

# MIDDLESBROUGH COUNCIL

## EXECUTIVE REPORT

### DigitalCity Business 2010/11 – 2011/12 Business Plan

Executive Member for Regeneration and Economic Development:  
Councillor C Rooney

Kevin Parkes, Director of Regeneration

Date: 24 August 2010

---

### PURPOSE OF THE REPORT

- To inform the Executive Member of the future direction of DigitalCity Business (DCB) and to seek approval for the funding package to deliver the 2010/11 - 2011/12 Business Plan.

### SUMMARY OF RECOMMENDATIONS

- It is recommended that the Executive Member for Regeneration and Economic Development endorses the principles of the DigitalCity Business Plan for 2010/11 – 2011/12 and approves its delivery.

Approval is also sought for the financial package required to deliver the plan, including £1,296,280 from One NorthEast and £100,000 from the Council's Local Authority Business Growth Incentive resources.

### IF THIS IS A KEY DECISION WHICH KEY DECISION TEST APPLIES?

- |  |   |
|--|---|
| It is over the financial threshold (£75,000)   | ✓ |
| It has a significant impact on 2 or more wards | ✓ |
| Non Key  | X |

### DECISION IMPLEMENTATION DEADLINE

- For the purposes of the scrutiny call in procedure this report is

|               |   |
|---------------|---|
| Non-urgent    | ✓ |
| Urgent report | X |

## BACKGROUND AND EXTERNAL CONSULTATION

### DigitalCity Business

5. DigitalCity Business (DCB) was formed in 2005 as part of the wider DigitalCity project, aimed at creating a successful and self-sustaining digital and creative 'supercluster' in the Tees Valley.
6. DCB represents the business end of a coordinated pipeline of support to progress graduates from Teesside University's Institute of Digital Innovation (IDI) and other potential digital entrepreneurs through to successful company formation and growth.
7. Although DCB was originally formed as part of the DigitalCity programme based at Teesside University, the core team has operated as part of the Council's Regeneration Department since 2007.

### Progress

8. The DigitalCity project commenced at a time when the digital cluster in the Tees Valley comprised just 10 companies with relatively low levels of ambition. The cluster also suffered from little or no access to specialist support, few opportunities for networking and little interaction with businesses or investors from outside of the area. Most crucially, no businesses within the cluster could be classified as *high growth* (using the Government definition of having potential for turnover of £500,000 by year three).
9. From relatively little activity in 2005, the project has developed a healthily growing cluster with more than 80 companies on DCB's active support list, with 20 currently identifiable as having high growth potential. The role of DCB in this development has been to take the companies leaving the IDI and other potential digital entrepreneurs and steer them through the early stages of business growth, accelerate their progress and maximise their economic potential.
10. Much of the success achieved by DCB has been down to the flexible and innovative way that individual companies are supported, as well as the work that has taken place to develop a fertile environment for collaborative working between companies. The opening of Boho One in July 2009 has also offered the cluster a physical presence that has raised its profile significantly and enabled interaction with a much wider network of people and opportunities.
11. As a result of this innovative work, the cluster is also starting to generate companies with the potential to become internationally renowned and create significant wealth for the area. A recent graduate of the DigitalCity project has just returned from America after raising private investment of over \$1 million to establish his company on the global stage. Market leaders such as Microsoft have been showcasing his product as "the future" at some of the highest profile international conferences for the digital industry. Such exposure (and commercial success) adds further impetus to the growing cluster and offer potential digital entrepreneurs an inspirational success story that has real relevance for them.
12. The cluster that exists in 2010 is therefore unrecognisable from that of 2005 and represents a real opportunity to contribute to the renaissance of the Tees Valley.

Cluster development does however require long-term intervention to become fully sustainable, and activities undertaken over the next two years could play a critical role in determining whether the cluster continues to develop as a regionally important sector and one that can have a genuine global impact.

## **2010/11 – 2011/12 Business Plan**

13. A comprehensive business plan has been developed for DCB activities to determine the strategic activity required to not only maintain the existing rate of cluster development but also accelerate progress to achieve greater impact on an international stage. Achieving this impact would be a critical factor in the cluster ultimately becoming self-sustaining. The activities programmed for delivery over the next two years can be broken down into three key areas.
  - a. Cluster Development – activity to support individual businesses in the Tees Valley and North East through the start up and acceleration phases and the wider development of cluster networking and collaboration. Specific activities include:
    - i. specialised business support for start-ups, including a new online Business Growth Workshop System;
    - ii. specialised business support for high-growth potential companies;
    - iii. network development to foster an integrated, collaborative sector; and,
    - iv. DigitalCity Satellite Initiative designed to draw outlying areas into the main project and mitigate ‘geographic’ and ‘cultural’ remoteness.
  - b. Business Development - outward looking activity to sell the products and services of the cluster in the global marketplace. Business development activities for the cluster include:
    - i. national and international business development including marketing and inward investment;
    - ii. activating digital as a crossover enabler for non-digital sectors, organisations and businesses; and,
    - iii. actively scanning the horizon, researching and ‘ground preparation’ related to mid and long-term opportunities in fast changing digital/crossover environments from which the cluster would benefit.
  - c. Operations - Providing the infrastructure for the cluster to grow successfully. Specific activities include:
    - i. administration and reporting;
    - ii. an online database to give real time cluster mapping with aggregated key metrics, automated records and audit trails; and,
    - iii. operation of Boho One as an effective tool for developing a high profile cluster.
14. The activities programmed for delivery during 2010/11 – 2011/12 would complement those delivered through the IDI - the other key element of the DigitalCity project. The specialist business support and business development activities would also build on and increase the impact of general support available through Business Link, and have been agreed by One NorthEast as meeting the objectives of the Government’s

Business Support Simplification Programme. The plan has also been formally signed-off by the DCB Advisory Board.

15. The business plan addresses the Innovator Connector theme of the North East's European Regional Development Fund (ERDF) programme, which is aimed at using innovation and creativity to enhance the competitiveness of the region and generate a step change in regional economic performance. As a high strategic priority of One NorthEast, DigitalCity's role as an Innovator Connector places it at the heart of the region's knowledge economy infrastructure.
16. Delivery of the business plan in its proposed form will ensure that the economic benefits of a strong digital cluster can be retained within the Tees Valley, but also that such activity becomes firmly embedded in Middlesbrough.

### Satellites

17. As part of the 2010/11 – 2011/12 Business Plan, arrangements are being put in place for DCB to provide support to digital companies within Redcar and Cleveland, Stockton and Barnard Castle. This support would be funded by a contribution from the relevant local authorities or Local Strategic Partnerships. By including this activity within the business plan, it is possible to secure a greater amount of match funding and therefore a contribution towards the core costs of operating DCB, without any loss of capacity within Middlesbrough. One NorthEast have endorsed the provision of support to these 'satellites' of DCB, and view this as an important step in the future development of the digital cluster in the North East.

### Funding Bids

18. The existing DCB project has to date been funded by One NorthEast Single Programme resources. The second phase of DCB activity to be delivered through the 2010/11 – 2011/12 Business Plan would however see an increase in both the scale and scope of activity, and consequently the cost of delivering the service.
19. As One NorthEast continue to value the contribution of DCB to the regional economy, the funding package has been built largely around a joint bid for Single Programme and ERDF resources. As an identified Innovator Connector, DCB also has a strategic significance beyond that of standard ERDF match-funded projects.
20. Although DigitalCity is a regional project, Middlesbrough Council is expected to directly contribute match funding, given the particular benefits and impacts that the project will have in its area. There will however be contributions from other areas, reflecting the growing reach of the activities and the genuine significance of the cluster.
21. In summary, the costs of delivering the new business plan for the two year period 2010/11 to 2011/12 are identified as:

| Item          | £                |
|---------------|------------------|
| Salaries      | 489,102          |
| Overheads     | 157,000          |
| Fees          | 734,178          |
| Other Revenue | 306,000          |
| <b>Total</b>  | <b>1,686,280</b> |

22. The funding package that has been pursued to fund this activity is as follows:

| Source                | £                |
|-----------------------|------------------|
| ERDF                  | 816,280          |
| Single Programme      | 480,000          |
| Middlesbrough Council | 100,000          |
| Stockton Council      | 170,000          |
| Barnard Castle Vision | 100,000          |
| Private Sector        | 20,000           |
| <b>Total</b>          | <b>1,686,280</b> |

23. The current status of the funding package can be summarised as follows:
- a. *ERDF / Single Programme* - a bid for £816,280 of ERDF and £480,000 of Single Programme has been submitted to One NorthEast for expenditure between 1<sup>st</sup> April 2010 and 31<sup>st</sup> March 2012, at an ERDF intervention rate of 49.06%. The bid is progressing through the approval process with an offer letter anticipated shortly..the offer will need to be formally accepted by the Council, before activity can commence;
  - b. *Middlesbrough Council* - a sum of £100,000 has been identified within the Local Authority Business Growth Incentive (LABGI) programme as the Council's contribution to delivering the business plan. This sum has previously been committed to support DigitalCity, specifically as a contingency fund for Boho One, but this is no longer required and can be released for re-investment;
  - c. *Private Sector* - a sum of £20,000 has been included to reflect the contribution made by cluster companies to business support schemes in which they participate; and,
  - d. *Other Contributions* - the contributions to be made by Stockton Council and the Barnard Castle Vision are all in the process of being formally approved by the respective bodies, to cover activity delivered in their own areas as well as a contribution towards the core costs of DCB.

## Outputs and Outcomes

24. Delivery of the business plan would see the following outputs/outcomes achieved during the next two financial years:
- a. 40 new businesses created;
  - b. 80 jobs created;
  - c. 52 businesses assisted ;
  - d. 20 further businesses identified as having high growth potential;
  - e. 2 companies achieving £500,000 turnover per year;
  - f. 20% increase in the aggregated turnover of the cluster; and,
  - g. 75% increase in international trade of the cluster.
25. Although developing further high growth potential businesses is vital to establishing an effective cluster (as the accompanying sub-contracting opportunities would feed others) the most significant benefits of the project would be the increase in turnover of the cluster by 20% and international trade by 75%. Although no mechanisms exist at present to capture the evidence of increased turnover and trade, a new Cluster Management System developed by DCB would be implemented to enable real time

information to be collected on companies within the cluster – a first for any project of this type.

### **Implications for the Council**

26. The activity contained within the business plan will enable DCB and the Council to build on the existing investment in DigitalCity, and further contribute towards key objectives within the Sustainable Community Strategy. The business plan will also provide the best possible opportunity to maximise the economic impact of Boho One, as the impact of the digital sector grows.
27. However, delivery of the 2010/11 - 2011/12 Business Plan would require DCB to operate in a more outward facing role, to ensure that cluster companies continue to exploit global opportunities and that DCB moves towards a more financially sustainable position. There would also be a need to act more entrepreneurially to exploit the commercial opportunities presented by a growing reputation. Without this outward facing, entrepreneurial approach, the cluster would ultimately fail to achieve the ambitious role identified for it by both local and regional strategies.
28. Much of the activity scheduled to take place during 2010/11 and 2011/12 would mirror that already underway through the project, with little additional impact upon the Council. Some new and expanding areas of activity may however have implications for how DCB interacts with the rest of the Council and as a result, the potential for tensions to arise between the way the Council (all Councils) operate and how DCB needs to operate.
29. To enable DCB to pursue this innovative role and maximise the opportunities presented by the global market, there is a need to adopt an approach more in line with the private sector than traditional public sector business support. As a result, it may be necessary to identify areas where specific arrangements or flexibilities might be necessary for DCB to enable a more private sector approach, without of course jeopardising the accountability or probity necessitated by the investment of public funds.

### *Foreign Travel*

30. In order to exploit the opportunities presented by a growing international reputation, DCB would need to undertake a comprehensive programme of sales and marketing visits to key areas where commercial digital activity takes place. As the digital sector is perhaps more global than any other, due to the transferable applications of technology, this would require DCB to interact and form long-term relationships with companies and infrastructure organisations located across the world on behalf of the cluster. As an example, recent trips to Japan and Barcelona undertaken by DCB staff have led to a commercial deal that could potentially bring returns of over £100,000 per year into the cluster.
31. Fulfilling this role would necessitate a programme of foreign travel well in excess of that required by recent DCB activity, as key centres of the digital industry are located in places such as Japan, South Korea, India and the US. As the nature and purpose of this travel is very different to typical local authority activities, there may also be tensions between the costs of such visits and the current Council guidelines for foreign travel. Given the political interest in this topic, the sensitivity of undertaking this work is understood.

32. The emphasis on developing the cluster outwards and pursuing global opportunities is driven not only by the needs of the cluster, but by One NorthEast, with a view to increasing wealth flowing *into* the region rather than creating greater financial churn from within – hence the requirement for a 75% increase in the international trade of the cluster by 2012.
33. Clearly DCB needs to operate in a way that is fit for purpose and it would be counter-productive (and potentially breach funding agreements) to constrain activities because of the fear of how they might be perceived. There is therefore a separate report on the Executive Member agenda that details the proposed programme of travel and recommended approval arrangements, to ensure compliance with Council procedures.

### *Shareholdings*

34. Over recent months, a number of commercial opportunities involving joint arrangements between DCB and major digital companies seeking to enter the UK market have materialised. By representing the cluster in a commercial environment, DCB has been integral in securing a number of opportunities for both cluster companies and DCB itself to enter into joint ventures or take shareholdings in newly formed companies. If DCB is to progress towards independent financial sustainability (and therefore move away from any future reliance upon Council funding), then these opportunities could represent a significant source of income.
35. As a local authority, the Council is not currently geared up to pro-actively pursue commercial opportunities in this way, and as such there are a series of complex issues constraining this type of activity. To capture the benefits of this potential source of income, it is necessary for DCB to develop a model that enables it to trade commercially, whilst still remaining part of the Council. Models for delivering this external, commercial role are currently being developed.

### *Independence*

36. As it is recognised that cluster development is a long-term role, it is necessary for DCB to look at future models of operation beyond the period where public sector support can be secured. Developing a sustainable organisation that is able to operate on behalf of the cluster, but not compete with companies in it, would ultimately require a delicate balancing act between pursuing commercial income for DCB itself and attracting commercial income into the companies it seeks to support. As the flexibility to act as a self-sustaining private sector-style organisation cannot be fully exploited as part of the Council, it may be necessary for DCB to seek a more independent long-term role.
37. By moving gradually towards an independent role, DCB would be able to benefit from continued access to public funding such as Single Programme and ERDF until such time as its commercial activities can provide sufficient income to make independence a viable option. Proposals for a gradual move towards a sustainable, independent organisation have already been discussed at officer level and are to be developed further as part of the 2010/2011 - 2011/12 Business Plan.

## **EQUALITY IMPACT ASSESSMENT**

38. An Equality Impact Assessment has been undertaken for the overall project. No negative impacts have been identified as part of this assessment.

## **OPTION APPRAISAL/RISK ASSESSMENT**

### **Option Appraisal**

39. As part of the business case development process with One NorthEast, a number of options were explored.

#### *Do nothing*

40. By ceasing DCB activity at the end of 2009/10, the cluster would remain structurally incomplete and unable to sustain itself. The established process of converting digital graduates into wealth creating entrepreneurs would be undeliverable without the business-focused activities of DCB. Previous investment made would also not be maximized. The impact of this on Middlesbrough would be dramatic, as Boho One would represent a high profile flagship project operating without the necessary infrastructure to deliver the cluster growth required to make it sustainable. The corresponding loss of confidence in the local economy would be substantial, as so much of the economic future of Middlesbrough rests upon opening up new sectoral areas such as digital, to replace more traditional industries.

#### *Altering the scale of the project*

41. Delivering a smaller scale project would enable some activities to happen, but as the different components are all inter-related, this would generate proportionately less impact due to a loss of critical mass. A larger scale project would allow further capital elements to be developed, but insufficient match funding exists to make it a realistic option.

#### *Outsourcing cluster activities*

42. The management and control of cluster activities would be hugely ineffective without a central body to oversee it. DCB already uses a high degree of outsourcing and reducing direct delivery further would not enable the same coherent packages to be put together for businesses at the start up or acceleration phase.

#### *Deliver the whole DigitalCity (DCB and Teesside University IDI) project through one body*

43. Although there are superficial reasons for merging the two projects (i.e. some minimal staffing efficiencies), the rationale for separate delivery structures has long been established and has ultimately proved successful. Teesside University recognises that it is not equipped to lead the direct business focus that DCB requires, just as DCB would not be equipped to lead the academic end of the project. The ethos and culture of the two elements of the project are totally different and recognised by both parties (and One NorthEast) as the most effective way to proceed.

#### *Preferred Option*



44. The approach taken in the business case is identified as the most appropriate option to deliver the overall DigitalCity vision of a successful and vibrant digital business cluster. It has a structure and methodology that has been successfully tried and tested, and has worked well in previous phases of DCB. The project would continue to be delivered by a small and highly focused core team that would utilise carefully chosen, high quality freelance provision where appropriate. This represents the best possible mix of an entrepreneurially oriented project that at the same time satisfies the requirements of the public sector: a fast moving, flexible, demand driven project led by business focused people, which at the same time is highly compliant, transparent and publicly accountable.

## **Risk Assessment**

45. As part of the business case development process with One NorthEast, a full and detailed risk assessment has been undertaken. The key risks associated with the submission and management of the business plan are also detailed below.

### *Partner Contributions*

46. Approval of the project by One NorthEast will be dependant upon the contributions identified from other partners being formally secured. Whilst all amounts included within the funding package have been agreed with officers of the appropriate organisations, each one will need to formalise their contribution prior to the issuing/acceptance of any offer letter from One NorthEast. Failure to secure formal approval for any of these contributions would result in the funding package (and therefore the ambitions of the business plan) being reduced, prior to it being resubmitted.

### *Private Sector Contributions*

47. The £20,000 included within the bid reflects a target set by One NorthEast to demonstrate the financial input of cluster companies in some of the business development schemes in which they participate. As this activity is not classed within the bid as 'eligible expenditure' and is not matched against ERDF, failure to secure the full £20,000 would have no effect on the total amount of ERDF or Single Programme funding secured.

## **FINANCIAL, LEGAL AND WARD IMPLICATIONS**

### **Financial Implications**

#### *Single Programme/ERDF*

48. Acceptance of the offer of £1,296,280 (the final sum is likely to be subject to minor adjustments during the appraisal/approval process) from One NorthEast would necessitate the Council acting as Accountable Body for the project. The extensive Single Programme/ERDF experience of the Regeneration Programmes Team will be utilised to ensure sound project management and that grant conditions are adhered to.

#### *LABGI*

49. Acceptance of the offer letter would also require the Council to commit £100,000 from LABGI resources, as detailed in paragraph 24. This allocation is currently identified within the LABGI programme and represents a contribution of 5% of the overall project total.

#### *Commercial Trading / Income*

50. As identified above, some of the activities undertaken by DCB would generate income, to contribute towards the financial sustainability of the organisation in future years. Maximising these opportunities would require a significant level of involvement from Legal Services and Strategic Finance to establish the appropriate vehicles and delivery mechanisms.

#### *Foreign Travel*

51. As identified in paragraph 31, a significant increase in foreign travel would be required for DCB to deliver their role in generating international trade. This issue is discussed further in the separate report.

#### *Board Member Remuneration*

52. The DCB Advisory Board currently has a private sector Chairperson who receives remuneration of £12,000 per annum. As the scope and scale of the bid will place increased demands upon the Chairperson, it is intended to increase the remuneration to £15,000 per annum. In line with Nolan principles, the post of Chairperson will be re-specified and re-advertised.

### **Legal Implications**

53. The offer letter issued upon confirmation of the project approval from One NorthEast would be subject to the same legal requirements as all others taking advantage of external funding opportunities.
54. No further contractual arrangements are being entered into as a result of approving the business plan, although future commercial/trading aspects would require input from Legal Services to ensure deliverability within a public sector environment.
55. The process for developing the legal structures for DCB to undertake commercial activity are well advanced and are being prepared jointly by Regeneration, Strategic Finance and Legal Services. Once finalised, these structures will require the appropriate internal endorsements before being put into place.

### **Ward Implications**

56. Although DCB is based within Middlehaven Ward, the businesses forming part of the cluster are located across Middlesbrough and the wider Tees Valley. The economic impact of a successful project would also extend across the whole of Middlesbrough and the wider Tees Valley.

## **RECOMMENDATIONS**

57. It is recommended that the Executive Member for Regeneration and Economic Development:
- a. endorses the activities of the 2010/11 – 2011/12 Business Plan, as set out in paragraph 13 and approves its delivery;
  - b. delegates the Director of Regeneration to undertake the necessary procedures to enable the full implementation of the DCB 2010/11 – 2011/12 Business Plan;
  - c. approves the contribution of £100,000 of Local Authority Business Growth Incentive resources towards delivery of the DCB 2010/11 – 2011/12 Business Plan; and,
  - d. notes the further work required to address the identified issues around foreign travel, commercial activity and future independence.

## **REASONS**

58. Delivery of the 2010/11 – 2011/12 Business Plan would provide the digital sector with the maximum opportunity to grow and establish itself as a key economic driver for the area. It would also offer the opportunity to capitalise on the previous investment made in the digital sector to enable it to further contribute to the delivery of Council objectives.

## **BACKGROUND PAPERS**

59. The following background papers were used in the preparation of this report:

*DigitalCity Business 2010/11 – 2011/12 Business Plan*

**AUTHOR: Richard Horniman**

**TEL NO: 729568**

---

*Address:*

*Website: <http://www.middlesbrough.gov.uk>*