Appendix 1

Proposed changes to criteria and guidance for the Business Growth Programme – for consideration and approval by the LEP Board, 18 July 2019.

1. Background

The Business Growth Programme (BGP) provides grant support of between £10,000 and £250,000 to eligible businesses towards capital related investment (plant, equipment, machinery and premises fit out/refurbishment) that leads to job creation. The programme provides a contribution of up to 20% of cost for small businesses (less than 50 employees) and 10% for both medium sized (50 - 249 employees) and large businesses (250 employees and above).

Since April 2015, the programme has been funded through the Local Growth Fund and currently runs until March 2021, with a total budget of £44.3 million. As of June 2019, £33.98 million had been offered to over 600 businesses, with 5,548 new jobs contracted for, against a programme target of 4,100 by March 2021. Actual expenditure as of June 2019 was £29.18 million, with 4,021 new jobs created. Inclusive Growth principles and criteria have been embedded in the programme since July 2018, and these were further strengthened in March 2019 for delivery from July 2019.

2. Sector Eligibility

Current criteria and guidance – priority is given to businesses operating in the key growth sectors, and/or, their direct supply chains, of the current Strategic Economic Plan for Leeds City Region. These are:

- *Healthcare and life sciences;*
- *Digital and creative;*
- *Low carbon and environmental;*
- *Manufacturing;*
- *Financial and professional services;*
- *Business to business services.*

Applications from businesses operating outside these sectors are currently considered on a case by case basis, with business-to-business operations prioritised. As of April 2019, applications from businesses operating outside the key growth sectors represented 15.7% of all grants awarded.

The highest volume of applications received from businesses operating outside the key growth sectors are from industries associated with the manufacturing sector, such as warehousing and distribution.

There are also a number of on-line retailers that have been supported through the programme. Positive factors considered within the appraisal of such applications have been the exposure to national and international markets, significant levels of

job creation and the regeneration benefits of brining large industrial units back into use in more disadvantaged parts of the City Region.

Applications are not accepted from high street retailers or localised business to consumer services on the grounds of potential displacement.

Feedback from Business Investment Panel (BIP) on 30 April 2019 and Business, Innovation and Growth Panel (BIG) on 28 May 2019

BIP and BIG Panel were in favour of maintaining the current sector criteria and the above approach in relation to large on-line retail/distribution facilities.

Recommendation One to LEP Board

No changes are made to the sector criteria, but this will be reviewed following the conclusion of the new Local Industrial Strategy. Until then, it is proposed that applications from on-line retailers will continue to be accepted where significant levels of new employment will be created, significant being defined as more than 50 new jobs.

3. Additionality and Affordability

Current criteria and guidance – applications must clearly demonstrate the need for public funding i.e. the impact on the investment project and on the business of securing the funding versus the impact of not securing it. The size and financial health of the applicant is also a key factor in the appraisal process i.e. their ability to finance the project without public intervention.

The most common reason for the rejection of applications to the programme is the lack of additionality/added value. All applications to the programme are appraised in line with Her Majesty's Treasury Green Book. This includes demonstrating additionality/added value, which is tested by one or more of the following:-

- The grant fills a funding gap;
- The grant accelerates an investment;
- The grant enables an investment to be made on a larger scale;
- The grant influences the location of an investment (where businesses are considering competing locations outside the City Region).

All of the above incorporate an element of financial need. During financial year 2018/19, a comparatively high number of applications were rejected due to a lack of additionality/need for support. The main reasons for this were high levels of cash reserves held by applicants and the amount of directors' remuneration and dividends taken.

It is difficult to put in place a prescriptive ceiling in terms of cash reserves, as this will differ greatly by size and sector of business, payment terms to which a business works and levels of working capital required. However, in terms of directors' remuneration and dividends, an internal guideline limits this to a maximum of

£150,000 per director/shareholder, per annum, averaged over a three-year financial period. The average over three years aims to reflect fluctuations a business may experience in trading conditions, which can have a consequential effect in terms of the levels of remuneration and dividends taken.

At present, programme guidance issued to applicants does not formally highlight the fact that levels of remuneration and dividends taken (in line with the threshold outlined above), along with levels of cash reserves, could adversely affect the outcome of an application.

Feedback from BIP on 30 April 2019 and BIG Panel on 28 May 2019

BIP recommended that the £150,000 per annum per director remuneration/dividend threshold be adopted as policy (for grants of between £10,000 and £100,000) and that programme guidance be updated to reflect this.

Recommendation Two to LEP Board

Programme guidance is formalised to reflect that the maximum amount of remuneration (salary and/or dividends) per annum per director, averaged over a three-year financial period, is £150,000 (for grants of between £10,000 and £100,000). The primary rationale for this is to provide clarity for businesses, and those working with them, of the criteria at pre-application stage, which may influence their decision to submit an application. In turn, this should lead to fewer rejections and deferrals.

4. Applications from Large Businesses

Current criteria and guidance – applications are considered from large businesses (250+ employees), but the intervention rate is capped at 10% of the overall investment, or, at 200,000 Euros if De Minimis is applied.

Related to additionality and affordability, a number of enquiries and applications to the programme were received in 2018/19 from large businesses (over 250 employees), and/or businesses owned by a larger group. Whilst applications are accepted from large businesses, grant awards are restricted to 10% of eligible capital costs, or 200,000 Euros if De Minimis is applied, in line with State Aid regulations. In a number of cases in 2018/19, the grant request was below £100,000, which made the additionality case less compelling, particularly where there was a modest return on jobs created and/or wider regeneration benefits.

Feedback from BIP on 30 April 2019 and BIG Panel on 28 May 2019

BIP and BIG Panel agreed that applications from large businesses should commence at £100,000 and that there should be a good return on new jobs created.

Recommendation Three to LEP Board

Applications from large businesses continue to be accepted, but only where minimum total project costs are £1,000,000 and proposed new job numbers are at least 20.

Additionally, grant awards are restricted to 10% of eligible costs, even where projects are funded through De Minimis.

5. Productivity Focus

Current criteria and guidance – costs related to the fit-out / refurbishment of premises are eligible for support, with an intervention rate of 10 or 20% applied depending on the size of the applicant. The minimum grant award for such projects is £10,000 and the maximum is £250,000.

The City Region's business productivity (Gross Value Added per hour worked) is 86% of the national average. Closing this gap would add £10 billion to the City Region's economy, which, at individual business level, predominantly means investing in more technologically advanced equipment, systems and processes, and not always requiring additional staff to generate higher levels of output.

Within the context of the high number of SME manufacturers in the City Region, the LEP's economic policy is increasingly focused on how to support them to become more productive and competitive, including via investment in new technology, adopting the practices of Industry 4.0 across supply chains and through ongoing workforce development, including leadership and management.

The programme continues to receive applications from businesses requesting support towards fit-out and refurbishment of new/existing premises. As with the above, the additionality case for grant investments within such projects can be more difficult to determine, particularly if the applicant owns the premises, or, has entered into a lease agreement prior to application. There is also a stronger case for productivity improvements where the applicant is investing in new equipment and technology, perhaps alongside improvements to premises, as opposed to solely fit-out / refurbishment projects. On that basis, and in the context of a reducing overall programme budget, a number of options are open, namely:

a) Make fit-out/refurbishment of premises ineligible for support on the grounds of more limited additionality and lesser alignment with productivity drivers.
b) Only allow fit-out/refurbishment works as an eligible cost when they form part of a wider package of investment that also incorporates purchase of new plant and machinery.
c) Cap the maximum amount of grant funding for costs associated with fit-out/refurbishment of premises.
d) Similar to above, but reduce the intervention rates for fit-out/refurbishment elements of investment projects e.g.5% for medium and large businesses and to 10% for small businesses.
e) Continue as at present, with each application judged on its own merits.

Feedback from BIP on 30 April 2019 and BIG Panel on 28 May 2019

Overall BIP members felt that fit-out/refurbishment costs should remain eligible as otherwise some important business sectors, including Creative and Digital and Financial and Professional Services, could be excluded from support on the basis that large capital equipment investment is much less likely in those sectors. However, members also recognised the pressure on the programme budget and the need to secure additionality and productivity improvements. Therefore, members were minded to either continue to assess each application on its own merit, or, introduce a maximum amount or reduced intervention rate for fit-out/refurbishment projects. Members also recognised that additionality was particularly weak in situations where applicants had already entered into a commercial lease or had recently purchased the premises.

The BIG Panel members were also reluctant to fully withdraw support for fit-out/refurbishment costs on the grounds of potentially excluding support for some sectors, and because the appearance and standard of business premises are important for both staff morale and productivity, and for customer attraction/retention. However, members also recognised the additionality challenges of fit-out/refurbishment projects and expressed a preference for limiting grant support for those costs, but not an amount too low to effect any additionality, particularly if the applicant is a large business. Members were also in agreement that if leases had already been entered into, or premises had been recently purchased, the additionality case for fit-out/refurbishment costs is particularly weak.

Members requested that officers should undertake some scenario planning and analysis of recent applications to determine an appropriate route that would prioritise or incentivise capital equipment investment, but not entirely preclude fit-out/refurbishment costs. This activity has been undertaken within the Business Support Team and the outcome was that the most deliverable and business-friendly approach would be to reduce the grant intervention rate for costs related to fit-out/refurbishment as set out below.

Recommendation Four to LEP Board

Grant support for costs related to property fit-out/refurbishment remain eligible, but the maximum grant amount available to support such costs is £100,000. Furthermore, grant support for costs related to property fit-out/refurbishment are not eligible if the applicant has already entered into a commercial lease or has recently purchased premises. Costs related to fit-out/refurbishment will be considered when the applicant has occupied the premises for at least six months.

6. Multiple Applications

Current criteria and guidance – businesses are restricted to the submission of three successful applications within a three-year period, or, receipt of a maximum of £250,000 over the same period.

The above criteria was introduced in September 2017 with the primary rationale of encouraging businesses to plan more strategically in relation to longer-term capital investment, and also broaden the reach of the programme to businesses that have not yet engaged with support from the LEP or its partners.
Feedback from BIP on 30 April 2019 and BIG Panel on 28 May 2019

BIP and BIG Panel were in favour of continuing with the current policy of three successful applications within a three-year period, or, receipt of a maximum of £250,000 over the same period.

Recommendation Five to LEP Board

Retain the current policy in relation to multiple applications as set out above. Note that this applies to all applications to the Business Growth Programme, whether funded through the Business Growth Programme or Access to Capital Grants.

7. Appeals policy and process

Current guidance - businesses that have applications rejected have the right to appeal in writing within two weeks of being notified of the decision. Appeals against decisions to reject applications up to and including £25,000 are considered by the Executive Head of Economic Services, with appeals from £25,001 to £250,000 considered by the Combined Authority's Managing Director, with those of over £100,000 first being considered by the BIP.

It has been proposed that the appeals process should be revised to set out more clearly the circumstances in which an appeal can be considered, and the associated timescales. In addition, consideration needs to be given to the governance and delegation arrangements for appeals, particularly for applications of over £100,000.

Feedback from BIP on 30 April 2019 and BIG Panel on 28 May 2019

BIP and BIG Panel were supportive of revising the appeals policy and process.

Recommendation Six to LEP Board

The appeals policy and process is revised in the coming weeks and considered by the BIP and BIG Panel, before coming back to the LEP Board for consideration and endorsement. This will clearly set out the approach to grounds for appeals, timescales for appeals and governance/delegation arrangements.

8. Next Steps

It is proposed that Recommendations One to Five are implemented from Quarter 3 of 2019/20, and that work commences with immediate effect on Recommendation Six.