown in the table below:

- (i) A further capital contribution of £162,000 from WNF; or
- (ii) Prudential Borrowing.

Substantive Project	£
ERDF	646,000
Prudential Borrowing / or WNF	162,000
	808,000
<u>Essential First Phase Repairs</u>	
WNF	246,000

Total Capital Costs	<u>1,054,000</u>
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5.2 Income / Cost Appraisal

- 5.2.1 The operating costs of the workspace are estimated at £35,750 per annum (excluding borrowing repayments and interest). An assessment of the operational financial viability of the project under different market conditions and rental levels has been undertaken. These models indicate that the debt repayment for Prudential Borrowing can be serviced by net income receipts, even if a worst case scenario were to prevail. However, the deployment of prudential borrowing does generate a significant operational liability to be repaid over a long period and consequently a significant revenue shortfall in the early years of operation based on the worst case scenario.
- 5.2.2 All scenarios assume a prudent occupancy build up from 20% in yr 1, 40% in yr2, 60% in yr 3 and then 80% thereafter. As bench marks for rental the LCB Depot charges £11 sq ft pa inclusive of service charges; Phoenix Square £14 sq ft pa including service charges; and Belgrave Hall Museum charges range from £10 to £13 sq ft pa which exclude service charges and rates. The worst case scenario assumes difficult market conditions are reflected in a rental level of just £6.50 sq ft plus a service charge of £1.53 sq ft (total £8.03 sq ft). The best case assumes a rental and service charge level on a par with the Depot (£11 sq ft pa).
- 5.2.3 In the worst case scenario and assuming deployment of prudential borrowing, by year 4 annual rental levels exceed the total of running costs and prudential borrowing repayments. However, the cumulative operational deficit would have reached £58k by year 3 for which there is no identified means of funding. Prudential borrowing cannot be used to fund the operational deficits because the repayment period would be too long – even without interest the scheme could only repay such a loan over a 15 year period.

	Prudential Borrowing at £162k. Cumulative operational deficit	Prudential Borrowing replaced by £162k WNF. Cumulative operational deficit
Best Case : £11 pr sq ft	(£36,000)	(£8,000)
Worst case : £8 pr sq ft	(£58,000)	(£18,000)

- 5.2.4 Once completed the value of the building as an asset will have appreciated considerably. The ongoing costs of maintaining a deteriorating listed building will also have been removed.

5.3 Recommendation

- 5.3.1 It is recommended that additional WNF resources of £162k are deployed to fund the remaining capital gap and that £18k WNF is deployed to cover the operational deficits in year 1 and 2. Together with the original repairs contribution of £246k that amounts to a total of £426k from the WNF programme.

FINANCIAL, LEGAL AND OTHER IMPLICATIONS

6. Financial Implications

- 6.1 The recommended use of WNF rather than prudential borrowing to fund the non ERDF capital and early years' operational deficits is recommended. Saddling schemes such as this with significant debt finance charges over a long period inevitably means greater risk that scheme will run into financial difficulty. Furthermore there is no obvious means of financing the operational losses in the early years which are increased by the debt repayments. Taking out further loans to fund revenue deficits would add to this risk and require an excessively long repayment period.
- 6.2 Given the recommended funding option the financial model has been assessed as prudent and sustainable as outlined in section 5.

Martin Judson, Financial Services

7. Legal Implications

- 7.1 In entering into a funding agreement with EMDA, the Council will be bound by the terms and conditions of the agreement, including those requiring actions to be carried out in accordance with the timescales set out in the agreement, the disposal of assets and the potential for repayment in the event of default.
- 7.2 The terms of the agreement (as presently drafted) provide that EMDA may seek repayment of the grant for any breach of its terms by the Council. There appears to be no restriction on EMDA's ability to terminate the agreement. Similarly clause 6 provides EMDA with wide powers to vary or withhold grant payments, particularly if the expenditure profile is not met or the deadlines for spend are not achieved. Should EMDA adjust the grant or seek repayment, the Council's protection under the conditions is limited and would need to rely on the general law relating to disputes under contract. The draft also contains other terms in respect for potential liability for other matters (such as responsibility for additional costs and fees and indemnities) that will need to be clarified before the agreement is finalised.
- 7.3 The terms of the draft agreement provide that the Council may not dispose of its assets (here meaning a disposal of the freehold interest or grant of a long lease) without EMDA consent. EMDA's consent will be subject to a condition whereby all or a proportion of the proceeds of any future disposal will be payable to EMDA to repay the grant. This will not affect the grant of short-term leases of the completed premises, as the application states that as the leases of the workshops will be on a short term basis, they will not fall within the definition of "disposal" under the agreement.

John McIvor, Team Leader (Property & Development), Legal Services, (ext 29-7035)

8. Climate Change Implications

Bringing this building back into use will result in an increase in city-wide carbon emissions. In order to keep these emission increases to as low a level as possible the scheme should aim to reach a high standard of BREEAM rating and during the conversion process action should be taken to make the building as energy efficient as possible. The businesses which move into the converted units should also be provided with information about how to use the building as efficiently as possible and simple actions they can take to ensure their carbon footprint is as low as possible.

Helen Lansdown, Senior Environmental Consultant - Sustainable Procurement

9. Other Implications

OTHER IMPLICATIONS	YES/ NO	Paragraph/References Within the Report
Equal Opportunities	YES	The development will be compliant with requirements of the Disability Discrimination Act
Policy	YES	The proposal is in line with the Council's Local Plan. All procurement to be carried out within approved procedure.
Sustainable and Environmental	YES	A sustainable and environmentally acceptable design will be a major feature of the project
Crime and Disorder	YES	Unoccupied / derelict properties are at an increased risk of vandalism and unauthorised entry. The development will incorporate Secure by Design Principles.
Human Rights Act	NO	
Elderly/People on Low Income	NO	
Corporate Parenting	NO	
Health Inequalities Impact	NO	

10. Risk Assessment Matrix

Risk	Likelihood L/M/H	Severity Impact L/M/H	Control Actions (if necessary/appropriate)
1. Worst case scenario prevails in respect to market take up of space and rental rates	M	L	The business case has assumed a worst case scenario prevailing.

achieved.			
2. Additional unforeseen capital costs arise during conversion	M	L	The detailed cost estimates contain an element of contingency to meet cost over runs. The project specification would be revised to contain costs.
3. Loss of ERDF funding	M	H	Sign ERDF agreement by end of December 2010
4. Failure to comply with terms of EMDA grant conditions	L	H	Ensure that any conditions of the grant are capable of being complied with, or that a reasonable extension can be obtained if necessary
5. Likelihood of repayment being required	L	H	To comply with the terms of the agreement, and in particular any key stages or milestones in order to avoid repayment triggers
6. Clawback of funds on future disposal	L	M	The property will need to be retained during the period of any restriction that would trigger clawback
7. Indemnity in respect of costs and fees	L	H	To ensure as far as possible that any such indemnity is in respect of costs and other matters that are directly the Council's responsibility

11. Background Papers – Local Government Act 1972

St George's Leicester – Cultural Quarter Property Strategy. Lathams Oct 2010.

12. Consultations

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