

## **Cabinet**

**15 June 2016**

### **Option to Create a Durham County Council Investment Fund – ‘Finance Durham’**



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#### **Report of Corporate Management Team**

**Ian Thompson, Corporate Director Regeneration and Economic Director**

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**Councillor Neil Foster, Cabinet Portfolio Holder for Regeneration and Economic Development**

**Councillor Alan Napier, Cabinet Portfolio Holder for Finance**

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#### **Purpose of the Report**

- 1 To seek agreement to the creation of an Investment Fund to help deliver business growth and job creation. The fund would be financed by the Council and operated on a commercial basis and as such it is intended to generate a financial return over the longer term.

#### **Background**

- 2 Within the context of continuing austerity and unprecedented cuts to local government funding, the Council no longer offers grants to businesses and indeed this has been the case for several years. However, within Economic Development, Business Durham exists to ensure strong focus on the business sector, including supporting existing businesses to establish and grow whilst ensuring new businesses seek to locate within County Durham.
- 3 In terms of attractiveness to business, County Durham presents many opportunities to companies that are either already based here or are considering County Durham as a potential location. However, in an increasingly competitive market, there is the opportunity to add to the attractiveness of the County as a business location in a way that is aligned with the Council's core objectives.
- 4 Several other areas of the country have in the last few years seen the creation of investment funds that are capable of supporting local economic development through direct investment in local businesses in a manner that is commercially attractive. In many circumstances these investment funds have been developed by Councils, using public money as an enabling tool.

- 5 Up until now, the North East and County Durham has had limited market success in providing access to finance to facilitate business growth. Opportunities have tended to be based on ad hoc tactical opportunities rather than through a more proactive strategic approach.

### **Current Position**

- 6 Within the last two years in County Durham, the Council has made equity investments in two businesses rather than offering grants. This means that the Council is partnered with and thus, has greater interest in the investee company and will hopefully make a financial return. Whilst businesses will always accept grants, as they equate to free money in reality they want help and investment and access to finance that will support their businesses to grow. Investments in businesses are more sustainable in the longer term for both parties and the economy as a whole. They also avoid any concerns over questions of State Aid as they are commercial arrangements.
- 7 Whilst much reduced than in previous years, there are still some grant products available in the North East as can be seen in the North East Local Enterprise Partnership (NELEP) Business Growth Hub. Government previously funded grant schemes via Regional Growth Fund (RGF) for large projects and the Lets Grow (RGF funded scheme) for smaller projects, specific to the North East. These are no longer available.
- 8 In addition to bank funding, County Durham businesses can access a range of other sources of finance e.g. North East Finance (JEREMIE) funds, invoice discounting financing, cloud (crowd funding) finance and venture capital/private equity. None of which are County Durham exclusive and all have differing limitations.
- 9 Based on Business Durham's engagement with business, evidence shows that businesses are happy to receive finance as an investment as part of a wider package, especially from a Local Authority as it demonstrates a degree of partnership working. Therefore, this proposal is not for a grant fund but for a self-sustaining Investment Fund.

### **Fund Structure**

- 10 A small working group comprising representatives of Corporate Finance, Legal Services, Regeneration and Economic Development, with advice from the Finance Director of North East Finance and a specialist Financial Conduct Authority (FCA) approved company Finance Tree have developed a fund proposal and a set of operating parameters as shown in table 1.

**Table 1 Proposed Finance Durham Fund Parameters**

<b>Size of Fund:</b>	<b>£ 20million</b> initial capital
<b>Name of Fund</b>	Finance Durham
<b>Additional co-invest</b>	Fund management targeted with attracting a similar level of co-investment from other sources
<b>Legal structure</b>	The Council will create a new Limited company and a Limited Partnership
<b>Life of Fund</b>	Unlimited in duration (known in the industry as “Evergreen”) although the modelling has been completed over a 10 year life cycle by way of illustration.
<b>Fund Management</b>	Creation of company, as the new fund management firm. Initially appoint external FCA authorised third party Fund Management business to set up the Fund and build Finance Durham
<b>Investment Strategy</b>	<b>Equity and Loan</b> targeting <b>early-stage to growth businesses</b> in County Durham area. Venture Capital style investments with capital gain the target. Investment will include an Incubation Fund of circa £2million (very early stage investments in companies developing new business ventures, small amounts invested for equity)
<b>Aims and Objective</b>	<b>Economic development focus</b> with emphasis on development and growth of <b>High-Growth Small Businesses (HGSB)</b>
<b>Small Medium Enterprises (SME’s) assisted</b>	Fund target will be to assist at least <b>500 SMEs</b>
<b>Jobs target</b>	<b>Impact 2000 jobs;</b> made up of <b>1250 jobs created</b> , 750 jobs preserved
<b>Non-EU funds</b>	Investment will not duplicate EU JEREMIE funds, however it may be utilised to replace JEREMIE funding when its term has expired.
<b>Investment Period</b>	<b>5 years extendable</b> on average
<b>Amounts invested</b>	<b>£400,000 average.</b> Individual investments are likely to vary between £200,000 to £2million other than the Incubation Fund
<b>Max single investment</b>	<b>£2million maximum:</b> unless into sub-funds (Tier 2)
<b>Sub-funds*</b>	Ability to create, cornerstone and invest in special sub-funds (Tier 2) or act as a Limited Partner in external locally focused funds with external investors
<b>Geographic restrictions</b>	To be ring fenced for County Durham businesses.
<b>Sector Focus</b>	No specific sector restrictions
<b>Investment profile</b>	<b>40 to 70</b> individual businesses over 10-year model
<b>Fees</b>	The appointed Fund Manager costs are expected to be <b>3.5%</b> of the fund size for years 1 – 5 reducing to 1.75% of fund size for years 6 -10. Arrangement and monitoring fees will be charged to the companies invested in which will reduce the fund management costs
<b>Business support</b>	Fees above to include delivery of support programme for SMEs

\*The Finance Durham structure has the flexibility to develop sub-funds. These would attract additional monies to target specific sectors, or develop new financial instruments. By way of illustration and example; Finance Durham invests £1 million along with two other parties to help digital firms creating a sub fund of £3 million but only costing the Finance Durham fund £1 million. These sub-funds would be aligned with the investment policy and contribute to the economic development and financial returns of the Finance Durham fund.

### **Economic Development Impact**

- 11 The fund has been designed with growing the County economy as its core function. The modelling has suggested that the fund will support 500 companies, making investments in about 70 companies over the first ten years, creating and safeguarding about 2,000 jobs. In the context of growing the economy of County Durham, these outputs are considerable and they also deliver increased reputation for Durham as a place to do business where the local authority is committed to economic growth.
- 12 The fund will be targeted at high growth businesses, which are businesses that will have the potential for significant growth in terms of turnover, profitability and job creation over a short period of time. Specific parameters will be developed in conjunction with the procured fund manager and will vary based on sector or technology. These types of businesses have been chosen as the preferred target because there is the potential for greatest financial return and economic development impact. In addition there is a clear market gap for investments in these types of businesses.
- 13 In addition, the benefits to business will be greater than just those receiving investment because they are supported through an investment journey by the fund manager before an investment is made. Businesses supported but not receiving investment may secure investment from elsewhere or fund growth in other methods, but they still benefit from the expertise of the fund manager.
- 14 A key responsibility of the fund manager will be to support the delivery of a stronger access to finance community in the County and spread the message about business finance. The fund manager will also deliver support to increase the capabilities and skills needed to raise and use finance beyond the remit of the Finance Durham fund.

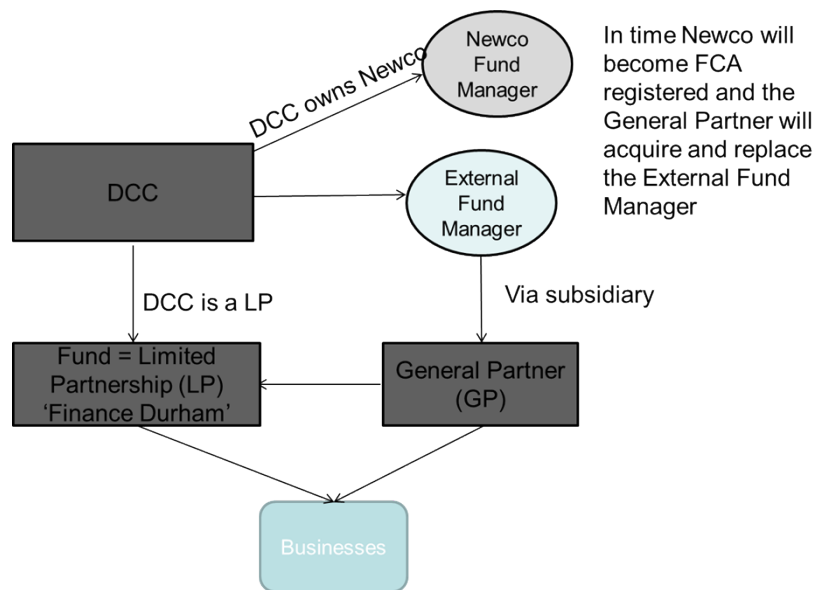
### **Fund Structure, Legal Arrangements and Governance**

- 15 The Fund structure will be a standard and well recognised venture capital approach of a limited partnership with a fund manager acting as a general partner. This structure is tax transparent and therefore efficient, i.e. tax is treated as it ordinarily would by the parties who form the partnership. This structure is also flexible and enables other investors to be added or new

sub funds to be created. Figure 1 provides an overview of the structure proposed.

- 16 In order to get the fund operating as quickly as possible, a FCA regulated fund manager will be procured, initially for three years. This fund manager will help set up and operate Finance Durham to enable investments in businesses and in parallel help set up a Council owned Newco Fund Management Company which is FCA approved. This flexibility enables the Council to secure maximum flexibility for the future.

**Figure 1. Legal Structure Proposed for Finance Durham**



- 17 In order for the fund to be a commercial success it is essential that the fund manager is authorised to make investment decisions consistent with the policies approved by the new company. Council officers and members will not be directly involved in those investment decisions as is the case with investments made by Pension Fund Managers. Their involvement will be limited to setting the parameters within which the fund manager is expected to work.
- 18 It is a legal requirement of the FCA that fund managers' report to their funders on the status of the funds under management every six months. The nature and details of these reports can be defined by the Council in conjunction with the fund manager upon formation of the fund.

## Finance

- 19 The Council alongside Finance Tree have produced a ten year financial model for Finance Durham based upon a range of assumptions. A business plan can be seen in appendix 2 for the creation of the Finance Durham. Although the intention would be for the investment fund to be 'Evergreen, a ten year model provides an indication of the forecast fund value at the end of year ten. It must be recognised that investments of the

nature detailed come with an element of risk. On that basis prudent assumptions have been made regarding the number of the investments that will fail. At the same time however those that are successful should result in strong equity returns and high levels of interest repayment in relation to loans, offsetting the losses from the investments that fail. The expectation is that the fund will make equity and debt investments into high growth businesses.

20 The assumptions utilised in developing the financial model are as follows. In all circumstances the assumptions are prudent.

- (i) **Maximum Investment Size** - £2million
- (ii) **Investment Type** – although the investment type will need to be flexible dependent upon individual company circumstance it is expected that investment will be weighted towards either pure equity or preference share investment as detailed below:

	£million
Equity Investment	10.0
Preference Shares	7.0
Loans	3.0
<b>TOTAL INVESTMENT</b>	<b>20.0</b>

- (iii) **Loan Interest Rate** – assumed to be 9%
- (iv) **Preference Share Dividend** – 6.5%
- (v) **Fund Manager Fees** – across the ten year period the fund manager fees (3.5% for years 1 – 5 and 1.75% for years 6 – 10) are forecast to be £5.2million. Set up costs of £0.14 million are also planned. The model also assumes the contract for the Fund Manager will also include incentive bonuses based upon performance – the sum assumed over the ten year period is £0.38million
- (vi) **Arrangement / Monitoring Fees** – across the ten years it is forecast that companies will be required to pay £1.88 million and these will partially finance the fund manager fees.
- (vii) **Investment Failure Rates** – It is prudent in terms of financial modelling to assume high levels of investment failure due to the nature of the investment type. The following levels of investment failure/non repayment of loan have been assumed.

	<b>Failure Rate</b>
	%
Equity	45
Preference Share	50
Loans	40

- (viii) **Increase in Equity Value** – it is forecast that a number of the equity investments will result in significant ‘capital’ growth. This will vary but the average growth return is forecast to be 2.5 times the initial investment, which is prudent when compared to experience elsewhere.
- (ix) **Return to the Council** – to recompense the Council for the loss of investment income on the £20 million invested it is intended that a small return would be made from the Investment Fund to the Council on an annual basis from the loan interest generated by the fund. Over the ten year period this sum will total £0.55 million and is expected to be paid in the form of a dividend.

21 Based upon the assumptions detailed above the value of the initial £20 million investment is forecast to have grown by year ten to £25.5 million. The expectation would be that the fund will be ‘evergreen’ and will continue to be invested in line with the original objectives i.e. job creation and job protection. Notwithstanding this desire the Council could still choose to sell all investments at some point to realise this full £25.5 million value. The table below summarises the forecast fund position at the end of year ten.

<b>INCOME</b>	£million
Capital Gains	16.6
Investment Income	2.2
Arrangement/Monitoring Fees	1.9
<b>TOTAL INCOME</b>	<b>20.7</b>
<b>LESS EXPENDITURE:</b>	
Bad Debts/Losses	8.9
Fund Manager Fees	5.7
Council Financial Return	0.6
<b>TOTAL EXPENDITURE</b>	<b>15.2</b>
<b>INCREASE IN FUND VALUE</b>	<b>5.5</b>

22 All of the transactions detailed above will be accounted for in the new company structure. In terms of Council investment this will amount to £20 million of capital investment which the Fund Management Company will invest into County Durham companies. Based upon cash flow modelling the £20 million of capital investment will occur over a five year period as detailed below. For financing purposes the first year of investment is forecast to be 2017/18.

<b>Year</b>	<b>£million</b>
2017/18	4.15
2018/19	4.87
2019/20	4.33
2020/21	3.68

2021/22	2.97
<b>TOTAL INVESTMENT</b>	<b>20.00</b>

- 23 Additional financial analysis is provided in Appendices 3, 4 and 5 as detailed below. The financial information provided in the Appendices relates to the Fund Management Company.
- (i) Appendix 3 – Ten year Income and Expenditure forecast
  - (ii) Appendix 4 – Ten year cash flow forecast
  - (iii) Appendix 5 – Balance Sheet forecast
- 24 Although the Council could ‘realise’ the £20 million investment at some point in the future it is prudent for the Council to plan to finance the full £20 million in terms of capital planning. In relation to 2017/18, Council agreed the capital budget for this year at Council on 24 February 2016. The additional funding required to fund the investments forecast in 2017/18 under this proposal was not included in the budget and therefore there will be a need to increase the capital budgets. In terms of 2018/19 and beyond it is recommended that the sums required are included as a ‘pre commitment’ against available capital resources in those years.
- 25 For 2017/18 it is recommended that the additional funding required is achieved by increasing the capital receipts target for that year from £17.9 million to £22.05 million i.e. by the required £4.15 million. The Asset Disposal programme for 2016/17 at this stage is forecast to over achieve against the set target by over the required £4.15 million.

### **Implementation and Time Scales**

- 26 The procurement of the fund manager can commence straight away with a view to getting the fund launched for the start of 2017. An implementation plan is in place.
- 27 Finance Tree Limited have assessed the viability of the model and produced a business plan for the new company.
- 28 The next step, subject to approval of this report, will be to form the company and limited partnership and procure the services of a Fund Manager.

### **Recommendations and Reasons**

- 29 Cabinet is recommended to:
- (a) Approve the principle of creating a Durham County Council investment fund to be known as Finance Durham;



- (b) Agree that a new limited company and limited partnership be formed to implement creation of Finance Durham;
- (c) Agree that capital funding of £20 million be made available to Finance Durham to be financed £4.15 million from capital receipts in 2017/18.
- (d) Authorise the Corporate Directors of Regeneration and Economic Development and Resources, in consultation with their respective portfolio holders, to take all necessary steps to implement these decision;
- (e) Note that annual progress reports be submitted to Cabinet after the fund has commenced operation.

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## **Appendix 1: Implications**

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### **Finance –**

Finance Durham will invest £20m in County Durham based businesses. It is forecast that the investments will be valued at £25.5m after ten years. In 2017/18 the forecast expenditure on investments of £4.15m will be financed by increasing the capital receipts income target for that year, with capital budgets being adjusted accordingly. From 2018/19 onwards the investment in Finance Durham will be treated as a pre commitment against available capital resources.

### **Staffing –**

The Fund Manager will engage his own staff and no secondment of Council staff is envisaged.

### **Risk –**

There is a risk of failure in relation to the investments made. A forecast level of investment failure is detailed in the report ranging from 40% to 50% based upon investment type. It is forecast that the gains on investments made will outweigh the losses.

### **Equality and Diversity / Public Sector Equality Duty –**

None.

### **Accommodation –**

None.

### **Crime and Disorder –**

None.

### **Human Rights –**

None.

### **Consultation –**

None at this stage.

### **Procurement –**

Procurement procedures will be followed to select a Fund manager.

### **Disability Issues –**

None.

### **Legal Implications –**

Legal structure and Governance issues are considered in the report. The Fund must be established in such a manner as not to give individual businesses support in a manner which could be classed as unlawful State Aid capable of distorting competition in the market. The Council has the power under the general power of competence in the Localism Act 2011 to embark on this venture through a limited company.

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## **Appendix 2 - Finance Durham Business Plan**

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### **Executive Summary**

There is an opportunity for Durham County Council (DCC) to support the growth of the economy, creating jobs, attracting businesses and helping businesses to grow by providing finance in the form of a venture capital loan fund (VCLF). The VCLF will be operated by a Financial Conduct Authority (FCA) regulated company and be a standalone, arm's length operation. Modelling has suggested that DCC should commit £20 million for investment in high growth businesses within County Durham. Successful venture capital investing also acts as a magnet that attracts additional financial and management skills as well as supporting a local entrepreneurial culture which retains and stimulates indigenous entrepreneurial talent, a higher level of professional advisers and raises the profile of an area.

The fund should be an evergreen fund and be targeted at businesses of all sizes and sectors based in County Durham. Based on a 10 year modelling period, five years for investment and five years for managing out the portfolio, the fund should make circa 70 investments, support 500 businesses, create and safeguard 2,000 jobs and yield a return of circa £6,000,000 after 10 years.

In order to establish a VCLF for Durham external advice from venture capital consultancy experts, Finance Tree Limited and specialist legal, tax and regulatory advice from the City firm RW Blears LLP was taken regarding the structural options available and building a case for the fund.

### **The demand for a fund**

The most comprehensive research undertaken with regard to publicly backed Financial Instruments is the work completed by Regeneris in advance of JEREMIE 2. Looking at the North East, Regeneris identify a substantial finance gap with indicative estimates on the scale of unmet demand of £560,000,000 per annum over and above what private and public backed providers already provide. This figure does not take into account the number of businesses with viable business plans however, Regeneris go on to illustrate the potential scale of the issue in the region by proposing that if 10% of the business propositions were viable this would imply a finance gap of £2,000,000 for microfinance and around £60,000,000 for larger amounts of finance over and above that which is being addressed by JEREMIE funds and other public sector backed initiatives.

Whilst there is a demand for funding in Durham it does require stimulating further and in part the establishment of Finance Durham will support this. In addition it is important the fund manager delivering Finance Durham has the capability to market the fund and to deliver a range of support services to help upskill and inform Durham's business regarding access to finance issues.

The proposed fund will sit alongside and complement existing provision within Durham, delivered by the private sector or publically backed funds, e.g. JEREMIE2.

## **The Fund Structure**

The fund will be established as an industry standard VCLF limited partnership. The partnership will be between two limited partners (LP): DCC and a FCA regulated fund manager (FM). The FM will take on the role of general partner (GP) via a newly created subsidiary company in order to set up and deliver the fund. There are two approaches that could be taken to secure a FCA regulated FM:

1. To procure an existing company to become the GP.
2. From the beginning create a Newco, secure FCA regulation and then launch the fund. Securing FCA regulation will take about 36 months.

The aim is to establish the fund by early 2017 and therefore the procurement of an external FM is to be progressed to achieve this time frame. Over time and in order to achieve the ambition of creating a legacy of a financial institution for Durham the intention is to create a DCC wholly owned new company (Newco) that will become FCA regulated and replace the FM as the GP in the Finance Durham LP. The procured FM will be responsible for establishing this new company with DCC officers.

Procurement of a FM will be via an invite to negotiate procurement procedure and will take about 5 months to complete.

Draft legal documents, namely management and partnership agreements are in place to facilitate the establishment of Finance Durham.

## **Operational Requirements of Finance Durham**

The key factors determining the staff costs and necessary back office are:

- Regulatory Compliance (FCA set-up, monitoring, reporting and training)
- Board and Director level oversight necessary to cover all functions
- Marketing to generate deal-flow and cover investor relations
- Assessment, due-diligence, investment management and decisions
- Monitoring and reporting.
- Delivering wider access to finance business support activities

The greatest expertise needed within a fund team is the management and growth of portfolio businesses and the whole exit process. This last part includes links to and knowledge of the investment and wider business and market/financial community. For these reasons the human resources proposed for the FM team are:

- 2 Directors at least 3 at full time operational level
- 1 Finance Director
- 2 Fund Management staff (this may include a Loans Manager)
- 1 Marketing and client relations manager

- 1 Assistant (covering legal, finance, office management, etc.)
- 1 office secretary

In the first instance these will be procured as part of the FM activity and will need to be established in the Newco as it is established. The specific details will be finalised once the procured FM is place.

An indicative time line to set up Finance Durham, following procurement of an FM and to establish Newco in as low cost manner possible is indicated below in figure 1.

**Figure 1. Finance Durham 3 year set up timetable**

Finance Durham Fund		CONFIDENTIAL											
Setup & Launch		Year 1				Year 2				Year 3			
2016-17		2017-18				2018-19				2019-20			
Q3 Q4		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Directors x2		<b>1. Setup Phase:</b> Independent external FM builds fund (full team)											
Finance Dir													
Fund Manager 1													
Fund Manager2													
Assistant													
Compliance Func													
Marketing Func													
Accounts													
Legal													
Abort fees													
Audit		<b>2. Investment Phase:</b> FM ensures marketing, deal-flow and investments made											
IT													
Accommodation													
Plan													
Systems													
Documentation													
FCA application													
Legal advice													
Recruitment													
Fund Manager 1													
Assistant 1													
Compliance													
Accounts													
		<b>4. FCA application:</b> in parallel with normal operation FM writes and submits FCA application, begins recruitment and systems in place											
		<b>5. Parallel running of Newco and FM: Setup Phase:</b> FM have to remain in control but new team starts to take over in Newco											
		<b>6. Final handover:</b> with FCA for Newco in place final handover at direction of FM senior team. Audit of fund and compliance in Newco											

**Budget to Operate Finance Durham and set up Newco**

Over the first three years of operation the indicative total cost for setting up Finance Durham via a procured FM and establishing Newco is £2,229,600. The first three year break down detail to this business case is summarised in table 1 below.

**Table 1. Summary of first three years FM costs**

Organisation and Cost	Set up and Launch 2016/2017	Year 1	Year 2	Year 3
Fund Manager	£125,000	£604,000	£581,250	£495,000
Newco	£10,000	£94,200	£116,950	£203,200
<b>Total</b>	<b>£135,000</b>	<b>£698,200</b>	<b>£698,200</b>	<b>£698,200</b>

These costs will be included as part of the £20,000,000 fund and not subject to additional budget.

### **Fund Parameters**

The Finance Durham fund parameters are presented below:

- Maximum Investment Size £2 million.
- Typical investment size £200,000 to £700,000.
- Investment Type – although the investment type will need to be flexible dependent upon individual company circumstance it is expected that investment will be weighted towards either pure equity or preference share investment based on the following ratios: Equity (50%), preference shares (35%) and loans (15%).
- Loan Interest Rate has been assumed to be 9%.
- Preference Share Dividend has been assumed to be 6.5%.
- Fund Manager Fees across the ten year period the fund manager fees (3.5% for years 1 – 5 and 1.75% for years 6 – 10) are forecast to be £5,200,000. Set up costs of £135,000 are also planned. The model also assumes the contract for the Fund Manager will also include incentive bonuses based upon performance – the sum assumed over the ten year period is £380,000.
- Arrangement / Monitoring Fees across the ten years it is forecast that companies will be required to pay £1,880,000 and these will partially finance the fund manager fees.
- Investment Failure Rates – It is prudent in terms of financial modelling to assume high levels of investment failure due to the nature of the investment type. The levels of investment failure/non repayment of loan have been modelled as: Equity (45%), preference share (50%) and loans (40%).
- Increase in Equity Value it is forecast that a number of the equity investments will result in significant ‘capital’ growth. This will vary but the average growth return is forecast to be 2.5 times the initial investment.
- Return to Funder (DCC) to recompense DCC for the loss of investment income on the £20million invested it is intended that a small return would be made from the Investment Fund to DCC on an annual basis from the loan interest generated by the fund. Over the ten year period this sum will total £550,000 and is expected to be paid in the form of a dividend.

The overall Finance Durham fund budget over the 10 year period is presented in table 2 below.

**Table 2. Overall 10 year budget for Finance Durham**

<b>INCOME</b>	<b>£million</b>
Capital Gains	16.6
Investment Income	2.2
Arrangement/Monitoring Fees	1.9
<b>TOTAL INCOME</b>	<b>20.7</b>
<b>LESS EXPENDITURE:</b>	
Bad Debts	8.9
Fund Manager Fees	5.7
Council Financial Return	0.6
<b>TOTAL EXPENDITURE</b>	<b>15.2</b>
<b>INCREASE IN FUND VALUE</b>	<b>5.5</b>

The investments targeted by the fund will be targeted a high growth businesses, irrespective of size or sector and in the range of £200,000 to £700,000. There will be 10% of the fund allocated to an incubator fund that will support businesses to prove concepts and as such become the next generation of high growth businesses in Durham.

### **Risks**

Finance Durham will be a commercially operated fund aimed at providing risk capital and as such there is a risk that DCC could lose the original investment. However, this is mitigated by the model and approach being developed and the use of a FCA regulated, experienced and qualified FM. The financial modelling has a conservative default rate and still demonstrates that the fund can make money.

The major other risk is that a FM cannot be procured. This is highly unlikely given the nature of the market in the NE and the competitive nature of how the fund has been developed.

## Appendix 3 - Finance Durham Investment Fund

### Income & Expenditure Account

	Year 1 £	Year 2 £	Year 3 £	Year 4 £	Year 5 £	Year 6 £	Year 7 £	Year 8 £	Year 9 £	Year 10 £	Total £
<b>Income</b>											
Investment Income	22,637	122,470	245,701	345,065	410,514	417,663	309,633	194,131	110,577	58,718	2,237,109
Capital Gains	(71,094)	(64,531)	43,750	173,906	337,969	2,881,176	3,582,680	3,452,524	3,320,180	2,976,640	16,633,200
Arrangement Fees	94,250	123,250	123,250	123,250	116,000	0	0	0	0	0	580,000
Monitoring Fees	35,100	81,000	126,900	172,800	216,000	216,000	180,900	135,000	89,100	43,200	1,296,000
Deposit Interest	0	0	0	0	0	0	0	0	0	0	0
<b>Income Total</b>	<b>80,893</b>	<b>262,189</b>	<b>539,601</b>	<b>815,022</b>	<b>1,080,483</b>	<b>3,514,840</b>	<b>4,073,213</b>	<b>3,781,654</b>	<b>3,519,857</b>	<b>3,078,558</b>	<b>20,746,309</b>
<b>Expenditure</b>											
Bad Debts	361,563	1,051,313	1,446,250	1,729,938	1,841,188	1,373,938	645,250	361,563	89,000	0	8,900,000
DCC-Treasury Management Return	0	50,000	100,000	100,000	100,000	100,000	50,000	50,000	0	0	550,000
Arrangement & Monitoring costs	0	0	0	0	0	0	0	0	0	0	0
Fund Manager Bonus	(969)	1,159	5,789	10,379	14,970	65,977	77,846	72,933	68,615	60,707	377,406
Start-up cost	135,000										135,000
Annual Administration cost	698,200	698,200	698,200	698,200	698,200	349,100	349,100	349,100	349,100	349,100	5,236,500
Disallowed VAT	0	0	0	0	0	0	0	0	0	0	0
<b>Expenditure Total</b>	<b>1,193,793</b>	<b>1,800,671</b>	<b>2,250,239</b>	<b>2,538,517</b>	<b>2,654,357</b>	<b>1,889,014</b>	<b>1,122,196</b>	<b>833,596</b>	<b>506,715</b>	<b>409,807</b>	<b>15,198,906</b>
<b>Surplus / Deficit</b>	<b>(1,112,900)</b>	<b>(1,538,482)</b>	<b>(1,710,638)</b>	<b>(1,723,495)</b>	<b>(1,573,874)</b>	<b>1,625,825</b>	<b>2,951,017</b>	<b>2,948,059</b>	<b>3,013,142</b>	<b>2,668,750</b>	<b>5,547,403</b>



## Appendix 4 - Finance Durham Investment Fund

### Cash Flow

	Year 1 £	Year 2 £	Year 3 £	Year 4 £	Year 5 £	Year 6 £	Year 7 £	Year 8 £	Year 9 £	Year 10 £	Total £
<b>Inflow</b>											
Durham Fund	4,144,494	4,869,949	4,334,849	3,677,991	2,972,717						20,000,000
Arrangement & monitoring fees	129,350	204,250	250,150	296,050	332,000	216,000	180,900	135,000	89,100	43,200	1,876,000
Repayments & Redemptions	(142,188)	(133,938)	173,750	555,188	1,023,938	2,201,938	2,390,500	2,009,063	1,621,750	1,100,000	10,800,000
Investment Income	22,637	122,470	245,701	345,065	410,514	417,663	309,633	194,131	110,577	58,718	2,237,109
Capital Gains	(71,094)	(64,531)	43,750	173,906	337,969	2,881,176	3,582,680	3,452,524	3,320,180	2,976,640	16,633,200
Deposit interest	0	0	0	0	0	0	0	0	0	0	0
<b>Inflow Total</b>	<b>4,083,200</b>	<b>4,998,200</b>	<b>5,048,200</b>	<b>5,048,200</b>	<b>5,077,138</b>	<b>5,716,777</b>	<b>6,463,713</b>	<b>5,790,717</b>	<b>5,141,607</b>	<b>4,178,558</b>	<b>51,546,309</b>
<b>Outflow</b>											
Advances	3,250,000	4,250,000	4,250,000	4,250,000	4,000,000	0	0	0	0	0	20,000,000
DCC-Treasury Management Return	0	50,000	100,000	100,000	100,000	100,000	50,000	50,000	0	0	550,000
Arrangement & Monitoring costs	0	0	0	0	0	0	0	0	0	0	0
Fund Manager Bonus						31,328				285,371	316,699
Operating costs (inc VAT)	833,200	698,200	698,200	698,200	698,200	349,100	349,100	349,100	349,100	349,100	5,371,500
Corporation Tax	0	0	0	0	0	0	0	0	0	0	0
<b>Outflow Total</b>	<b>4,083,200</b>	<b>4,998,200</b>	<b>5,048,200</b>	<b>5,048,200</b>	<b>4,798,200</b>	<b>480,428</b>	<b>399,100</b>	<b>399,100</b>	<b>349,100</b>	<b>634,471</b>	<b>26,238,199</b>
<b>Net Inflow/ Outflow</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>278,938</b>	<b>5,236,349</b>	<b>6,064,613</b>	<b>5,391,617</b>	<b>4,792,507</b>	<b>3,544,086</b>	<b>25,308,110</b>
<b>Balance brought Forward</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>278,938</b>	<b>5,515,287</b>	<b>11,579,900</b>	<b>16,971,517</b>	<b>21,764,024</b>	<b>0</b>
<b>Balance Carried Forward</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>278,938</b>	<b>5,515,287</b>	<b>11,579,900</b>	<b>16,971,517</b>	<b>21,764,024</b>	<b>25,308,110</b>	<b>25,308,110</b>

## Appendix 5 - Finance Durham Investment Fund

### Balance Sheet

	Year 1 £	Year 2 £	Year 3 £	Year 4 £	Year 5 £	Year 6 £	Year 7 £	Year 8 £	Year 9 £	Year 10 £
<b>Investments</b>										
Loans	450,938	987,000	1,392,000	1,647,188	1,713,000	1,191,188	744,188	447,000	300,000	300,000
Redeemable Preference Shares	1,137,500	2,340,625	3,171,875	3,631,250	3,631,250	2,165,625	1,071,875	350,000	0	0
Equity	1,442,188	3,035,625	4,429,375	5,679,688	6,748,750	5,160,313	3,665,313	2,313,750	1,100,000	0
<b>Investments Total</b>	<b>3,030,625</b>	<b>6,363,250</b>	<b>8,993,250</b>	<b>10,958,125</b>	<b>12,093,000</b>	<b>8,517,125</b>	<b>5,481,375</b>	<b>3,110,750</b>	<b>1,400,000</b>	<b>300,000</b>
<b>Current Assets</b>										
Bank	0	0	0	0	278,938	5,515,287	11,579,900	16,971,517	21,764,024	25,308,110
Deposit Interest	0	0	0	0	0	0	0	0	0	0
<b>Current Assets Total</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>278,938</b>	<b>5,515,287</b>	<b>11,579,900</b>	<b>16,971,517</b>	<b>21,764,024</b>	<b>25,308,110</b>
<b>Current Liabilities</b>										
Fund manager Bonus	(969)	190	5,979	16,358	31,328	65,977	143,823	216,756	285,371	60,707
Corporation tax	0	0	0	0	0	0	0	0	0	0
<b>Current Liabilities Total</b>	<b>(969)</b>	<b>190</b>	<b>5,979</b>	<b>16,358</b>	<b>31,328</b>	<b>65,977</b>	<b>143,823</b>	<b>216,756</b>	<b>285,371</b>	<b>60,707</b>
<b>Net Assets</b>	<b>3,031,594</b>	<b>6,363,060</b>	<b>8,987,271</b>	<b>10,941,767</b>	<b>12,340,610</b>	<b>13,966,435</b>	<b>16,917,452</b>	<b>19,865,511</b>	<b>22,878,652</b>	<b>25,547,403</b>
<b>Capital &amp; Reserves</b>										
Durham	4,144,494	9,014,443	13,349,292	17,027,283	20,000,000	20,000,000	20,000,000	20,000,000	20,000,000	20,000,000
Income & Expenditure Account	(1,112,900)	(2,651,382)	(4,362,021)	(6,085,516)	(7,659,390)	(6,033,565)	(3,082,548)	(134,489)	2,878,652	5,547,403
<b>Capital &amp; Reserves Total</b>	<b>3,031,594</b>	<b>6,363,060</b>	<b>8,987,271</b>	<b>10,941,767</b>	<b>12,340,610</b>	<b>13,966,435</b>	<b>16,917,452</b>	<b>19,865,511</b>	<b>22,878,652</b>	<b>25,547,403</b>