

## REVIEW OF REASONS PUT FORWARD BY STEAMSHIP GROUP FOR REJECTING LEVELLING UP FUNDING

Steamship Group have issued a “fact sheet” setting out their reasons for not pursuing Levelling Up Funding. This was published on the Steamship Group’s web site, features in their media statements and was also included with the letters sent by the group to the Secretary of State for Transport, Minister for Maritime, Permanent Secretary at the Department for Transport, Secretary of State for Levelling Up, Secretary of State for Defence, and the Chairman of the Council of the Isles of Scilly.

The table below shows the outcome of the fact checking process undertaken by officials at the Council of the Isles of Scilly.

Isles of Scilly Steamship Group “Fact sheet”			Council of the Isles of Scilly Outcome of fact check assessment
1.	<b>LEVELLING UP FUNDING IS NOT A GRANT</b>	Levelling Up Funding is not a grant. It is not free money. The Company would have to pay a substantial annual lease charge for the use of the vessels.	<p><b>INCORRECT</b></p> <ul style="list-style-type: none"> <li>Levelling Up Funding is a grant. It is free money as no repayments are required.</li> <li>No lease charge was proposed.</li> <li>The annual sum referenced was to cover the cost of the mid-life refit of the vessels and requirement to meet net zero targets set by Government. Any operator should set aside funds to meet these costs irrespective of how the vessels are financed.</li> <li>The fund stays with the vessels, whoever operates them, to ensure the mid-life refit can be paid for without additional fare increases being required.</li> </ul>
2.	<b>RISK OF CHALLENGE</b>	There was a high risk of challenge from other shipyards as our procurement process, although rigorous, did not follow a public procurement process. There was also a risk of challenge from other operators due to the initial operation of the route under LUF being awarded directly to the Company.	<p><b>INCORRECT</b></p> <ul style="list-style-type: none"> <li>The Government offered the opportunity to the Steamship Group in August 2022 to play a leading role in the delivery of the project. This would have allowed the Steamship Group to use its designs, adapt its procurement process with guidance to minimise risk, manage the vessel build and commissioning process and operate the new vessels for an initial period.</li> <li>The proposal to award the initial operation of the route to the Steamship Group was considered justifiable given the age of the existing vessels, progress with design and market engagement, route knowledge and the importance of sea links services.</li> <li>Following further work by the Council of the Isles of Scilly and Department for Transport, a further offer was made to the Steamship Group in August 2023 which would have allowed the Steamship Group to use the Levelling Up Funding to deliver the new vessels and initially operate them for between 10 - 15 years before the service would be subject to competitive tendering.</li> </ul>
3.	<b>DELAYS AND HIGHER COSTS</b>	If these risks of challenge materialised, which was highly likely, this would result in further delays of potentially 2 years, resulting in new vessels not being in operation until 2028 as a result of having to restart a new public procurement process and to respond to legal challenges. This would mean significantly higher build costs and also a great deal of Company money having to be spent fighting the challenges.	<p><b>INCORRECT</b></p> <ul style="list-style-type: none"> <li>The leading role offered to the Steamship Group in August 2022 provided the opportunity for the Group to work with the Government and Council to adapt its procurement process to minimise any risks.</li> <li>Any potential challenge would have been against the decisions taken by the public bodies involved and not Steamship Group.</li> <li>In August 2022, the Steamship Group was offered the opportunity to submit its plans to ensure the continuity of lifeline link services and any additional costs prior to the introduction of new vessels, to the Department for Transport so that the funding requirements could be assessed.</li> </ul>
4.	<b>CURRENT VESSELS ARE IN URGENT NEED OF REPLACEMENT</b>	The current vessels are over 40 years old and in urgent need of replacement. Any delay beyond 2026 will result in more disruption to the service and increasingly higher maintenance costs.	<p><b>CORRECT but incomplete</b></p> <ul style="list-style-type: none"> <li>The Government offered the Steamship Group the opportunity in August 2022 to submit its plans to ensure the continuity of lifeline link services and any additional costs prior to the introduction of new vessels so that the funding requirements could be assessed.</li> <li>No plan was submitted by the Steamship Group and therefore the funding required to maintain the existing vessels until the new vessels entered service could not be assessed.</li> </ul>

5.	<b>NO CERTAINTY OF FUNDING</b>	There was no certainty with LUF. The money was not guaranteed from Government. It may never have materialised. The Company had already waited over 2 years following the announcement of funding being awarded but there was still no mechanism in place to obtain the funding. Private finance ensures certainty that the vessels will be in the water by 2026.	<p><b>INCORRECT</b></p> <ul style="list-style-type: none"> <li>Funding for the new vessels was announced by the Government in its Autumn Budget Statement in October 2021.</li> <li>In announcing that £48.4m was to be made available, the then Secretary of State for Transport, RT Hon Grant Shapps MP, said –“ I have just committed £48.5m of levelling up funding to contribute to the replacement of the current passenger and freight vessels, which will sustain the long-term future of the sea links services between the Isles of Scilly and the mainland.”</li> <li>All major projects are required to submit a business case to Government for approval in order for the funding to be released.</li> <li>The business case prepared for the Sea Links Project could not be completed as the Steamship Group were not prepared to provide all the information required to complete the business case and meet the Government’s requirements.</li> </ul>
6.	<b>RESTRICTIONS ON PROFITS – HIGHER SKYBUS FARES</b>	A condition of the LUF is that the level of profit generated by the sea link operation would be restricted to a “reasonable level”. This restriction in profit to this level would have meant the Company could not provide the current level of support to Skybus for its capital expenditure requirements. Therefore, Skybus prices would have to increase by at least 25% which would be a detrimental outcome for the community and would consequentially reduce the number of visitors to the islands. Although we raised concerns with officials on the impact this condition would have on Skybus fares, our concerns were rejected.	<p><b>INCORRECT</b></p> <ul style="list-style-type: none"> <li>No maximum profit was ever set for the operation of the sea link services, but a minimum guaranteed profit was proposed.</li> <li>Steamship Group did request a minimum group profit be guaranteed including the air services but this was not acceptable to Department of Transport and the Council of Isles of Scilly.</li> <li>No restrictions were proposed which would limit the company’s ability to subsidise the air link.</li> <li>Confirmation that there were no restrictions on the profitability of sea link services together with provisional minimum profit and incentivised profits levels were confirmed in writing to the company in advance of its Board meeting in September 2023 with further confirmation that there was not a maximum amount for the profitability of the sea link services.</li> <li>The Government waived the requirement for the Steamship Group to contribute the standard 10% towards the total cost of the vessels saving the company £4.2m.</li> </ul>
7.	<b>FUTURE UNCERTAINTY</b>	The Company would have to tender for the operation every 5-7 years, meaning not only a huge amount of cost - both financial and time - having to undergo a tender process, but also uncertainty for existing employees and difficulty in recruiting new or replacement employees.	<p><b>INCORRECT</b></p> <ul style="list-style-type: none"> <li>An initial operating period of between 10-15 years before the Steamship Group would need to tender for the operation was proposed by the Council and Government in the draft memorandum of understanding provided to the company in 2023.</li> <li>Any future procurement would be biased towards the social value of the sea link services rather than the lowest cost in recognition of the lifeline nature of the route.</li> <li>If the tendering did result in a different operator providing the service, operational and customer facing staff would automatically transfer to the new operator under the Transfer of Undertakings (Protection of Employment) Regulations.</li> </ul>
8.	<b>LACK OF CONTROL</b>	The Company would not have full control of its own business as it would have minor representation on the Special Purpose Vehicle (SPV) Board.	<p><b>INCORRECT</b></p> <ul style="list-style-type: none"> <li>The Steamship Group would have still had a strong influence over the control of sea link services provided. The Memorandum of Understanding developed by the external legal advisors appointed by the Government proposed the following board membership for the Special Purpose Vehicle company: <ul style="list-style-type: none"> <li>Steamship Group - 4 representatives</li> <li>Council of the Isles of Scilly - 2 representatives</li> <li>Department for Transport – 1 representative</li> <li>Independent non-executive directors – 3 appointed, one who will be the chair.</li> </ul> </li> <li>The board of directors were to be responsible for the overarching management of the Special Purpose Vehicle company, with a list of issues reserved for unanimous agreement between the board members representing the shareholders.</li> <li>To allow the Steamship Group to operate the sea links services effectively, a scheme of delegation was proposed to ensure it had the responsibility for day-to-day management and operational decisions.</li> </ul>
9.	<b>PRIVATE LOAN FINANCIALLY FAVOURABLE</b>	Long term, the private finance route is more financially favourable as the loan repayments would stop in 20 years (reducing each year throughout that period) but the lease payment under LUF would continue forever and most likely increase.	<p><b>INCORRECT</b></p> <ul style="list-style-type: none"> <li>The levelling up grant funding had no repayment amounts included. By taking out the loan, Steamship Group has to meet the loan repayments and interest charges over the duration of the loan.</li> <li>The vessel refit fund is to cover the cost of the mid-life refit of the vessels and requirement to meet net zero targets set by Government. The Steamship Group will have to build up these funds regardless of grant funding or private financing.</li> </ul>