European Union
European Regional
Development Fund

ANNEX 1: BACKGROUND TO THE FUNDS

The North West Evergreen Limited Partnership (“Evergreen”) acting by its general partner, North West Evergreen (GP) Limited, the Greater Manchester Evergreen 2 Limited Partnership (“Evergreen 2) acting by its general partner Greater Manchester Evergreen 2 (GP) Limited, and the Greater Manchester Low Carbon (UDF) Limited Partnership (“LCF”) acting by its general partner Greater Manchester Low Carbon (UDF) (GP) Limited, wish to receive Tenders for an Investment Adviser and Operator Services contract.

BACKGROUND INFORMATION

The Joint European Support for Sustainable Investment in City Areas (JESSICA) was an initiative developed by the European Commission and the European Investment Bank (EIB), in collaboration with the Council of Europe Development Bank as part of the 2007-13 European Regional Development Funding (ERDF) programme. The core principle of JESSICA was to take a more commercial approach to the use of public funds in delivering regeneration and economic development. JESSICA has enabled ERDF and match funding to be invested through Urban Development Funds (UDF) in urban projects across the United Kingdom via loans, equity and/or guarantees. Returns from these investments are used to make new investments in projects thereby recycling the returns and creating revolving funds.

As part of the JESSICA initiative, the North West Urban Investment Fund (NWUIF) was established as an EIB managed holding fund to operate in the North West region. The EIB launched a tender process for the selection of two UDFs to receive resources from NWUIF. The role of each UDF was to facilitate the disbursement of NWUIF funding in the North West by making repayable investments in urban regeneration projects. Evergreen was selected as the UDF for the North West of England excluding the Merseyside sub-regional area.

In November 2016, NWUIF was novated from its original ownership structure to a wholly owned subsidiary of the Greater Manchester Combined Authority. Whilst the ownership of NWUIF has changed and EIB no longer retains a role in managing NWUIF, its core responsibilities are largely consistent.

Building on the success of its first JESSICA fund, GMCA allocated £60m of its 2014-20 ERDF funding allocation, for a Fund of Funds structure and underlying sub-funds. In November 2016, it was announced by the Ministry for Housing, Communities and Local Government (now Department for Levelling Up, Housing and Communities (“DLUHC”)), that the GMCA had been successful in its application. The Fund of

Funds initially managed £60m of ERDF investment through its two created sub-funds and received a further £30m of ERDF during the course of the Initial Investment Period. The Evergreen 2 fund invested £75m of ERDF monies (made up of £30m from Priority Axis 1a of the 2014-20 ERDF Operational Programme and £45m from Priority Axis 4b), whilst the Low Carbon Fund invested £15m under Priority Axis 4b. The Low Carbon Fund was initially allocated £15m under Priority Axis 4a, however, the pipeline of projects was not at a sufficiently advanced stage and as such, funding was transferred to Priority 4b where the pipeline was stronger.

Strategic Focus

Since 2014, England has moved to one national Operational Programme. This programme sets out the strategy for smart, sustainable and inclusive growth and the achievement of economic, social and territorial cohesion.

The strategy is built around functional economic areas and reflects the main priorities for development across these. It focuses most resources on the core objectives of innovation, SME competitiveness and the low carbon economy but recognises the need for targeted interventions under other objectives where EU funding can unlock barriers that matter strategically to specific areas in England.

GM identified the following priorities for the GM Fund of Funds:

1a – Enhancing research and innovation infrastructure and capacities to develop research and innovation excellence, and promoting centres of competence, in particular those of European interest:

Investments made by our Urban Development Fund will enhance research and innovation (R&I) infrastructure and capacities to develop R&I excellence, and promoting centres of competence, in particular those of European interest.

Science and Life Sciences are a key growth sector for GM. We are well positioned to deliver around this objective building upon the recent launch of the second GM&C Life Sciences Fund, the National Graphene Institute (NGI), and the Sir Henry Royce Advanced Materials Institute. Supported by other regional universities and the private sector, these assets will play a crucial role in addressing the challenges facing society and making advanced materials a catalyst for economic growth in the UK. We intend to build further on this base in places such as future expansions and new developments on the Corridor in Manchester.

The Ex-Ante Assessment provided confidence about the current and potential demand from final recipients for investment and the Urban Development Fund has provided much needed finance in this area to allow viable projects to capitalise on the commercialisation and research opportunities flowing from vibrant sector of activity. The Evergreen Funds have made a number of investments to comparable projects such as three phases of Citylabs, Didsbury Technology Park and The Hub.

EG2 will continue to develop, retain and exploit excellence in GM’s Science / technology / Innovation assets, through investment in the appropriate volume, specification and flexibility of commercial floor-space. This will include investment in the development of new sites, the remediation and redevelopment of brownfield and the development / refurbishment of commercial floorspace.

4a – Promoting the production and distribution of energy derived from renewable sources:

It was proposed that the Low Carbon Fund would invest £15m ERDF into activities eligible under this Investment Priority. Its objective is to increase small-scale renewable energy schemes. ERDF resources were allocated to support initiatives such as micro-energy installations, low carbon/ renewable energy generation, renewable/ low carbon decentralised energy networks, and ground/air source heat pumps. The Low Carbon Fund remains interested in supporting these measures to increase the production of renewable and low carbon energy through the deployment of renewable and low carbon heat and power through, for example, decentralised energy networks, however, will look to come back to this priority when true demand can be evidenced by the Fund Manager which will support discussions with DLUHC.

The activities undertaken by the final recipients will support delivery of the output indicators identified under this Investment Priority.

4b – Promoting energy efficiency and renewable energy uses in enterprises:

The objective of this Investment Priority is to promote increased energy efficiency in particular in SMEs. The Investment Priority presents an opportunity to use ERDF resources to support improvements in the buildings. This includes energy efficient new buildings as well as deep renovations of existing buildings. The Investment Priority recognises the use of Financial Instruments to deliver the creation and refurbishment of urban infrastructure.

Our investments will increase innovation in, and adoption of, low carbon technologies. Such projects cannot currently attract conventional private finance but the public sector is able to support a number of these viable projects in the short to medium term until the mainstream finance market matures.

The activities undertaken by the final recipients will support delivery of the output indicators identified under this Investment Priority.

MARKET CONDITIONS

The North West of England, its economy and its diverse communities have demonstrated significant growth since the inception of the original Evergreen Fund. However, as the country emerges from a recession and still attempts to stabilise the economy, there remain hard choices to be made about public expenditure and the context for regeneration is a challenging one. The approach to investment that has been developed no longer assumes that resources necessary to create the conditions for growth will be available from the public sector, and focuses on recyclable investment leveraging private sector capital. Market constraints and lending regulations have reduced the accessibility of debt finance to support viable schemes. Evergreen has recognised these problems and has developed a proposition which has successfully created a new framework for growth - a now tried and tested investment model with clear priorities, and robust and professional scrutiny and governance arrangements.

This is why the Evergreen Funds remain so critical to our region's prospects. Evergreen has become a major investor in the North West economy, underpinning its long-term growth and stability through the prudent investment of public and private sector funding.

Whilst prime schemes in prime areas of the region are starting to attract investment at some positions in the funding stack, particularly if there is a strong pre-let element to the scheme, there is still a clear need for the Funds, both to bolster private sector investment in the prime opportunities, and to fund schemes that are outside of the prime classification.

Low carbon and renewable energy schemes also struggle to attract investment as they tend to have high up-front capital costs and relatively low long-term returns. Whilst they can provide long-term stable income once operational, these initial high capital costs and long project lifetimes mean that they can struggle to meet commercial funding hurdle rates. The challenge of guaranteeing revenue streams over long lifetimes can also result in schemes having a higher risk profile that conventional property investments. This is a particular barrier to funders who may not have invested in low carbon or renewable schemes previously. The provision of public sector funding can help to leverage private sector investment by assisting with funding for the initial capital costs and demonstrating long-term stable returns.

FUNDING ALLOCATIONS AND EXISTING PORTFOLIO

Evergreen has an existing allocation of 2007-13 ERDF and national match funding totalling £60 million. To date, Evergreen has invested in projects that result in the creation of commercial floorspace in Greater Manchester, Lancashire and Cheshire in line with the objectives of Action Area 3.2 and 4.3 of the 2007-2013 North West Operational Programme (NWOP) thereby supporting the rejuvenation of our commercial and industrial assets, thereby sustaining employment in our key regional centres and creating opportunities the length and breadth of the region.

EG2 and the LCF invested their full £90m allocation to projects across Greater Manchester in accordance with the 2014-20 programme priorities.

The ERDF allocations are governed by a Contingent Loan Agreement (for Evergreen this is an Operational Agreement) between the relevant sub fund and its holding fund. The Contingent Loan Agreement/Operational Agreement sets out a number of obligations in relation to compliance with EU rules, delivery of output targets and monitoring and reporting requirements. All obligations in the Contingent Loan Agreements reflect those imposed on GMCA in its funding agreement and in respect of which the GMCA had minimal scope for negotiation.

By investing debt, Evergreen has created a revolving investment instrument and has levered investment and expertise from a range of public and private sector partners to generate a sizable underlying project portfolio. The successful bidder will be required to assume responsibility for the existing portfolio. There are currently 12 schemes in the portfolio, with c£140m committed. In addition to managing the existing loan book, the adviser will be required to invest new funds in accordance with the recycled investment strategy in the case of EG1 or under the broad parameters of the GM FoF strategy (EG2 / LCF). Copies of these strategies are attached in this note. Note that these documents have been prepared under the umbrella of the wider regional economic strategies for the various key stakeholders.

ERDF Requirements

Most ERDF requirements no longer apply to new investments made by the EG1 Fund, beyond the sector restrictions of urban development, SMEs and energy efficiency; it is essential however that the Fund maintains its targeted approach to investing in Urban Projects, and the principles of ensuring that best value is achieved by outputs will remain. This is tailored to overall GVA and the contribution towards the overarching objectives of the NWOP. In addition, Evergreen will continue to report its original output of floorspace (BREEAM), brownfield land and private/sector investment.

EG2 and the LCF have minimum contracted outputs from DLUHC as follows:

Indicator	Output Target	PA1 - Promoting Research and Innovation	PA4 - Supporting the shift towards a low carbon economy in all sectors
Public or Commercial Buildings built or renovated (sqm)	55,000	55,000	
Productive Investment: Number of enterprises receiving support	5		5

GHG Reduction: Estimated decrease of GHG emissions (000 tonnes)	10	10

For the LCF, the focus will be on greenhouse gas reduction. Progress towards achieving the target for GHG emission reductions will be measured in line with the ERDF Priority Axis 4 Guidance in terms of CO_2 reductions. This will be evidenced through design team calculations and reports, in accordance with the following guidance for the listed project types:

Project Type	**Measure**
Energy efficiency in new and existing (refurbished) buildings	Energy Performance Certificates (EPCs) above that required by Building Regulations, BREEAM Energy scores and calculations using Simplified Building Energy Models (SBEM).
Renewable/ low carbon technology installations	The CO_2 associated with the heat or electricity supply that is being off-set by the installation
District energy networks (supplying any combination of heat, cooling and power)	The difference between: the heat (and where appropriate, electricity) related CO_2 outputs of the proposed network, and the heat (and where appropriate, electricity) counterfactual CO_2 outputs (or the alternative means for meeting heat demand in the absence of the proposed network).

Whilst the Initial Investment Period has now ended, the sub-funds will continue to report on these targets and the sub funds will develop their own business plan for approval by the sub fund Board and Holding Fund Board which may include suggested outputs in addition to the above. The Managing Authority (DLUHC) may, on the basis of the annual reporting, look to reduce funding to the project in the event of significant underperformance so it is therefore imperative we are able to demonstrate continued progress on a regular basis through recycling of funds.

Selection Criteria Which Supports Strategic Investment

Funds will select projects for investment based on a process that incorporates contractual obligations, strategic investment priorities and prudent management of funds. There will be a clear emphasis on selecting projects which contribute to the economic growth of the region with GVA, jobs and development of new commercial floorspace as key priorities.

Basis for Investment

The Funds should not supplant lines of private finance for projects that would otherwise be available. On this basis, each sub-fund will only invest in circumstances where its intervention can enable qualifying projects to proceed (or for delivery to be significantly accelerated) in circumstances where this would not be the case if purely privately financed. In this way, the intention is to leverage the benefits of ERDF investment as far as possible – applying funding which is complementary to private sector senior debt and equity.

Investments

Now that all funds have been fully invested and recycled, there is no longer a requirement to match at project level. The Funds will, however, continue to invest on the basis of a reasonable and prudent level of loan to cost investment in schemes, that is matched to some extent by other sources of capital. It is not envisaged that more than 70% loan to cost investments will be made without express Board approval.

It is proposed that Evergreen Funds will invest by way of senior and mezzanine/subordinated debt products with a tenor of up to five years (an extension to this time period is only possible in exceptional circumstances with the approval of the Board) and the LCF will have tenor up to 15 years. Equity investments will be permissible only with evidence of compliance with state aid and/or Subsidy Control rules. Separate reporting will be required for equity investments.

EVERGREEN STRUCTURE

Please see Figure 1 for the structure of the Financial Instrument.

Evergreen is a Limited Partnership wholly owned by sixteen North West local authorities (the local authorities). The Partnership acts through its General Partner (GP), Northwest Evergreen (GP) Limited (Company Number 07460907). The local authorities are the shareholders of the General Partner and also make up the sixteen Limited Partners. The GP Board of Directors (the Evergreen Board) is made up of three AGMA directors and three County local authority directors.

EVERGREEN 2 AND LOW CARBON FUND STRUCTURE

Please see Figure 2 for the structure of the Financial Instrument.

EG2 and the LCF are also Limited Partnership vehicles but these are owned by the GM FoF, itself a directly owned subsidiary of the GMCA. The GP Board for each of these funds currently comprises 3 GM Directors. There is potential for additional limited partners to come into these funds at a later date but is not currently expected.

For each fund, the GP is responsible for ensuring that the sub fund and its portfolio is always managed and operated by a person authorised to do so under the relevant regulations.

The GP has full discretion to select an Investment Adviser to manage and operate the funds and its portfolio (which includes all investments, money, assets or borrowings for the time being held by or to the order of the sub fund).

Final Recipients

The Investment Adviser should be aware that in respect of the sub funds, final recipients will be predominantly private sector organisations. Public sector final recipients will only be considered, where projects facilitate/enable ultimately private sector led development and job creation.

Investment will not be permitted in project activities that represent a wholly statutory duty on public bodies, nor will investment be permitted where it involves the creation of further financial instruments such as venture capital, loan and guarantee funds. Investment must always finance the development and construction of project assets.

Risk diversification provisions will also need to apply, with single project investments representing a maximum of 20% of the overall investment committed to the fund, and a maximum of 30% of the overall fund investment will be committed to a single counterparty. Requests to vary these provisions will be considered by the sub fund Boards on a case by case basis.

Reutilisation / Winding Up / Exit Strategy

It is intended that project exits will be achieved through either the sale and/or refinancing of project investments, or on maturity and final repayment of investment. The resources paid back to the fund (including capital repayments, income and gains) generated during and until the end of eligibility period can be used for further investments, remuneration of investors and payment of management fees in accordance with applicable EU Regulations. Once Investment Advisers are appointed, an updated business plan will be submitted to the Managing Authority for each sub fund to reflect its recycled investment strategy and utilisation of funds.

Evergreen 1 Investment Strategy

Summary of Evergreen Recycled Investment Strategy

- Priority areas: The 6 priority areas identified in the Evergreen investment strategy will be maintained. These are as follows:
  1. Creating a high employment region
  2. Investing in science, research and innovation
  3. Building on the region's strengths in culture and media
  4. Supporting strong and diverse town centres
  5. Promoting a wider, stronger and more sustainable industrial base
  6. Ensuring sustainable sites are ready for development.

  The continuation of these priorities will ensure that the fund maintains its original identity and focus but will not restrict its flexibility given they are priority areas, rather than requirements, and given the emphasis on jobs, any projects should fit with the first priority of creating a high employment region.
- Evergreen will support eligible Urban Projects that demonstrate a clear fit to the relevant LEP strategy and the underlying objectives of the Northwest Operational Programme. Each Urban Project supported by Evergreen needs to be set within an Integrated Plan for Sustainable Urban Development (IPSUD) to ensure that they contribute to economic growth and regeneration which takes account of wider social, economic and environmental objectives.
- There will be a clear emphasis on selecting projects which contribute to the economic growth of the region with productivity, GVA, jobs and tackling worklessness as key priorities.
- Mixed use schemes, which may include elements of commercial, retail, leisure or residential, will be considered subject to them meeting the objectives of the Northwest Operational Programme and demonstration that they will unlock additional growth, particularly productivity, GVA and jobs as listed above, and investment. Pure residential and retail schemes remain excluded.
- Most ERDF requirements no longer apply to the Fund, Urban Projects must however fall within the following three sectors - urban development, small and medium sized enterprises or for energy efficiency and the use of renewable energy in buildings, including in existing housing.
- Existing governance and investment approval process will remain in place.
- Whilst there is no longer a requirement to match at project level, Evergreen will continue to invest on the basis of a reasonable and prudent level of loan to cost investment in schemes, that is matched to some extent by other sources of capital. It is not envisaged that more than 70% loan to cost investments will be made.
- SA 32835 provides that it shall be a condition of any intervention authorised under the notification that a minimum of 50% of the project's funding is secured through private investments in each project as match the funding to the Evergreen investment.
- The Fund will provide investments at commercial rates in accordance with this Investment Strategy via debt funding, at senior or mezzanine level.
- The Fund will also consider an element of longer term equity funding, where the GVA impact will be appropriate to the investment in comparison to other potential investments at that point in time of the Fund's life cycle. It is expected that equity investment will be utilised alongside Evergreen loan finance.

GM Fund of Funds Investment Strategy – EG2 and LCF

2. Investment strategy

The GM EU Investment Plan strategy and objectives

2.1 The GM EU Investment Plan proposes investment of ESIF resources across six themes:

- Competitive Places
- Science, Innovation and Knowledge Economy
- Competitive Business
- Low Carbon
- Employment and Inclusion
- Supporting Reform

Funding for Evergreen 2 and the Low Carbon Fund have been provisionally allocated as follows in the Investment Plan:

Theme	Evergreen 2 £m	Low Carbon Fund £m
Science, Innovation and Knowledge Economy	30	
Low Carbon	30	30
Total	60	30

2.1.1 Aside from investing across the above themes, a pre-requisite of any projects funded by Evergreen 2 and the Low Carbon Funds is that they demonstrate a clear fit to the English ERDF Operational Programme.

2.1.2 It is intended that through the Fund of Funds, the resources provisionally allocated to Evergreen 2 and the Low Carbon Fund could be re-allocated on the basis of fund performance.

2.2 **Science, Innovation and Knowledge Economy** - GM has identified the following Strategic Priorities in relation to Science, Innovation and Knowledge Economy**:**

- Placing the city region at the leading edge of science and technology
- Improving GM's international competitiveness
- Building a global brand
- Delivering an employer-led skills programme

2.3 **These Strategic Priorities have been translated into the following priority interventions for the Fund of Funds:**

- Develop, retain and exploit excellence in GM‟s science/technology/innovation assets, through investment in the appropriate volume, specification and flexibility of commercial floor-space.

- This will include investment in the development of new sites, the remediation and redevelopment of brownfield and the development/refurbishment of commercial floor-space

2.4 **Low Carbon – GM** has identified the following Strategic Priorities in relation to Low Carbon:

- Seizing the growth potential of a low carbon economy and increased resource efficiency
- Crafting a plan for growth and infrastructure
- Improving connectivity locally, nationally and internationally
- Delivering an employer-led skills programme

2.5 **These Strategic Priorities have been translated into the following priority interventions for the Fund of Funds:**

- Investment to drive the growth of a low carbon economy through capital investment in energy efficiency and generation projects, including heat networks, non-domestic energy efficiency, photovoltaic, wind and hydro energy generation and improved process technologies
- Support to develop GM's whole place low carbon infrastructure to deliver resilient/well adapted places to support the low carbon transition, including energy & waste to energy infrastructure and investment in GM‟s strategic transport network/systems.

2.6 With low carbon investment alongside Urban Development investment in some schemes. This will provide the physical infrastructure and space to meet the needs of the growth in the Economy and high growth businesses in Greater Manchester and fulfil the needs of the Operational Programme and the ESIF Plan. GM's investments will increase innovation in, and adoption of, low carbon technologies.

2.7 The funding context of the Fund of Funds is an important factor to consider. The investment of the ESIF funds via the sub funds into Urban Projects sits alongside existing Greater Manchester funding streams, such as Growing Places funding, and local authority funding mechanisms which may be used where possible by Greater Manchester partners as match funding subject to budget availability.

Figure 1:

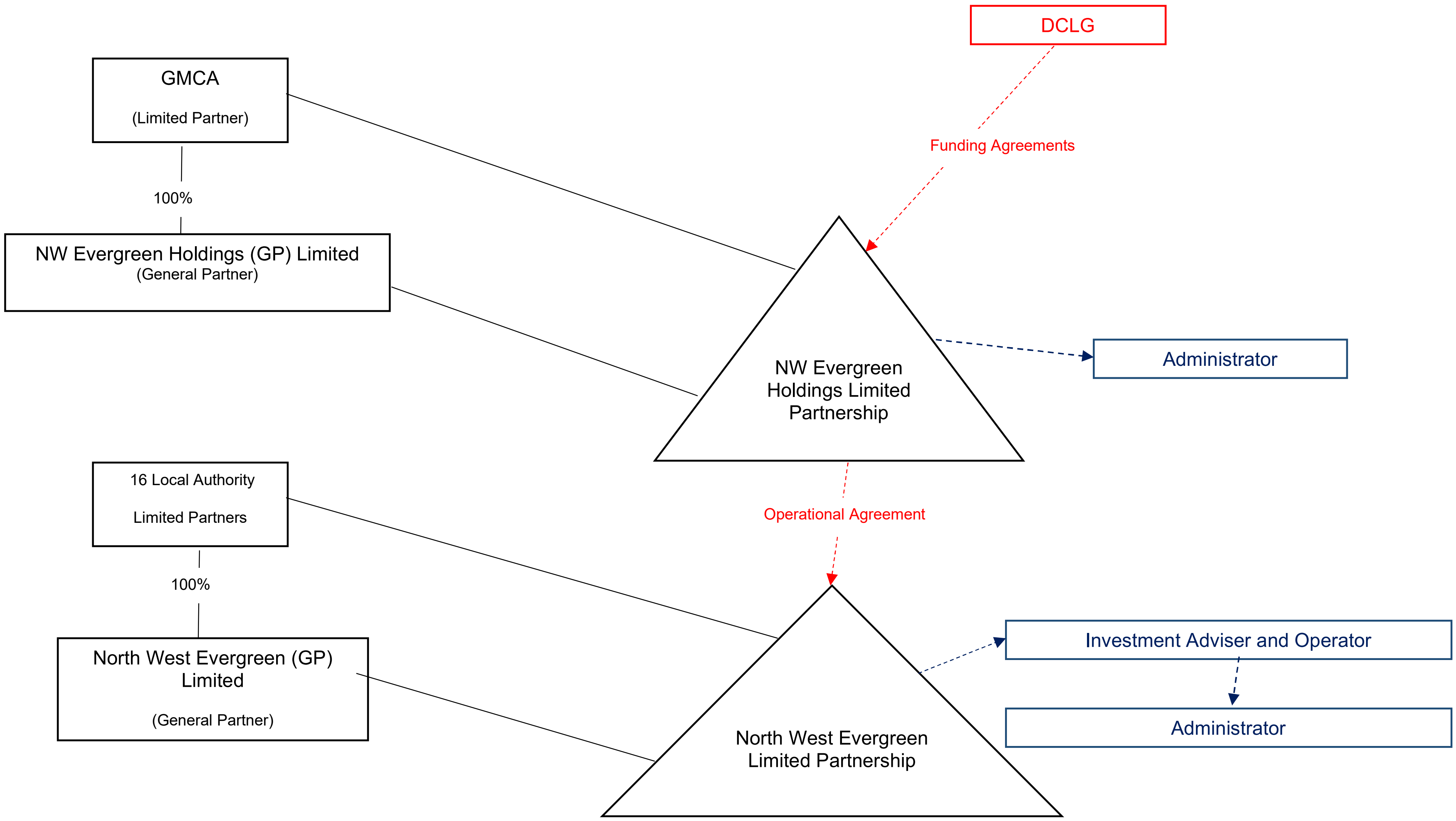
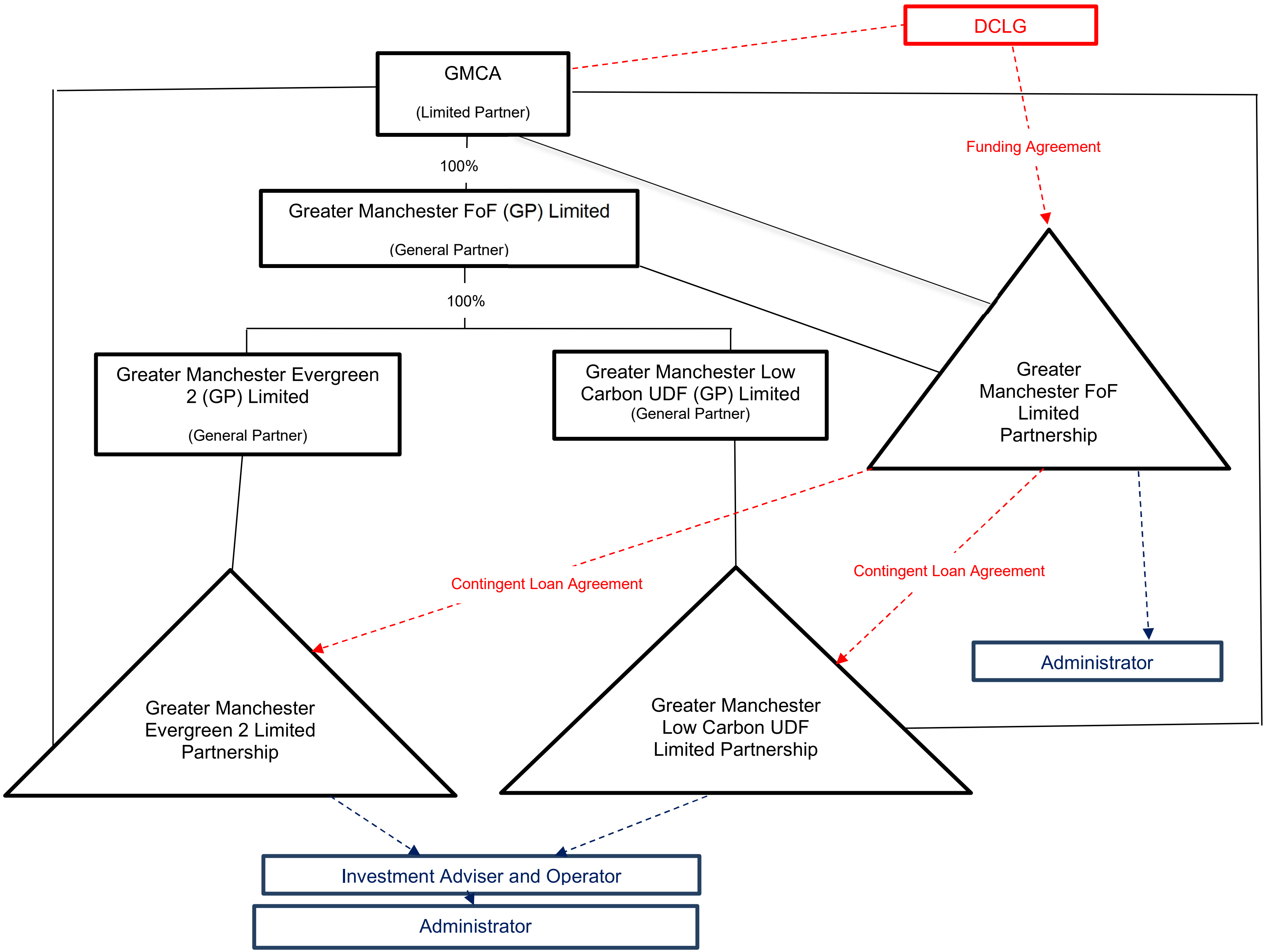

DCLG
Funding Agreements
GMCA
(Limited Partner)
100%
NW Evergreen Holdings (GP) Limited
(General Partner)
NW Evergreen Holdings Limited Partnership
Administrator
Operational Agreement
16 Local Authority
Limited Partners
100%
North West Evergreen (GP) Limited
(General Partner)
North West Evergreen Limited Partnership
Investment Adviser and Operator
Administrator

Figure 2:



DCLG
GMCA
(Limited Partner)
100%
Greater Manchester FoF (GP) Limited
(General Partner)
100%
Funding Agreement
Greater Manchester Evergreen 2 (GP) Limited
(General Partner)
Greater Manchester Low Carbon UDF (GP) Limited
(General Partner)
Greater Manchester FoF Limited Partnership
Contingent Loan Agreement
Contingent Loan Agreement
Greater Manchester Evergreen 2 Limited Partnership
Greater Manchester Low Carbon UDF Limited Partnership
Administrator
Investment Adviser and Operator
Administrator