

Agenda – Public Accounts Committee

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| Meeting Venue: | For further information contact: |
| Committee Room 3 – Senedd | Fay Bowen |
| Meeting date: 5 November 2018 | Committee Clerk |
| Meeting time: 14.45 | 0300 200 6565 |
| | SeneddPAC@assembly.wales |

(Pre-Meeting)

(14.45 – 15.15)

1 Introductions, apologies, substitutions and declarations of interest

(15.15)

2 Paper(s) to note

(15.15 – 15.20)

(Pages 1 – 3)

2.1 Natural Resources Wales: Scrutiny of Annual Report and Accounts 2017–18 – Correspondence from Clare Pillman (17 October 2018)

(Page 4)

3 The Welsh Government’s relationship with Pinewood: Evidence session with the Welsh Government

(15.20 – 16.30)

(Pages 5 – 85)

Research Briefing

PAC(5)–29–18 Paper 1 – Auditor General for Wales’ Report

PAC(5)–29–18 Paper 2 – Letter from Bethan Sayed AM, Chair of the Culture, Welsh Language and Communications Committee

PAC(5)–19–18 Paper 3 – Paper from the Welsh Government

Andrew Slade – Director General, Economy, Skills and Natural Resources, Welsh Government

Jason Thomas – Director Culture, Sport and Tourism, Welsh Government

Tim Howard – Deputy Director of Property, Welsh Government



4 Motion under Standing Order 17.42 to resolve to exclude the public from the meeting for the following business:

(16.30)

Items 5 & 6 and Items 1 & 2 of the meeting on 12 November 2018

**5 The Welsh Government's relationship with Pinewood:
Consideration of the evidence received**

(16.30 – 16.45)

6 Natural Resources Wales: Consideration of the draft Report

(16.45 – 17.00)

(Pages 86 – 108)

PAC(5)-29-18 Paper 4 – Draft Report

Concise Minutes – Public Accounts Committee

Meeting Venue:

Committee Room 3 – Senedd

Meeting date: Monday, 22 October 2018

Meeting time: 13.15 – 16.00

This meeting can be viewed

on [Senedd TV](#) at:

<http://senedd.tv/en/5036>

Attendance

| Category | Names |
|---------------------|--|
| Assembly Members: | Nick Ramsay AM (Chair) Mohammad Asghar (Oscar) AM Neil Hamilton AM Rhianon Passmore AM Jenny Rathbone AM |
| Witnesses: | David Anderson, National Museum Wales Neil Wicks, National Museum Wales Nia Williams, National Museum Wales |
| Wales Audit Office: | Adrian Crompton – Auditor General for Wales Ann-Marie Harkin Dave Rees Matthew Mortlock |
| Committee Staff: | Adrian Crompton Ann-Marie Harkin Dave Rees Matthew Mortlock |



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| | Fay Bowen (Clerk) Meriel Singleton (Second Clerk) Claire Griffiths (Deputy Clerk) Helen Jones (Researcher) |
|--|---|

1 Introductions, apologies, substitutions and declarations of interest

- 1.1 The Chair welcomed Members to the meeting.
- 1.2 Apologies were received from Adam Price AM.

2 Paper(s) to note

- 2.1 The papers were noted.

3 Scrutiny of Accounts 2017–18: National Museum Wales

- 3.1 Members scrutinised David Anderson, Director General, Neil Wicks, Deputy Director General and Director of Finance and Corporate Resource, and Nia Williams, Director of Learning & Engagement from National Museum Wales on National Museum Wales' Annual Report and Accounts for 2017–18.
- 3.2 Neil Wicks agreed to provide the Committee with the average number of days per employee lost through sickness in 2017–18.

4 Motion under Standing Order 17.42 to resolve to exclude the public from the meeting for the following business:

- 4.1 The motion was agreed.

5 Scrutiny of Accounts 2017–18: Consideration of evidence received and discussion of key issues for the draft report

- 5.1 Members considered the evidence received.

6 Natural Resources Wales: Consideration of the draft report

- 6.1 Members considered and agreed the draft report.

7 Care experienced children and young people: Agreement of draft Report

7.1 Members agreed the draft report.

Agenda Item 2.1



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Naturiol
Cymru
Natural
Resources
Wales**

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Mr Nick Ramsay
Chair, Public Accounts Committee
National Assembly for Wales
Cardiff Bay
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CF99 1NA

17 October 2018

Dear Nick –

Public Accounts Committee – Monday 24 September 2018

Following the Public Accounts Committee evidence session of the 24 September 2018, you requested that further information was provided on how much timber produced in Wales was processed in Wales in 2017-18.

It is not currently possible to give the exact figures for the amount of Welsh grown timber processed in Wales, due to the way such information is recorded, this is especially true of the private woodland sector, which will account for around 50-60% of harvesting in any year.

However, our best estimate for the period 2017-18, is that around 93% or the 622,000 tonnes of Welsh grown timber from the Welsh Government Woodland Estate was processed in Wales.

I will write to you separately regards the payment to our previous Chief Executive.

Best wishes,

Clare Pillman

Chief Executive, Natural Resources Wales

Document is Restricted

Archwilydd Cyffredinol Cymru
Auditor General for Wales

The Welsh Government's relationship with Pinewood



WALES AUDIT OFFICE
SWYDDFA ARCHWILIO CYMRU



I have prepared and published this report in accordance with the Government of Wales Act 2006.

The Wales Audit Office study team comprised Ian Hughes and Anwen Worthy under the direction of Mike Usher.

**Huw Vaughan Thomas
Auditor General for Wales
Wales Audit Office
24 Cathedral Road
Cardiff
CF11 9LJ**

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Mae'r ddogfen hon hefyd ar gael yn Gymraeg.

Contents

Our review examined the Welsh Government’s relationship with Pinewood. This commenced with the Collaborative Agreement entered into by the Welsh Government and Pinewood in February 2014 to promote TV and film production in Wales. We set out the facts leading to the termination of this agreement, together with details of the successor Management Services Agreement that commenced in November 2017.

| | |
|--|-----------|
| Summary report | 6 |
| What this review is about | 6 |
| Key findings | 8 |
| Part 1 – Establishment of the Welsh Government’s Collaboration Agreement with Pinewood in February 2014 | 12 |
| Welsh Government Ministers entered into a Collaboration Agreement with Pinewood to promote TV and film production in Wales | 12 |
| The Welsh Government established a £30 million budget to invest in film and TV production, and appointed Pinewood Film Advisors (Wales) Ltd to identify projects suitable for investment | 22 |
| Part 2 – Operation of the Collaboration Agreement until October 2017 | 25 |
| The Welsh Government established an independent Media Investment Panel to decide which projects put forward by Pinewood should be supported by the investment budget | 25 |
| The Media Investment Budget’s performance did not meet the panel’s expectations | 27 |
| Pinewood Studios Wales Ltd was unable to operate the studio as a going concern without the support of Pinewood Group Limited | 30 |
| Part 3 – The revised management arrangements from November 2017 | 33 |
| In October 2017, the Welsh Government terminated its Lease and Collaboration Agreements with Pinewood, and Pinewood ceased to manage the Media Investment Budget | 33 |
| In November 2017, the Welsh Government entered into a new three-year ‘management services agreement’ with Pinewood Studios Wales Ltd | 33 |

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|---|-----------|
| Appendices | 39 |
| Appendix 1 – Our audit approach and methods | 39 |
| Appendix 2 – Timeline of events | 40 |
| Appendix 3 – The Welsh Government’s overall approach to promoting Wales as a venue to produce high-impact film and TV productions | 41 |
| Appendix 4 – The seven types of investment that the Welsh Government can make in TV and film productions | 42 |
| Appendix 5 – Productions supported by the Media Investment Budget, 2014-2018 | 44 |

Summary report

What this review is about

- 1 In February 2014, the Welsh Government purchased the former Energy Centre site at Wentloog¹ for £6.3 million to develop as a film and TV studio in collaboration with Pinewood Shepperton Plc (Pinewood).
- 2 Shortly afterwards, Welsh Government Ministers entered into a 'Collaboration Agreement' with two newly established subsidiary companies of Pinewood. The agreement involved the Welsh Government:
 - leasing the Wentloog studio to Pinewood;
 - establishing a £30 million Media Investment Budget (for which Pinewood would source productions suitable for Welsh Government investment); and
 - sponsoring Pinewood to market and promote both the studio and the investment budget.
- 3 By entering into this Collaboration Agreement, over five years, the Welsh Government expected to generate an estimated £90 million production spend in Wales, creating or safeguarding at least 1,950 full-time equivalent job years.
- 4 In order to deliver the benefits of the Media Investment Budget, the Welsh Government created an independent Media Investment Panel to scrutinise the investment proposals identified and put forward by Pinewood.
- 5 Members of the Panel² decided in August 2016 that the Collaboration Agreement was unlikely to meet the Welsh Government's expectations for the performance of the investment budget. In January 2017 Pinewood confirmed its willingness to renegotiate the terms of the Collaboration Agreement.
- 6 Following negotiations, the Welsh Government and Pinewood entered into a new 'Management Services Agreement' on 1 November 2017.
- 7 There has been political and media interest in the new agreement and the events leading up to it. An Assembly Member has raised concerns with the Auditor General about the terms of both the original collaboration agreement and the new management services agreement.
- 8 The National Assembly's Culture, Welsh Language and Communications Committee is currently conducting an inquiry into major film and television production in Wales.

1 Located between Newport and Cardiff.

2 In conjunction with members of the Welsh Government's Creative Industries Sector Panel.

- 9 This 'facts only' report sets out the key matters relating to the Welsh Government's agreements with Pinewood. We have not examined the value for money the Welsh Government has obtained from the Collaboration Agreement or the effectiveness of its work in promoting this sector of the Welsh economy.
- 10 **Appendix 1** sets out our audit approach and methods, and **Appendix 2** sets out a timeline of key events.
- 11 **Appendix 3** sets out the Welsh Government's overall approach to promoting Wales as a venue to produce high-impact film and TV productions, whilst **Appendices 4 and 5** provide further details about the Media Investment Budget.

Key findings

- 12 In February 2014, the Welsh Government purchased the former Energy Centre site at Wentloog for £6.3 million to develop as a film and TV studio in collaboration with Pinewood. The building was renovated at a cost to the Welsh Government of £3.1 million. This included unforeseen roof repairs of just under £1 million.
- 13 The Welsh Government also acquired a Grade II Listed Farmhouse as part of the purchase. This needed improvements of around £360,000 to meet required standards. Although the farmhouse was seen as a potential valuable asset, it has not been renovated as planned and remains derelict on land adjacent to the main Wentloog site.
- 14 Shortly after the Wentloog site was purchased, Welsh Government Ministers entered into a 'Collaboration Agreement' with Pinewood Shepperton Plc to promote TV and film production in Wales. The agreement involved the Welsh Government:
 - leasing the former Wentloog Energy Centre to Pinewood Studio (Wales) Ltd over a 15 year term;
 - redeveloping the site and branding it 'Pinewood Studio Wales';
 - creating a £30 million Media Investment Budget, to be made available over a period of five years for investment in film and TV development, production and distribution. Pinewood Film Advisors (Wales) Ltd was established and appointed to identify and formulate production proposals to utilise the budget; and
 - 'sponsoring' Pinewood Studio (Wales) Ltd to market and promote the new film and TV studio and media investment budget at an annual cost of £525,600 over a five year term.
- 15 The Welsh Government established a new and independent Media Investment Panel to decide which productions sourced by Pinewood should be supported by the investment budget and by what type(s) of funding package.
- 16 By August 2016 members of the Media Investment Panel and Creative Industries Sector Panel had become dissatisfied with the performance of the Media Investment Budget, which was lower than anticipated.

- 17 The latest available figures show that £13.8 million of the £30 million budget has been invested across 14 projects. A total of £4.3 million has so far been recouped from the projects supported. One project has recouped more than its original investment; four projects have recouped some of their original investment and nine projects have not yet recouped any of their original investment. These projects are in various stages of development; some have not yet benefitted from international cinematic release or TV broadcast, and funds will continue to be recouped through auxiliary sales.
- 18 Welsh Government officials advised the Cabinet Secretary for Economy and Infrastructure in August 2016 of their concerns about the budget's performance. These concerns were:
- a greater number of higher-risk investments being put forward by Pinewood because productions could obtain lower-risk funding from other sources;
 - Pinewood's operating model meant it was reluctant to invest its own money in these higher-risk projects alongside the Welsh Government; and
 - Pinewood might be conflicted in its involvement with the budget as it also had an interest (not prohibited under the Collaboration Agreement) in providing its own London-based services to the industry. Welsh Government officials felt that a perception had arisen amongst other companies that Pinewood had an unfair competitive advantage in securing post-production work in Wales. They therefore considered that this had the potential to reduce the economic benefits to Wales.
- 19 By January 2017, Pinewood had been acquired by new owners, and informed the Welsh Government of its willingness to introduce a new arrangement for operating the studio. By this time:
- Pinewood had adopted a new international business model, focussing on the provision of studio facilities instead of investing directly in TV and film productions;
 - the height of the eaves at Pinewood Studio Wales (25 feet) had been identified as a limiting factor, as the site was unable to accommodate higher-budget film productions which required aerial panoramic perspectives; and
 - the anticipated demand for the studio had not materialised, resulting in it being run at a loss to Pinewood once the initial two-year rent-free period had ended.

- 20 Pinewood executives told us that the opening of a new film and TV production studio by Bad Wolf Studios (Wales) Ltd in Trident Park, Cardiff, in May 2017 had a detrimental impact on the occupancy of Pinewood Studio Wales. The number of enquiries they received for it had fallen as a consequence, although demand for Pinewood studios within the UK remains strong.
- 21 Bad Wolf has benefited from a £9 million funding package from the Welsh Government which is structured as an initial £4.5 million repayable loan that can be converted into non-repayable grant funding if certain milestones are met in relation to production spend in Wales. The Welsh Government will release the remaining £4.5 million as grant payments if additional production spend targets are met. In addition, the Welsh Government leases to Bad Wolf, on commercial terms, the Wolf Studios Wales facility in Cardiff Bay.
- 22 Welsh Government officials told us that demand for studio facilities will fluctuate as productions come and go but, in their view, demand for the Wentloog site had been affected by a change of focus after a change in ownership at Pinewood.
- 23 Welsh Government officials do not believe there has been a drop in enquiries for Pinewood since Wolf Studios Wales opened its doors. In the last 12 months, Wales Screen has conducted studio visits with major productions on ten occasions. Pinewood was not included on only two of these occasions and both were a result of producer choice. The Welsh Government considers that Wales Screen³ promotes all facilities in Wales equally, however that assertion is contested by Pinewood. To date, Wolf Studios Wales has only been home to Bad Wolf productions, whereas Pinewood has been used for productions from the BBC, Channel 4 and independent film companies.
- 24 In October 2017, the Cabinet Secretary for Economy and Infrastructure accepted his officials' advice to terminate both the Lease and the Collaboration Agreement with Pinewood, and to place the Media Investment Budget on hold.

3 See Appendix 3 for more details about Wales Screen.

- 25 On 1 November 2017, the Welsh Government entered into a new three-year 'management services agreement' with Pinewood Studios (Wales) Ltd. This new agreement contains two complementary parts; the sales and marketing of the studio and the studio operation and management services. The Media Investment Budget is now being managed by Welsh Government officials.
- 26 The annual net cost to the Welsh Government of the management services agreement is estimated to be £392,000 (plus an additional annual management fee to Pinewood, which has been redacted from this report on the grounds of commercial sensitivity⁴).
- 27 This net cost estimate assumes that the annual revenue forecast of £714,000 which was included in the submission to the Cabinet Secretary is realistic. However, that annual revenue forecast was supplied by Pinewood based on the pipeline of projects in March 2017 and before the opening of Bad Wolf Studios. Pinewood had added the caveat at the time that these revenues could be lower due to increased competition from Wolf Studios. Welsh Government officials told us that the reliability of the revenue forecast was tested and scrutinised by officials and also by independent property advisors.
- 28 Welsh Government officials recognise that these financial projections do not represent good value for money. However, in their view it was more financially advantageous to enter into a three-year agreement with Pinewood⁵ with the prospect of generating some commercial revenues, compared to the costs that the Welsh Government would have incurred by leaving the site empty whilst they searched for a new tenant.

4 See Paragraph 3.13, Exhibit 10 and Footnote 29 for further explanation of the reasons for this redaction

5 This agreement included a clause permitting either party to terminate with six months' notice, after the initial 12 months.

Part 1 – Establishment of the Welsh Government’s Collaboration Agreement with Pinewood in February 2014

Welsh Government Ministers entered into a Collaboration Agreement with Pinewood to promote TV and film production in Wales

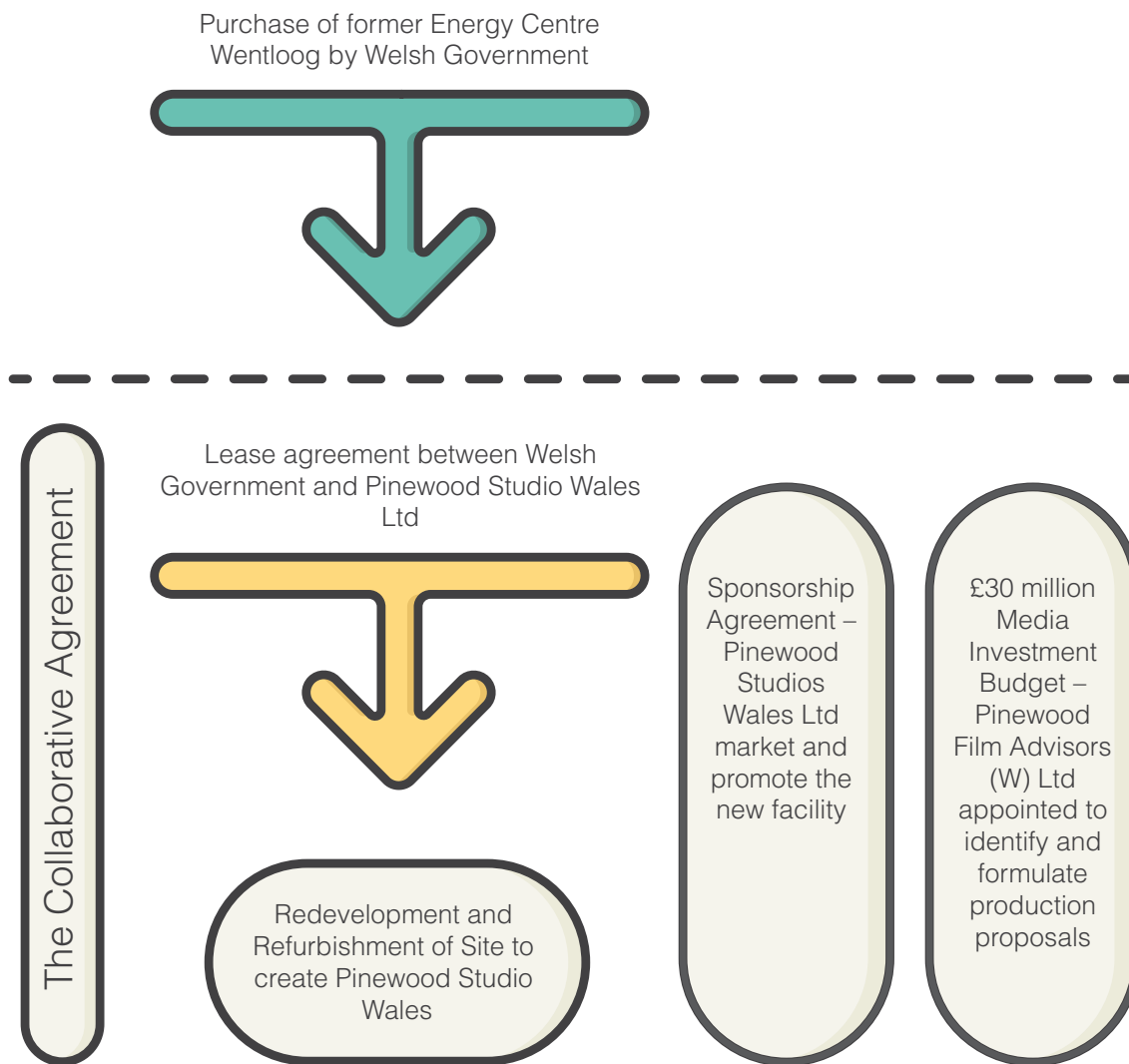
- 1.1 During 2013-14, Welsh Government officials held discussions with Pinewood executives about establishing a world-class studio facility in Wales. This would form part of Pinewood’s global network of film studios. To complement the studio, the Welsh Government also developed plans to create a £30 million investment budget to support film and TV productions in Wales. This would be operated by Pinewood Film Advisors (Wales) Ltd on behalf of the Welsh Government.
- 1.2 A keystone element of the proposal, distinct from the Collaboration Agreement itself, was the Welsh Government’s acquisition of the Energy Centre building at Wentloog. This was to be redeveloped by the Welsh Government and Pinewood as the studio facility. The studio would be run by Pinewood Studio (Wales) Ltd, another newly established subsidiary company of Pinewood.
- 1.3 The Welsh Government anticipated a rental income of £1.6 million from Pinewood Studio (Wales) Ltd for the studio facility over the first five years of the agreement.
- 1.4 Pinewood had already worked with the Isle of Man Government to introduce the Isle of Man Media Development Fund in 2012; this was a fund of £25 million to be used on film and TV productions. This fund built on a range of creative-sector initiatives introduced by the Isle of Man Government since 1995. Independent economic analysis of the Isle of Man’s support for TV and film productions, concluded that it had generated a direct local spend of £100 million and 2,140 full-time equivalent jobs since 1995.
- 1.5 Both the Scottish Government⁶ and the Northern Ireland Assembly⁷ were also expanding their dedicated studio facilities to cope with increasing demand from the film and TV industry.

6 Scottish Government website, [Creative Industries: Film and TV production in Scotland](#)

7 Northern Ireland invested in new sound stages in October 2012 to provide additional studio space at Titanic Studios, Belfast.

1.6 On 17 February 2014, the Welsh Government and Pinewood concluded their negotiations and Ministers entered into a 'Collaboration Agreement' with Pinewood Film Advisors (Wales) Ltd, as shown in **Exhibit 1**.

Exhibit 1: The key elements of the Collaboration Agreement



Source: compiled by the Wales Audit Office from information held by the Welsh Government.

- 1.7 According to projections, the Welsh Government could expect to see an estimated £90 million of film and television production expenditure in Wales over the next five years through this Collaboration Agreement. This spend would create or safeguard at least 1,950 full-time equivalent job years. These projections drew on an independent economic analysis undertaken in respect of the Isle of Man fund. Pinewood's internationally recognised brand name was seen as being central to the success of the proposal.
- 1.8 Welsh Government officials had undertaken financial due diligence on the financial forecasts provided for the activities to be undertaken by the two Pinewood subsidiaries; Pinewood Film Advisors (Wales) Ltd and Pinewood Studio (Wales) Ltd. The Welsh Government concluded that the financial risks of entering into the deal were low, based on the assumption that both businesses would be financially supported by Pinewood Shepperton Plc.
- 1.9 Officials also commissioned a media industry specialist to provide accountancy advice, and to conduct a desktop review of Pinewood's business plan. That review concluded that the potential weaknesses identified were individually, and in aggregate, insignificant compared to the upsides of increased UK studio capacity, the establishment of a regional film studio, job creation and economic benefit for Wales. However, the review did flag up the potential challenges of attracting film and TV productions to the Wentloog site, given there was already some four million square feet of potential studio space within the M25.
- 1.10 Officials in the Welsh Government's Creative Industries sector team also analysed the business case for the proposals, and concluded that it represented a sound investment. This conclusion was based on a detailed analysis of the business plan provided by Pinewood, and consideration of industry demand for a film and TV studio and access to an investment budget in Wales.

The Welsh Government purchased the former energy site in Wentloog to develop as a film and TV studio

- 1.11 As a prelude to the agreement and in order to be able to establish a film and TV studio, the Welsh Government needed to purchase a suitable site.
- 1.12 A search was undertaken by Welsh Government officials to identify suitable sites based on Pinewood's specific requirements. Pinewood shortlisted two sites and subsequently identified the former Energy Centre building at Wentloog as the better of the two shortlisted options. The building was being actively marketed by agents at a purchase guide price of £8.34 million (including VAT). It was known that there was market interest in the property on both a purchase and rental basis. Purchase of the site to include the freehold interest was considered by the Welsh Government to represent better value for money than a lease of the site⁸.
- 1.13 An independent valuation of the building established a market value of £6.54 million (including VAT). Officials therefore considered that the £6.3 million purchase price negotiated by the Welsh Government in the autumn of 2013 was a good deal. The owners indicated to the Welsh Government that they were prepared to conclude the sale if contracts could be exchanged within a month.
- 1.14 The condition of the building⁹ at the time was observed and reported by the independent valuers as follows:
- 'the building appeared to be in a generally reasonable state of repair commensurate with its age and use. No urgent or significant defects or items of repair were noted which would be likely to give rise to substantial expenditure in the foreseeable future or which fall outside of the scope of the normal annual maintenance programme'.
- 1.15 In December 2013, the Minister for Education, Science and Transport approved proposals submitted by officials for the purchase of the premises by the Welsh Government for £6.3million¹⁰.

8 Welsh Government officials explained to us that leasehold interests are considered 'wasting assets', whose value would reduce over time.

9 For completeness, it can be noted that there is a large wind turbine also present within the Wentloog property which, at the time of acquisition by the Welsh Government, was subject to an existing lease to an energy supplier.

10 Together with associated professional fees of up to £30,000.

- 1.16 The submission to the Minister stated that under the Heads of Terms, the Welsh Government would invest £1.8 million (inclusive of VAT) on improving the building, matched by an £800,000 investment by Pinewood¹¹. The agreed physical works would be carried out by the Welsh Government, or alternatively by Pinewood under the supervision of the Welsh Government. Upon satisfactory completion of the works, the occupational lease would be granted to Pinewood.
- 1.17 Welsh Government officials advised the Minister that, although the Collaboration Agreement with Pinewood had not yet been signed, the purchase of the Energy Centre at Wentloog should nonetheless go ahead.
- 1.18 This presented a risk in that, if the Pinewood project did not progress, the Welsh Government neither had the skills nor the expertise internally to develop and manage an international studio facility. However, officials identified that these risks could be mitigated if needed via a range of actions. These included contracting out the management of the facility through an open-market procurement process.
- 1.19 The acquisition of the Wentloog site by the Welsh Government was completed on 7 February 2014. The precise extent of repairs and improvements needed for the building had not been agreed or finalised between the Welsh Government and Pinewood at the date of the purchase.
- 1.20 Shortly before Pinewood moved into the building, a number of water leaks became apparent, mainly in the vicinity of the rainwater gullies. The required roof repairs could have been restricted to these areas. However, in order to minimise operational and reputational risks Welsh Government officials opted to implement a more extensive scheme costing £979,000. This provided a coating for the entire roof and had the benefit of extending the life of the roof¹². In the view of Welsh Government officials, this would assist with the ongoing management of the property and would also add value should it seek to dispose of the property in the future.

¹¹ See paragraphs 3.10 and 3.11

¹² A 20-year manufacturer guarantee was provided.

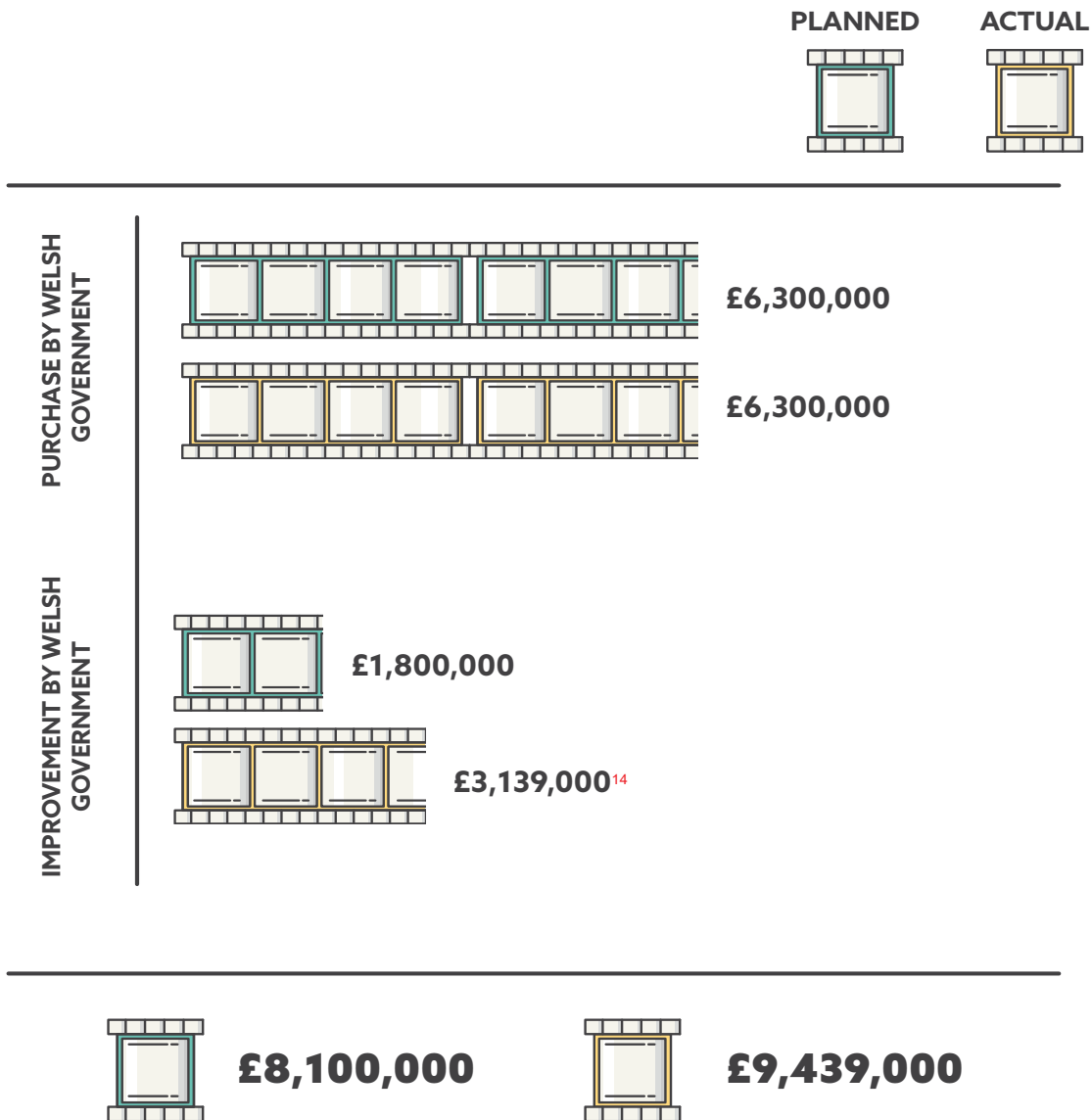
Exhibit 2: The Grade II Listed Building adjacent to Pinewood Studio Wales



Source: Wales Audit Office site visit April 2018

- 1.21 As part of the site purchase, the Welsh Government also acquired a derelict Grade II listed farmhouse located adjacent to the main building. In purchasing the farmhouse, the Welsh Government came under a statutory obligation to renovate the building at an estimated cost of £360,000 (including VAT). Welsh Government officials anticipated that, once renovated, the farmhouse could become a valuable asset that could be leased or sold, either with or separate to the main building.
- 1.22 During the lease negotiations, Welsh Government officials and Pinewood discussed whether the farmhouse should be renovated and included with the studio for ancillary-use purposes. It was eventually determined that Pinewood would only lease the industrial property. With no certain use for the farmhouse, the Welsh Government decided not to invest in the renovation works for the time being. Welsh Government officials told us that it may form part of a future project, or else be disposed of separately.

Exhibit 3: The costs incurred by the Welsh Government on the acquisition and renovation of the former Energy Centre at Wentloog¹³



Source: Welsh Government.

¹³ All figures include VAT where applicable. The Welsh Government elected to tax the building in order to recover VAT costs.

¹⁴ Composed of £1,800,000 planned improvements, £979,000 roof repairs and £360,000 office refurbishment.

The Welsh Government leased the Wentloog site to Pinewood Studio (Wales) Ltd, and agreed to contribute the majority of the funding required for its refurbishment

- 1.23 Welsh Government Ministers signed the Collaboration Agreement with Pinewood Shepperton Plc on 17 February 2014, a few days after completing the purchase of the Wentloog site. The agreement facilitated the leasing of the site to a newly-established subsidiary of Pinewood; Pinewood Studio (Wales) Ltd.
- 1.24 The lease between Welsh Government Ministers and Pinewood Studio (Wales) Ltd was not signed until 20 October 2016, although an Agreement for Lease was signed on 16 July 2014. Pinewood occupied the site and started production work from early 2015.
- 1.25 The terms agreed were for a 15-year, full repairing lease on standard letting and market terms from January 2015, with the first two years being rent-free. Under the terms of the lease, Pinewood Studio (Wales) Ltd had an option to break the lease during the fifth and eighth years of the term, upon the repayment of appropriate tenant incentives. The initial rent of £546,876 per annum was agreed to commence from 12 January 2017.
- 1.26 Over the first five-year term of the lease agreement (to January 2020), the Welsh Government expected to generate rental income of £1.6 million¹⁵ from Pinewood for the studio facility.

Pinewood Studio (Wales) Ltd was sponsored by the Welsh Government to market and promote the new film and TV studio at an annual cost of £525,600 (including VAT) over a five-year term

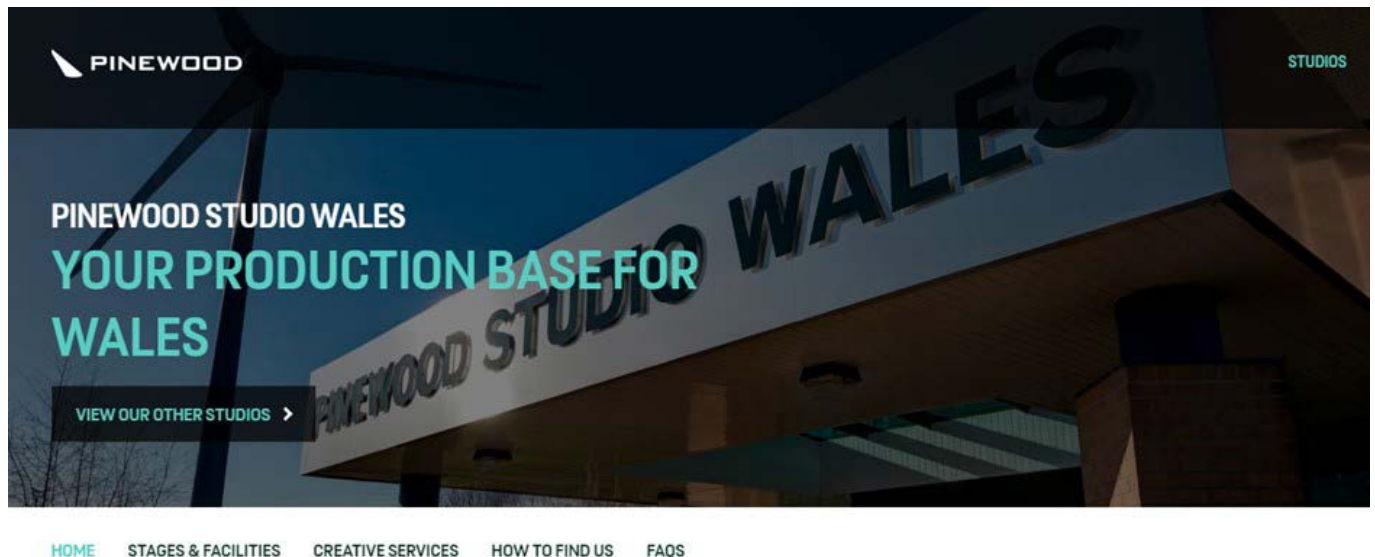
- 1.27 As part of the Collaboration Agreement signed on 17 February 2014, the Welsh Government also entered into a 'sponsorship agreement' with Pinewood Studio (Wales) Ltd at an annual cost of £438,000 for the five years from 1 March 2014 to 31 March 2019.
- 1.28 Shortly after the Collaboration Agreement was signed, Welsh Government officials recognised that VAT had been omitted from the original sponsorship agreement. The Minister's approval was therefore obtained to increase the annual sponsorship by £87,600 to £525,600. The total payable to Pinewood over the five-year sponsorship agreement would therefore be £2.63 million.

¹⁵ Being three years' rental income, following the initial two-year rent-free period.

- 1.29 The sponsorship agreement specified that the studio would be named 'Pinewood Studio Wales' and would be promoted and marketed internationally as a film and television studio, alongside other international Pinewood Group facilities¹⁶. This was expected to build on Wales' reputation as a great location in which to film and linking in to the services of the Wales Screen Commission.
- 1.30 The studio at Wentloog would be the first Pinewood-branded studio in the UK outside of south-east England. **Exhibit 4** shows how the studio is currently promoted through a dedicated website established by Pinewood.

¹⁶ Across Pinewood sales teams in London, New York and Los Angeles and at film festivals.

Exhibit 4: Home page for Pinewood Studio Wales



Source: Pinewood Studio Wales website, as at May 2018.

- 1.31 Under this agreement, Pinewood agreed not to offer branded studio facilities (other than any with its current partners or affiliates) in Scotland, Northern Ireland, Merseyside or Avon and Somerset, without the approval of the Welsh Government. The Welsh Government also agreed to sign up to a five-year exclusivity agreement not to build another studio in Wales without Pinewood's approval. This agreement placed certain restrictions on what Ministers would be able to do in the future with regard to other studios.
- 1.32 Welsh Government officials were aware that it was crucial they could justify the annual fee, given it was significantly more than the value of other sponsorship arrangements they had entered into. They were also aware that the fee should not constitute unlawful State Aid to Pinewood. Welsh Government officials satisfied themselves that the fee represented good value for money and was on market terms. They concluded that these arrangements would provide mitigation against the risk of any legal challenge.

The Welsh Government established a £30 million budget to invest in film and TV production, and appointed Pinewood Film Advisors (Wales) Ltd to identify projects suitable for investment

- 1.33 As part of the Collaboration Agreement, the Welsh Government committed to create a £30 million film and TV investment budget. This Media Investment Budget would be managed by Pinewood Film Advisors (Wales) Ltd on behalf of the Welsh Government. It would operate on a pilot basis, initially for five years, and be subject to an interim review after 18 months.
- 1.34 The Media Investment Budget would be used to finance the development, production and distribution of filmed entertainment projects or any other media projects submitted to the Welsh Government by Pinewood Film Advisors (Wales) Ltd. The Welsh Government expected to benefit from its collaboration with Pinewood because of its sector expertise, knowledge and networks, and experience of collaborating in a similar arrangement in the Isle of Man.
- 1.35 The Welsh Government intended to recoup its investments through repayments of loans and returns on equity, and for those income streams to be reinvested in further production projects. This had the potential to create a self-renewing or 'evergreen' fund. Officials anticipated that the Media Investment Budget would invest between £12 million and £15 million per year¹⁷.
- 1.36 Pinewood Film Advisors (Wales) Ltd did not receive funding from the Welsh Government for undertaking this management role. However, under the Collaboration Agreement it would be able to generate revenues from the businesses making productions funded from the Media Investment Budget, to include:
- Pinewood could negotiate production/arrangement fees with the production company, which should be included in the production budget and paid by the production company.
 - Pinewood could receive distribution fees and/or costs when the acquisition of UK distribution rights was included in the approval. These fees and costs would be receivable by Pinewood from the collected receipts from the distribution rights, with no recourse to the Welsh Government for payment.
 - Pinewood could also, at its discretion, invest its own funds into these productions.

¹⁷ Investments would be made between 1 April 2014 and 31 March 2019. All supported production and post-production activity would need to be completed by 31 March 2020.

- 1.37 The Media Investment Budget and Pinewood Studio Wales were officially launched at an event in Cardiff on 17 February 2014.
- 1.38 **Exhibit 5**, taken from Pinewood Studio Wales' website as at July 2017, summarises Pinewood's promotion of the Welsh Government's Media Investment Budget.

Exhibit 5: Pinewood's promotion of the Welsh Government's Media Investment Budget

Key considerations of the Welsh Government's Media Investment Budget:

- Production must be able to shoot 50% of principal photography in Wales;
- Pinewood Pictures and Wales Screen can provide information on shooting in Wales. For an overview, please go to www.wallesscreen.com;
- In addition, Pinewood's own studio facility in Cardiff is available for film and TV productions:
 - Including 2 sound-treated stages at 20,000 sq ft each and an additional 30,000 sq ft of shooting floor;
 - 70,000 sq ft of mixed use production space, including production accommodation and modern, flexible offices and amenities;
 - Close proximity to central Cardiff and a variety of **stunning locations**;
 - For more information please go to www.pinewoodstudiowales.com.

Previous projects include TAKE DOWN, DON'T KNOCK TWICE, and THEIR FINEST HOUR AND A HALF.

Source: Pinewood Studio Wales website as at July 2017.

- 1.39 There are seven types of investment that the Welsh Government is able to make into productions via the Media Investment Budget. Projects can use just one type of funding, or a combination of them. On occasion, the Welsh Government can opt to provide grant funding alongside the commercial investment funding. However, each type of investment attracts different timescales and risks, as shown in **Exhibit 6**. **Appendix 4** contains more details about each type of investment.

Exhibit 6: The seven types of investment that can be made via the Media Investment Budget

| TYPE OF INVESTMENT | DESCRIPTION | TIMESCALE |
|-----------------------------------|---|--|
| Tax Credit | Cash advances against the tax credits the production is eligible for | Usually within 12 months of production being completed |
| Pre Sales | Cash advances against sales already made to distributors | Within six months of the final cut being approved |
| Gap | Commitment against unsold sales territories based on sales estimates | When sales begin, following sales screenings after the final cut is approved |
| Mezzanine | Funding based on the film receiving higher sales than estimated | Close to or following the production's release |
| Equity | Final investments repaid, requiring the production to sell well to distributors | After all other funding has been fully repaid |
| Repayable Business Finance | Discretionary financial support on a repayable or non-repayable basis | Pinewood advised on when funding can be recouped if repayable |
| Development Funding | Funding for the development stage of a project, repaid if the project enters production | Repaid on the first day of principal photography |

 **LOW RISK**
 **MEDIUM RISK**
 **HIGH RISK**

Source: compiled by the Wales Audit Office from information held by the Welsh Government.

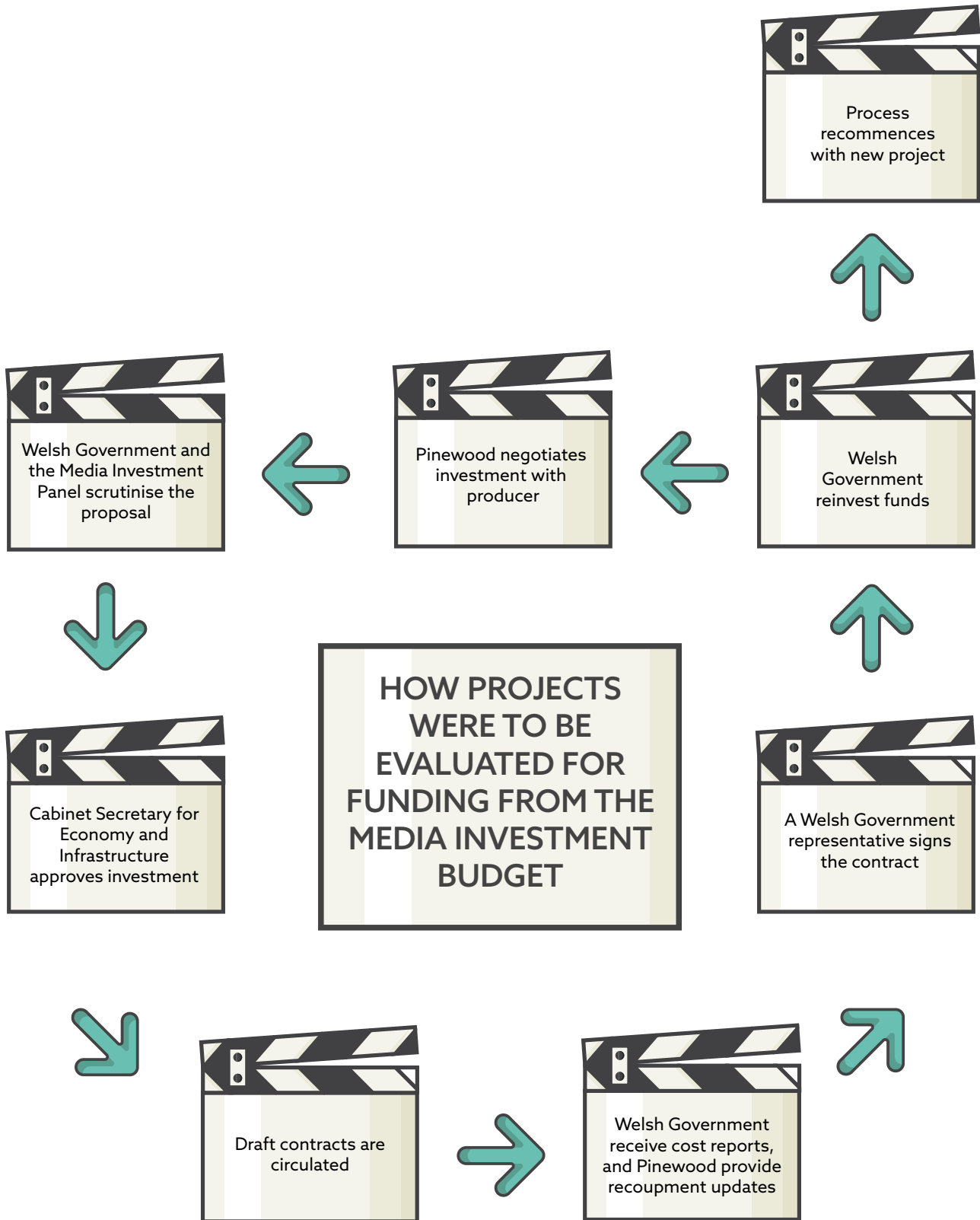
Part 2 – Operation of the Collaboration Agreement until October 2017

The Welsh Government established an independent Media Investment Panel to decide which projects put forward by Pinewood should be supported by the investment budget

- 2.1 The Welsh Government anticipated that its Media Investment Budget would normally only invest in projects costing over £1 million to produce. The Minister for Economy, Science and Transport approved the establishment of a private-sector-led Media Investment Panel which would provide the required expertise to scrutinise and approve these projects. The Media Investment Panel would be set up as a task and finish group for an initial period of 18 months, and would be chaired by an industry expert¹⁸.
- 2.2 The Media Investment Panel was established in April 2014 as a publicly appointed panel of sector experts.
- 2.3 Welsh Government officials would also undertake independent due diligence reviews of all proposed projects, and would be responsible for undertaking compliance reviews to ensure funding terms and conditions were being met. In particular:
 - at least 50% of production must be shot in Wales;
 - 35 to 40% of 'below the line' production budget must be spent on Welsh production expenditure; and
 - the Welsh Government would share in the commercial upside from film and TV productions.
- 2.4 **Exhibit 7** summarises how projects were to be evaluated for funding from the Media Investment Budget.

¹⁸ With appropriate arrangements being put in place to manage any actual or perceived conflicts of interest.

Exhibit 7: how projects were to be evaluated for funding from the Media Investment Budget



Source: compiled by the Wales Audit Office based on information held by the Welsh Government.

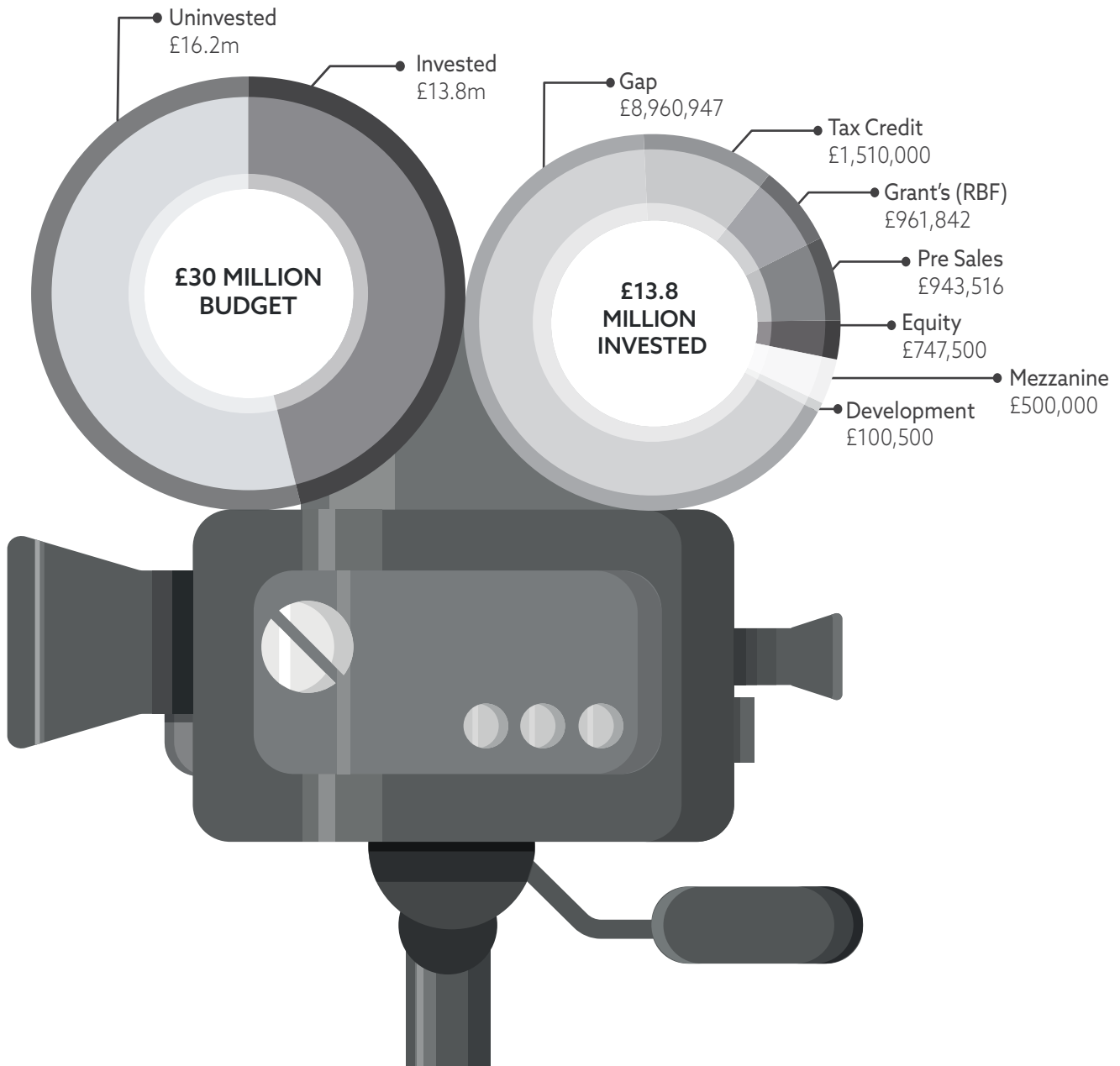
The Media Investment Budget's performance did not meet the panel's expectations

- 2.5 By summer 2016, members of the Media Investment Panel and Creative Industries Sector Panel had become dissatisfied with the performance of the Media Investment Budget. The Chair of the Creative Industries Sector Panel accordingly advised Welsh Government officials that the budget should be opened up and made non-exclusive to Pinewood.
- 2.6 Welsh Government officials wrote to the Cabinet Secretary for Economy and Infrastructure in August 2016, setting out the following concerns that they had about the budget's performance:
- a greater number of higher-risk investments being put forward by Pinewood, because productions could obtain lower-risk funding from other sources without the requirement to be filmed in Wales;
 - Pinewood's operating model meant it was reluctant to invest its own money in these higher-risk projects alongside the Welsh Government; and
 - Pinewood might be conflicted in its involvement with the budget as it also had an interest (not prohibited under the Collaboration Agreement) in providing its own London-based services to the industry. Welsh Government officials felt that a perception had arisen amongst other companies that Pinewood had an unfair competitive advantage in securing post-production work in Wales. They therefore considered that this had the potential to reduce the economic benefits to Wales.
- 2.7 On 2 November 2016, Welsh Government officials wrote to Pinewood to set out issues with the Media Investment Budget and the Collaboration Agreement. Two issues were of particular concern to them:
- **Compliance** – there was a perceived lack of transparency regarding the extent of wider Pinewood Group involvement in productions. This perceived lack of transparency had exacerbated concerns about the financial advantage Pinewood may have had over other companies through its exclusive access to the Media Investment Budget¹⁹.
 - **Contract Performance** – the original business plan had estimated an overall Welsh spend figure of £90 million, which represented a leverage ratio of 1:3 in terms of public to private funding. According to Welsh Government officials, at this time the actual ratio was 1:1, significantly reducing the potential for the Media Investment Budget to become self-funding.

¹⁹ The risk that this perception might be created was either not identified or considered immaterial by Welsh Government officials at the time of the February 2014 submission to the Minister that had recommended approval of the Collaboration Agreement, as the submission paper is silent on this point.

- 2.8 We questioned Pinewood executives about these concerns. Pinewood told us that they did not recognise the rationale for the Welsh Government's expressed concern about Pinewood's perceived reluctance to invest in projects alongside the Welsh Government, and stated that they had done so for nine projects. Pinewood noted that it was yet to recoup any of its investment in two of these projects. By investing in projects such as 'Show Dogs', Pinewood had enabled these projects to close financing while shooting in Wales. In the case of 'The Collection', Pinewood considers that the offer of funding from the Welsh Government alone would not have been sufficient to relocate the shoot away from Yorkshire. In Pinewood's view, their own investment in that project had tipped the funding balance to move the production to Wales.
- 2.9 Pinewood executives also assured us that they had addressed the Welsh Government's expressed concern about compliance by confirming to them that productions were entirely free to choose either to accept Pinewood's post-investment proposal to provide production services or else to make their own separate arrangements to use another company instead. As examples of this, Pinewood cited to us the producers of 'Journey's End', who had decided to use a post-production house independent of Pinewood and not based in Wales. Similarly, the producers of 'The Collection' had opted to use another non-Pinewood studio for their stage and backstage filming.
- 2.10 As regards the Welsh Government's concern about contract performance, Pinewood executives told us that their records reflect an approximate 1:6 funding to spend ratio on projected recoupment.
- 2.11 We have established that Pinewood Film Advisors (Wales) Ltd has generated a total of £1,180,421 in production/arrangement fees from productions funded by the Media Investment Budget. As noted above, any additional income generated by the company from the provision of post-production services has been derived from open competition, rather than the provision of taxpayer-funded support. We have therefore not included that revenue stream within the scope of our audit examination. We note that the published accounts of Pinewood Film Advisors (Wales) Ltd disclose a retained loss of £320,000 on the company's activities at the year ending 31 March 2017.
- 2.12 The latest available figures provided to us by the Welsh Government show that £13.8 million of the £30 million budget has been invested across 14 projects. **Exhibit 8** analyses the £13.8 million over the seven types of investment vehicle available to the Media Investment Budget.

Exhibit 8: investments made from the Media Investment Budget²⁰



Source: information held by the Welsh Government.

²⁰ This diagram includes all projects funded by the Media Investment Budget (to May 2018), including those sourced by Pinewood and those subsequently sourced under the Welsh Government's management. See Appendix 5 for further details.

2.13 Welsh Government figures show that a total of £4.3 million has been recouped so far, from five of the 14 projects supported:

- one project has recouped more than its original investment;
- four projects have recouped some of the original investment; and
- nine projects have not yet recouped any of the original investment.

These projects are in various stages of development. Some projects have not yet benefitted from international cinematic release or TV broadcast and funds will continue to be recouped through auxiliary sales.

2.14 **Appendix 5** shows further details of the productions supported and their recoupment.

Pinewood Studios Wales Ltd was unable to operate the studio as a going concern without the support of Pinewood Group Limited

2.15 Between November 2016 and October 2017, negotiations took place between Pinewood and the Welsh Government, focussing on:

- changes to the role of Pinewood in the Media Investment Budget; and
- Pinewood's management of Pinewood Studio Wales, which was not fully occupied and had become loss-making for Pinewood²¹.

From 25 June 2017, Welsh Government agreed that Pinewood's obligation to pay rent for the Wentloog facilities would be suspended, pending finalisation of the negotiations²².

2.16 During this period, there was a change in ownership and leadership at Pinewood²³. In discussions between Welsh Government officials and the new Pinewood executives, it became apparent that there was a shared desire to agree a new operating model for the studio.

21 Although by September of 2016 Pinewood had successfully staged six productions and licensed business space at the studio for 20 companies, the level of occupation by film-production companies had not reached the level originally expected.

22 As noted in paragraph 3.8, all unpaid rents were subsequently settled in full as part of the renegotiation of the agreement.

23 Pinewood Shepperton Plc was sold to Venus Grafton Sarl in October 2016.

- 2.17 In 2017, Pinewood management decided to end activities relating to fund management, investment advisory services to third party funds and investment of its own funds in film and television productions. This decision was taken as these activities did not represent Pinewood's core offerings, nor did they represent a significant proportion of its turnover.
- 2.18 As the Collaboration Agreement was contractually linked to the lease of the studio, the termination of the Collaboration Agreement allowed Pinewood to terminate the lease early.
- 2.19 We met with the Chairman and Acting Chief Executive of Pinewood, together with the company's Corporate Affairs Director on 16 April 2018. They told us that the opening in May 2017 of a new film and TV production studio by Bad Wolf in Trident Park, Cardiff, had in their view a detrimental impact on the occupancy of Pinewood Studio Wales, and that the number of enquiries they received had consequently fallen.
- 2.20 Bad Wolf Studios Ltd has benefited from a £9 million funding package from the Welsh Government. The funding is structured based on an initial repayable loan of £4.5 million, which can be converted into a grant as soon as performance milestones are achieved within a 10-year period. These milestones relate to both the profitability of the company and the amount of production spend that is generated within the Welsh economy as a result. The remaining balance of £4.5 million is payable as a grant, subject to achievement of additional production spend targets. In addition, the Welsh Government leases to Bad Wolf Studios Ltd, on commercial terms, the Wolf Studios Wales facility in Cardiff Bay.
- 2.21 Unlike Pinewood Studio Wales, which has a maximum eave height of 25 feet²⁴, Wolf Studios Wales is the only facility in Wales able to offer a stage space with an eave height of 57 feet. This eave height was referred to in a Welsh Government press release on 15 May 2017 which promoted Wolf Studios Wales as 'an attractive proposition for high end television productions and big budget feature films from around the world'.

²⁴ The maximum eave height of 25 feet is recognised by both Welsh Government and Pinewood to be a factor that can limit the suitability of the studio to certain types of productions.

- 2.22 Welsh Government officials told us that demand for studio facilities will fluctuate as productions come and go but that, in their view, demand for the Wentloog site was affected by a change of focus after the change in ownership at Pinewood. They do not believe there has been a drop in enquiries for Pinewood since Wolf Studios Wales opened its doors. In contrast, Pinewood executives told us that Pinewood's focus remains the selling of space at studio facilities, and that it is Pinewood's expertise in this field that the Welsh Government has sought to retain under the new Management Services Agreement (covered in [Part 3](#) of this report). Pinewood also told us that demand for other Pinewood studios in the UK remains strong.
- 2.23 According to Welsh Government officials Wales Screen has conducted ten studio visits with major productions in the last 12 months. Pinewood was not included on only two of these occasions and both were a result of producer choice. To date, Wolf Studios Wales has only been home to Bad Wolf productions, many of which required the higher maximum eave height, whereas Pinewood has had productions from the BBC, Channel 4 and independent film companies.
- 2.24 Welsh Government officials emphasised to us that Wales Screen continues to equally promote Pinewood Studios Wales, Wolf Studios Wales and other studios in Wales. In the Welsh Government's view, a high level of demand for the Pinewood studio facilities is likely to continue into the autumn. However, Pinewood executives told us that they believe that the opening of a competing studio has impacted on demand for space at the Wentloog site and that equal promotion by Wales Screen does not address this.

Part 3 – The revised management arrangements from November 2017

In October 2017, the Welsh Government terminated its Lease and Collaboration Agreements with Pinewood, and Pinewood ceased to manage the Media Investment Budget

- 3.1 In the light of the position described in Part 2 of this report, Welsh Government officials provided formal advice to the Cabinet Secretary for Economy and Transport on 29 September 2017 and requested his approval to:
 - terminate the Collaboration Agreement with Pinewood;
 - terminate the existing occupational lease agreement of the studio to Pinewood on 31 October 2017; and
 - put the Media Investment Budget on hold.
- 3.2 On the advice of the Creative Industries Sector Panel and Media Investment Panel, the Media Investment Budget subsequently came under the management of Welsh Government officials.
- 3.3 In the meantime, negotiations continued with Pinewood to introduce a new studio management agreement by the lease termination date of 31 October 2017.

In November 2017, the Welsh Government entered into a new three-year ‘management services agreement’ with Pinewood Studios Wales Ltd

- 3.4 Welsh Government officials took advice from independent experts on the drafting of a new operating model for Pinewood Studio Wales. Pinewood had committed to acting in good faith to negotiate a new deal that could be signed by the termination date of the Collaboration Agreement and lease.
- 3.5 A new ‘Management Services Agreement’ was put to the Cabinet Secretary for Economy and Infrastructure by his officials on 30 October 2017. It contains two complementary parts:
 - the sales and marketing of the studio; and
 - its operation and management.

- 3.6 Under the terms of the new agreement, Pinewood would continue to operate the studio on behalf of the Welsh Government. The Welsh Government could terminate the agreement on six months' notice at any time after the first anniversary of the agreement, which commenced on 1 November 2017. Pinewood would also continue to promote Wales as a centre of excellence for TV drama and film.
- 3.7 Under the agreement, the costs of running the facility, together with payment of a Pinewood management fee, would now be met in full by the Welsh Government. In return, all revenues received by Pinewood for promoting and licensing the studio would be retained by the Welsh Government. These would off-set the operational costs of the building. Any profits generated from the operation of the studio would rest with the Welsh Government.
- 3.8 All outstanding financial commitments such as unpaid rents would be settled in full as part of the termination arrangements.
- 3.9 The key elements associated with terminating the Collaboration Agreement and moving forward with a new Management Services Agreement as reflected in Ministerial Advice are summarised in [Exhibit 9](#).

Exhibit 9: key elements associated with terminating the Collaboration Agreement and moving forward with a new Management Services Agreement

| The Welsh Government would: | Pinewood would: |
|--|--|
| Incur the annual costs of managing the property (including facilities management, rates and insurance) | Receive an annual management fee from the Welsh Government. |
| Acquire the value of all tenant's improvements to the Wentloog facilities. | Receive reimbursement by the Welsh Government of its production services costs (subject to an annual cap). |
| Retain all future revenues generated by the studio. | Receive a compensation payment from the Welsh Government for rental payments made during the renegotiation period. |
| Contract directly with licensed occupiers of the offices and production companies which hire the studio space. | |

Source: information held by the Welsh Government.

3.10 The Ministerial Advice prepared by Welsh Government officials dealing with the termination of the existing contracts (Collaboration Agreement and Lease) stated that Pinewood had carried out works and investments in equipment at around £800,000. It went on to say that the termination agreement would contain a narrative that the benefit of any modifications to the building made by Pinewood (tenant's improvements) would remain in place and become the property of Welsh Government. However, Welsh Government officials have told us they do not have a schedule of the tenant's improvements that have been completed to date and that have now been acquired by the Welsh Government.

- 3.11 Pinewood executives told us that there were discussions prior to the original contracts around the contribution they would make to the studio. They stated that the Heads of Terms (which were subject to contract) provided that the Welsh Government would do the fit out works and that Pinewood would make a contribution of £800,000²⁵ or Pinewood would complete the fit out works and Welsh Government would contribute £1.8 million (including VAT) towards the cost. They went on to say that the Agreement to Lease makes no reference to the £800,000 but does specify the works the tenant is required to undertake and requires the Welsh Government to contribute £1.8 million.
- 3.12 The Cabinet Secretary for Economy and Infrastructure approved the termination of the existing contracts and the new management services agreement came into effect on 1 November 2017, for a period of three years.
- 3.13 Under the terms of the Management Services Agreement, there is a net annual cost to the Welsh Government, as shown in [Exhibit 10](#). One of the cost components, the annual management fee payable to Pinewood, has been redacted from this report at the request of Pinewood²⁶. The net annual cost is therefore shown as £392,000, plus the annual management fee.

²⁵ Over the 15 year term of the lease.

²⁶ The Auditor General has accepted Pinewood's contention that placing this information in the public domain would be likely to cause substantial harm to the commercial interests of Pinewood by giving its customers, competitors and suppliers an unfair advantage in future price negotiations.

Exhibit 10: The annual net cost to the Welsh Government of operating the management services agreement²⁷

| | £ |
|--|----------------|
| Annual studio running costs | 890,000 |
| Reimbursement of Pinewood production costs | 216,000 |
| Less: Projected studio revenues | (714,000) |
| Net annual operating cost before management fee | 392,000 |
| Plus: Management fee payable to Pinewood | [redacted] |
| Net annual operating cost | [redacted] |

- 3.14 The annual studio revenue forecast of £714,000 was supplied to Welsh Government officials by Pinewood, and was then included in the submission to the Cabinet Secretary. The net operating cost totals in Exhibit 10 assume that this figure is realistic. Welsh Government officials told us that the reliability of the forecasts were tested and scrutinised by officials and also by independent property advisors. However when the figure was provided, Pinewood added the caveat that revenues could be lower due to increased competition from Wolf Studios.
- 3.15 Welsh Government officials recognise that these financial projections do not represent good value for money. However, in their view it was better to enter into a three-year agreement with Pinewood with the prospect of generating some commercial revenues, when set against the costs of simply leaving the site empty whilst they searched for a new tenant.

²⁷ The figures in this exhibit are inclusive of VAT, where applicable. The recoverability of some VAT elements may slightly improve the overall out-turn, but this is unlikely to be material.

3.16 In a briefing to the Cabinet Secretary for Economy and Infrastructure on 29 October 2017, Welsh Government officials stated that if a new agreement with Pinewood was not entered into, then the Welsh Government would incur annual property holding costs of around £890,000 (including VAT), and could expect only around £124,000 of annual income from the letting of office space. If these estimates were accurate, then the likely net annual cost to the Welsh Government under that alternative scenario would have been £766,000.

Appendix 1 – Our audit approach and methods

Scope

The scope of this report is confined to our examination of the agreements entered into by the Welsh Government and Pinewood subsidiaries between 2014 and 2017. Specifically we have looked at:

- the acquisition of the former Energy Centre at Wentloog, Cardiff in February 2014;
- the Collaboration Agreement between the Welsh Government and Pinewood Film Advisors Wales Ltd dated 17 February 2014; and
- the Management Services Agreement between the Welsh Government and Pinewood Studio Wales Ltd on 1 November 2017.

We have also examined the governance arrangements in place for the Welsh Government's Media Investment Budget. However, we have not considered the value for money of the Media Investment Budget as a whole, reviewed any individual projects benefitting from the budget or examined the Welsh Government's arrangements for monitoring compliance with the terms and conditions of funding.

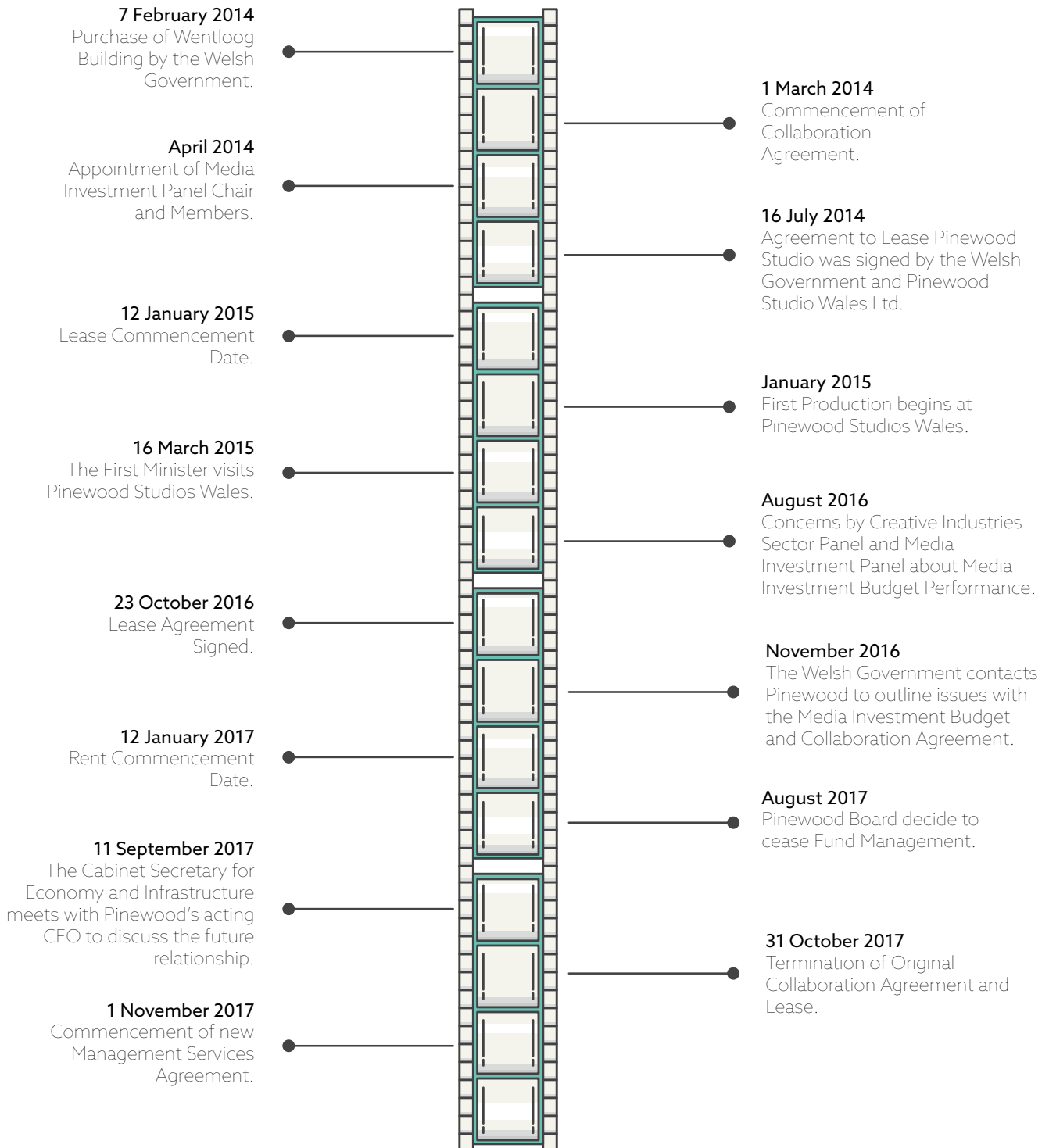
Our report is made on a 'facts only' basis, and we have not therefore drawn conclusions or made recommendations arising from our audit work.

Methods

In undertaking the review we:

- reviewed documentary evidence provided from the Welsh Government and made further enquiries of Welsh Government officials based on our review of the key documents;
- undertook a site visit to Pinewood Studio Wales and met with executives from Pinewood Group Limited; and
- prior to publication, we agreed the factual accuracy of our report with the Welsh Government and the named third parties.

Appendix 2 – Timeline of events



Appendix 3 – The Welsh Government’s overall approach to promoting Wales as a venue to produce high-impact film and TV productions

The Welsh Government uses several methods and organisations in order to encourage producers to choose Wales as a venue.

Financial and Strategic Support

The Welsh Government has given support to both Pinewood Studios and Wolf Studios for the establishment of studio space within Wales.

Creative industries in Wales are also able to access Welsh Government Repayable Business Finance (including the Wales Screen Fund) and the Wales Economic Growth Fund.

Media Investment Budget

£30 million of commercial funding for TV and film productions.

£13.8 million of funding has been awarded to date.

Wales Screen

A team based within the Welsh Government’s Creative Industries sector.

Wales Screen provides a free service to support film and TV productions through location scouting, logistical arrangements and assistance sourcing crew and facility companies.

Sky Vision Fund

The Welsh Government has invested £200,000 in conjunction with Sky Vision to fund new factual and entertainment programmes.

Development, pilot and top-up funding is available, the Welsh Government portion of which is non-repayable.

Funding is available for independent production companies based in Wales and UK-based companies producing shows in Wales.

Promotion of Wales by Pinewood

Originally, Pinewood were sponsored to promote Pinewood Studios Wales and Wales in general as a location for filming and post-production.

Under the revised agreement, Pinewood is paid to promote Pinewood Studios Wales.

The agreement details that promotion should be through film festivals, television markets and sales teams.

Appendix 4 – The seven types of investment that the Welsh Government can make in TV and film productions

Tax credit

Films with a budget under £20 million can claim 25% of UK expenditure as a tax credit. Films with a budget over £20 million can receive 25% of the first £20 million and 20% of any additional expenditure. Tax credit investments involve advancing funds to the production for the tax credit which will be received. These investments are therefore seen as the safest type of investment that can be made as the prospect of recoverability is high. The money is usually guaranteed to be returned in full within 12 months of production being completed.

Pre sales

Pre sales are made to distributors in advance of the film being made. Pre-sales investments are similar to tax-credit investments as they involve advancing cash against confirmed figures for sales already made. This means that the investments are almost always recouped in full within six months of the final cut being approved. There is therefore a high prospect of recoverability from the investments.

Gap funding

Gap funding is committed against unsold territories and based on sales estimates provided by the sales agent. Pinewood would assess the sales agent's estimates and produce a 'cover' figure, which would be based on a low number of sales with associated fees subtracted. This results in a safe figure which should be at least partially recouped unless the production was a flop and there was little or no take up of the film. The prospect of recoverability is therefore medium. Recoupment would occur when sales are made after the final cut is approved.

Mezzanine

Mezzanine funding is based on productions achieving higher sales than the low estimates used for gap finance. Higher sales could be due to the production having a well-known cast or a sales agent who has a reputation for delivering strong sales. As the investment is based on exceeding the safe figure, the prospect of recoverability is low and would involve a higher premium. Recoupment would begin after all of the above financing has been recouped, normally close to or following the production's release.

Equity

Equity funding is the highest-risk financing available under the Media Investment Budget, as equity investments are usually the last production finance recouped. The production needs to sell well and fully recoup its other investments for equity investors to receive a return. The prospect of recoverability is low, and will involve high premiums.

Business Finance

Repayable Business Finance is discretionary financial support to eligible businesses to fund capital investment and job-creation projects. Support is available to eligible film and TV productions at a negotiated level. The support must be below state-aid ceilings and must be the minimum required for the project to proceed. Funding for mobile projects, where the project could be undertaken in another country, is non-repayable and funding for non-mobile projects is 100% repayable. Although the level of risk for productions will be individually assessed, overall the prospect of recoverability is low.

Development funding

Development funding finances the development of productions, prior to commission. As part of the development deal, the Welsh Government are assigned 50% of development materials and copyright which would be re-assigned to the production on repayment of the funding. They are also given the option to provide full production funding, if they wish. The Welsh Government also receive a 50% premium on their investment, which is repaid on the first day of principal photography. The prospect of recoverability is low, due to the number of productions which never progress from development to commission.

Appendix 5 – Productions supported by the Media Investment Budget, 2014-2018

These tables include the individual loans investments, the funding recouped (banked) to 31 May 2018 and the balance of each project that has been supported by the Media Investment Budget.

These figures were provided by the Welsh Government in June 2018, and it should be noted that the projects are in various stages of development. Some projects have not yet benefitted from international cinematic release or TV broadcast, and funds will continue to be recouped through auxiliary sales.

Pinewood have also provided us with their own analysis, although there are some small timing differences in the recoupment values, the largest being in respect of The Collection, which they show as having recouped £192,631.

The Media Investment Budget was managed by Pinewood until September 2017, and has subsequently been managed by the Welsh Government.

Exhibit 11: projects funded by the Media Investment Budget under the management of Pinewood (February 2014 to September 2017)

| Project | Investment Value (£) | Amount Recouped to May 2018 (£) | Net Gain/(Loss) to Date (£) |
|---------------------------------|-------------------------|---------------------------------|-----------------------------|
| Take Down | 3,144,000 | 959,824 | (2,184,176) |
| Their Finest | 2,000,000 | 2,049,985 | 49,985 |
| The Collection | 1,750,000 ²⁸ | 119,075 | (1,630,925) |
| Show Dogs | 1,565,789 ²⁹ | 0 | (1,565,789) |
| Journey's End | 850,000 | 630,860 | (219,140) |
| Don't Knock Twice ³⁰ | 629,516 | 496,064 | (133,452) |
| Minotaur | 25,500 | 0 | (25,500) |
| Lionel the First | 25,000 | 0 | (25,000) |
| Jack Staff | 25,000 | 0 | (25,000) |
| Total | 10,014,805 | 4,255,808 | (5,758,997) |

²⁸ The investment value includes £600,000 of grant funding from the Media Investment Budget.

²⁹ The investment value includes £361,842 of grant funding from the Media Investment Budget.

³⁰ Don't Knock Twice also received £75,000 of grant funding under the Welsh Government's Business Finance scheme.

Exhibit 12: projects funded by the Media Investment Budget under the management of the Welsh Government (September 2017 onwards)

| Project | Investment Value (£) | Amount Recouped to May 2018 (£) | Net Gain/(Loss) to Date (£) |
|-------------------------|----------------------|---------------------------------|-----------------------------|
| Trampires ³¹ | 2,000,000 | 0 | (2,000,000) |
| Eternal Beauty | 1,050,000 | 0 | (1,050,000) |
| Bang | 350,000 | 0 | (350,000) |
| Tiny Rebel | 317,500 | 0 | (317,500) |
| Goose Green | 25,000 | 0 | (25,000) |
| Total | 3,742,500 | 0 | (3,742,500) |

Exhibit 13: overall Media Investment Budget Investments

| | Investment Value (£) | Amount Recouped to May 2018 (£) | Net Gain/(Loss) to Date (£) |
|--------|----------------------|---------------------------------|-----------------------------|
| Total: | 13,757,305 | 4,255,808 | (9,501,497) |

31 Trampires also received £52,572 of grant funding under the Welsh Government's Business Finance scheme.

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Nick Ramsay AM

Chair, Public Accounts Committee
National Assembly for Wales

28 September 2018

Dear Nick

Auditor General's Report – The Welsh Government's relationship with Pinewood

You will be aware that the Auditor General recently published a facts-only report looking at The Welsh Government's relationship with Pinewood. This followed interest in the matter from a number of Assembly Members over a period of years, who had asked the Welsh Government for information explaining the nature of the relationship.

Background

In 2014, the Welsh Government purchased the former Energy Centre site at Wentloog to develop as a film and TV studio in collaboration with Pinewood Shepperton Plc. Shortly afterwards, Welsh Government Ministers entered into a 'Collaboration Agreement' with two newly established subsidiary companies of Pinewood. The agreement involved the Welsh Government:

- leasing the Wentloog studio to Pinewood;
- establishing a £30 million Media Investment Budget (for which Pinewood would source productions suitable for Welsh Government investment); and
- sponsoring Pinewood to market and promote both the studio and the investment budget.

The Welsh Government and Pinewood entered into a new 'Management Services Agreement' on 1 November 2017.

This new agreement contains two parts; the sales and marketing of the studio and the studio operation and management services. The Media Investment Budget is now being managed by Welsh Government officials. The annual net cost to the Welsh Government of the management services agreement is estimated to be £392,000 (plus an additional annual management fee to Pinewood, which has been redacted from the WAO report on the grounds of commercial sensitivity).

Welsh Government officials acknowledge that the current financial projections for this relationship do not represent good value for money. However, in their view it was more financially advantageous to enter into a new three-year agreement with Pinewood with the prospect of generating some commercial revenues, compared to the costs that the Welsh Government would have incurred by leaving the site empty whilst they searched for a new tenant.

When the report was published the Culture, Welsh Language and Communications Committee was nearing the end of its inquiry into film and major television production. The Welsh Government's relationship with Pinewood is a key part of its support for this industry. As such, when the WAO report was published, the Committee was keen to pursue the issues it raised with the Welsh Government, the chair of the Welsh Government's Creative Industries Sector Panel (Mr Ron Jones) and Pinewood themselves.

Accordingly, the Committee has taken oral evidence from Mr Jones, the Cabinet Secretary for Economy and Transport (Ken Skates AM), the Minister for Culture and Sport (Dafydd Elis-Thomas AM) and Welsh Government officials. These sessions took place on 20 June 2018 and 12 July 2018. As Pinewood were not able to attend a meeting before the summer recess, the Committee has written to them with a number of questions.

The Committee also received a private briefing from WAO officials at our meeting on 28 June, which was attended by Lee Waters AM as a Member of PAC. Adam Price AM was also able to attend our meeting on 12 July as a Member of PAC and was able to put some questions direct to Ministers and officials.

The Committee has looked at the Welsh Government's relationship with Pinewood as a key component of the Welsh Government's support for the screen industry. It will be reporting on the relationship in this light in the autumn. However, the WAO report, and



the subsequent evidence the Committee has received, raise a number of areas of concern that it thinks merit further scrutiny by the Public Accounts Committee. These concerns include:

- **Transparency:** the Welsh Government has refused on a number of occasions, following questions from individual Assembly Members, to disclose details of its relationship with Pinewood or to respond on the relationship and in particular its measurable benefits, citing commercial sensitivity. However, the WAO's report – which has been agreed by both the Welsh Government and Pinewood – only omits the value of the management fee that the Welsh Government is currently paying Pinewood. In the Committee's view, there was a strong public interest in disclosing as much detail of the relationship as possible. While we accept that commercial sensitivity is important, the fact that both the Welsh Government and Pinewood now accept that much of what was previously considered confidential can now be released, seems to demonstrate that greater efforts toward transparency should have been made earlier. The Committee has considerable concerns that, despite requests for information from various Assembly Members had it not been for the WAO report, this information would still not be in the public domain, and Assembly Members and the Welsh public would still be in the dark about the full nature of this relationship.
- **Nature of the property:** following the Welsh Government's acquisition of the old Energy Centre, it needed to undertake urgent repairs to the leaking roof, which cost £979,000. The Committee heard on 12 July that these were not identified before purchase, as the Welsh Government did not conduct a full building survey, just a valuation. This valuation report stated "No urgent or significant defects or items of repair were noted which would be likely to give rise to substantial expenditure in the foreseeable future". The Committee is surprised that the purchase of a property valued at over £6m was not subject to a more comprehensive building survey, which we would expect to be common practice on a purchase of this value. The Committee is not satisfied with the Government's response on this point.
- **Sponsorship arrangement:** as part of the original Collaboration Agreement, the Welsh Government also entered into a 'sponsorship agreement' with Pinewood



Studio (Wales) Ltd at an annual cost of £438,000 for the five years from March 2014 to March 2019. Shortly after the Collaboration Agreement was signed, Welsh Government officials recognised that VAT had been omitted from the original sponsorship agreement, so annual payments rose to £525,000. Both this error and the unforeseen roof repairs mentioned above give concerns about the degree of due diligence during this work. In particular, it is difficult to understand how the VAT implications could not have been understood if specialist advice was received.

- **Media Investment Budget:** Under the original collaboration agreement, Pinewood managed the Media Investment Budget (MIB) on behalf of the Welsh Government. This fund has underperformed against forecasts, both in terms of how much the Welsh Government has invested, and how much spend this has stimulated in the Welsh economy. The Welsh Government is still receiving returns on this investment, but initial receipts do not look promising. Pinewood has been involved in a similar fund on the Isle of Man: it is not currently clear the extent to which this fund's performance should have caused Welsh Government officials to have concerns about Pinewood's involvement in a similar fund in Wales.
- **Conflict of interest:** In August 2016 Welsh Government officials wrote to the Cabinet Secretary for Economy and Infrastructure setting out concerns with the MIB's performance, including that "Pinewood might be conflicted in its involvement with the budget as it also had an interest (not prohibited under the Collaboration Agreement) in providing its own London-based services to the industry". The Committee has received somewhat conflicting evidence on the extent to which this issue was covered under the original agreement. When asked on 20 June why the Welsh Government had not identified the possible conflict of interest at the outset of the relationship with Pinewood, a Welsh Government official said:

"...a conflict of interest was covered in the original agreement".

This assertion does not seem to be supported by the WAO report. This states that Pinewood's provision of London-based services to the industry was "not prohibited under the Collaboration Agreement". Your Committee may wish to seek further explanation of this apparently conflicting evidence.



- **Estimated revenues:** the Welsh Government has said that, despite annual estimated revenues of £714,000, the Pinewood studio will still run at an annual loss of more than £392,00 (this figure excludes a management fee, the value of which is redacted in the WAO report. The Cabinet Secretary told Members that Pinewood is currently “operating at capacity”. The Committee is unclear what exactly is meant by “at capacity”, and whether the annual estimated revenue has been revised in light of this fact. Recent correspondence from Pinewood indicated that the “occupancy rate for Stages 1–3 from November 2017 to end June 2018 was 44.12%”. The Committee would be interested in a further exploration of how this tallies with the Cabinet Secretary’s statement that the studio is “operating at capacity”.
- **Value of works carried out by Pinewood:** The Ministerial Advice prepared by Welsh Government officials that recommended termination of the original contracts with Pinewood (the Collaboration Agreement and Lease Agreement) stated that 'Pinewood had carried out works and investments in equipment at around £800,000'. However, it has become clear that the Welsh Government did not know the value of works carried out by Pinewood, and that this value of works was not specified in the Agreement to Lease the site. This issue was covered in the session with the Minister and officials on 12 July, though Members feel this issue merits further scrutiny, not least because we would expect to a schedule of required works to be attached to any lease agreement.
- **Listed Building:** A derelict Grade II listed farmhouse was included as part of the Energy Centre site. The Committee was disappointed that the Minister in his evidence told us that Welsh Government will only work on the farmhouse if required to do so by the local planning authority or Cadw.

These are the main issues that are of concern to the Committee. The Committee agrees that the relationship merits further scrutiny. However, this Committee’s focus has been on the broader policy issues, and we think that the relationship with Pinewood would benefit from the Public Accounts Committee’s focus on value-for-money and governance.

The WAO report is “facts only”, meaning that it does not contain recommendations to the Welsh Government. Although our work on the screen industry will no doubt

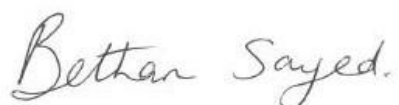


contain recommendations relating to Pinewood, we feel that the value for money and governance issues are ones that PAC is best placed to help the Welsh Government learn constructively from this episode. Given the concerns we have outlined, we hope that the Public Accounts Committee will ask the Welsh Government to respond to the WAO report on this occasion.

Consequently, I would be grateful if the Public Accounts Committee would now consider the Welsh Government's relationship with Pinewood and the issues of governance and value for money raised by the Auditor General's report.

I have asked the officials supporting the Committee to liaise with their counterparts supporting PAC to ensure that they have all the information they need to support PAC in taking this matter forward.

Yours sincerely



Bethan Sayed AM
Chair



Evidence Paper in advance of the Public Accounts Committee Scrutiny Session – 05.11.2018

Auditor General for Wales Report on Pinewood Studios

The purpose of this paper is to provide Written Evidence to the Public Accounts Committee on the Auditor General for Wales Report on Pinewood Studios. A timeline is attached at Annex 1.

Project Initiation

Officials initially approached the former CEO of Pinewood Shepperton plc in the summer of 2013 regarding potential investment into a new film and TV studio in Wales. This was in response to an ever increasing demand for studio space in the UK due to the high level of major inward investment feature films and high end TV drama, coming to the UK on the back of UK Tax incentives. This was backed by the British Screen Commission's call for more studio space in the regions to cope with the demand as London was becoming full. During discussions Pinewood proposed the creation of a £30m film and TV fund for Wales. The money was to be retained by the Welsh Government and Pinewood were to work with production companies to structure commercial deals that were considered suitable for Welsh Government investment. These deals were then to be presented to an independent panel of experts, who would have responsibility for providing advice to Welsh Government on whether to invest in the production. This was an opportunity for Wales to establish a sustainable commercial fund to reinvest into productions securing the long term future of the industry in Wales, sharing in the commercial success of productions at the same time as securing economic benefits of spend across the Welsh Film & TV supply chain. This was a unique opportunity for the Welsh Government to collaborate with one of the leading providers of studio and related services to the worldwide film and television industries. Officials saw the opportunity to market Wales' Film & TV industry on the back of a globally recognised brand via a sponsorship agreement.

Pinewood Collaboration Agreement

These discussions led to the development of the Collaboration Agreement which was a binding contract between the Welsh Government and Pinewood. The Collaboration Agreement commenced on the 1st March 2014 and had three main components:

- 1. A film and television studio facility*
- 2. A £30m Media Investment Budget, to provide a mix of flexible film and television finance.*
- 3. A sponsorship agreement*

Studio

Following an extensive search for appropriate sites for the studio, Pinewood Shepperton plc expressed a preference for Wentloog as the preferred site for the new facility. The new site was considered to be the best option due to its location, size and accessibility. Since opening in 2015 the studio has been home to several major drama productions and films to date, including Journeys End, Sherlock Season 4, The Bastard Executioner, The State and Showdogs. The facility is also home to key film and television supply chain companies such as Andy Dixon Facilities, Real SFX and Lubas Medical.

Media Investment Budget

For productions supported via the Media Investment Budget (MIB), the criteria to date has been that projects must undertake 50% of principal photography in Wales and spend a minimum of 35% of their budget on local below the line expenditure¹. However, this is combined with a requirement for all commercial funding to be compliant with the Market Economy Operator Principle (MEOP) and repaid in full, plus profit.

Pinewood's role was to develop commercial projects to a point whereby they were considered ready to apply to the MIB. The commerciality of projects applying for funding via this route is ratified by external media experts and then considered by a panel of media specialists. Any project not considered to be MEOP compliant would not be recommended for funding.

The specialist panel assesses the level and type of funding being requested and considers the probability of its potential to provide a return on investment, based on but not limited to, independent sales projections, how other projects of a similar genre have done in the market place and track record of the production team.

Under the original Collaboration Agreement, Pinewood brought forward nine projects through the MIB that were filmed in Wales.

We have had some particular successes, for example 'Their Finest' which has seen excellent box office takings and significant critical acclaim. Welsh Government has recouped all of its investment on this film. In addition, 'Journey's End', based on the famous play by R. C. Sherriff, released in Cinemas in the UK in March 2018 has received very favourable reviews and fared well at the box office. The Welsh Government has already recouped two thirds of its investment into the film.

Overall, each project supported by MIB has also spent a significant proportion of their budget locally; employing freelance crew and facilities companies in Wales. This expenditure is running in excess of £18m.

The very first project supported via the MIB 'Take Down' did not do so well. This was the very first project supported via the fund and provided some important lessons learned for Pinewood, Welsh Government Officials and the Media Investment Panel. In particular, it was considered that future projects should have a greater balance of private investment and therefore requiring a lesser contribution from Welsh Government, better value for money and more detail to be provided to assess potential recoupment.

Details of projects supported via the MIB under the Collaboration Agreement are detailed in the Wales Audit Office Report.

¹ Below the line expenditure can be defined as all production costs excluding the creative talent – such as Actors, Director, Producers, and Writers from the other crew.

Sponsorship

The sponsorship was for Pinewood to promote Wales as a centre of excellence for film and high end TV drama, as part of their international offer. It is not comparable with any other sponsorship agreement that Welsh Government has entered into hitherto.

Having such a well known brand in Wales has helped to elevate Wales as a premier production location and has given Wales a global advantage over other regions.

Pinewood has worked closely with Welsh Government to bring other productions to Wales.

The return on investment for having the Pinewood brand linked to Wales and promotion in global markets is difficult to quantify. Whilst the success of the TV and film industry in Wales cannot be attributed to Pinewood alone, there is little doubt that their sales efforts and their brand have led to an increase in enquiries for film and TV in Wales.

Officials believe that the production expenditure for projects that Pinewood have brought to Wales via their sponsorship activities is in excess of £24m.

Issues with the Collaboration Agreement

Transparency

Officials wrote to Pinewood on 2nd November 2016 highlighting the need for full transparency in the information it provides to Welsh Government and Media Investment Panel about the extent of wider Pinewood Group involvement in productions. This was part of an agreement between both parties to work together to resolve any outstanding problems and continue to deliver great projects to Wales. Officials requested that for all projects we are provided with the full details of all benefits which Pinewood would accrue from the deal proposed within and across the Group. Pinewood did then provide Welsh Government with information regarding to any services they would be providing and the cost to the production for each project brought forward for consideration for MIB.

Perceived Conflict of interest

The lack of transparency referred to above gave rise to concern about Pinewood having a perceived advantage over other companies through its exclusive access to the MIB. Local companies had voiced these concerns, having been unsuccessful in securing work through productions brought in via this route.

As a result, we entered into further discussions with Pinewood, and procedures were tightened to provide additional assurance. The independently appointed Media Investment Panel considered potential conflicts of interest in projects brought forward by Pinewood Pictures, and sought to ensure the best deal possible for Wales in providing advice to Welsh Ministers.

To add to this, the Pinewood Studio facility, and the MIB, operated independently of each other and there were no conditions imposed to use Pinewood Studio Wales when accessing the MIB.

Contract Performance

Officials raised concerns with Pinewood in November 2016, about performance of the fund, with investment and returns falling significantly short of the original business plan.

Pinewood stated that this was mainly due to changes in the market place, but it was recognised that changes needed to be made and a new business plan was duly requested.

A new business plan was submitted, but did not meet Welsh Government's expectations and further negotiations commenced. In October 2016, Pinewood came under new ownership, followed by the appointment of a new Chairman and interim CEO, following the then Chief Executive's departure from the company in April 2017. The new Chairman and interim CEO took over responsibility for re-negotiating the terms of the Collaboration Agreement with officials. It was during this period that Pinewood made the decision to withdraw from third party fund management.

Reasons for move to new agreement

Pinewood's decision to withdraw from third party fund management across the board – not just in Wales - presented us with the opportunity to renegotiate the terms of our collaboration with Pinewood.

Whilst the full terms of our new agreement are in confidence, at Pinewood's request, this means that they remain fully committed to operating the studio in Wentloog, and are continuing to promote Wales internationally as a destination for high end TV and film production.

The success of the TV and film industry in Wales cannot be attributed to Pinewood alone, however, there is little doubt that its sales efforts and brand have led to an increase in enquiries for film and TV in Wales.

Therefore, it was considered by Welsh Government that retaining the Pinewood brand through a new three-year agreement, which would also generate commercial revenues through the studio, was a better value for money proposition than simply leaving the site empty, the costs of which would be significant to Welsh Government.

In addition, the new agreement can be terminated by the Welsh Government upon six months' notice at any time after the first anniversary of the agreement, 1st November 2018.

The Property

This modern industrial property which is located at Wentloog was built to a high standard by the former Welsh Development Agency in 1998. The property was later sold to the private sector and has largely remained in beneficial occupation ever since and up until its re-purchase by Welsh Government in 2014.

When acquiring or disposing of property, it is normal practice for a valuation report to be carried out to confirm that the transaction represents market value. Such reports comment on the condition of the building but do not extend to a full examination of the roof, unlike a full structural survey which would have looked at all aspects of the building. In this case, the purchase price paid by Welsh Government was less than the valuation provided by Welsh Government's property advisors and significantly below the Vendor's quoting price at the time.

As the AGW Report noted, the condition of the buildings at the time was observed and reported by the independent valuers as being in a generally reasonable state of repair commensurate with its age and use. No urgent or significant defects or items of repair were

noted within the valuation report which would be likely to give rise to substantial expenditure in the foreseeable future or which fall outside of the scope of a normal annual maintenance programme.

Shortly before Pinewood moved into the building, a number of water leaks became apparent, mainly in the vicinity of the rainwater gullies. The required roof repairs could have been restricted to these areas. Officials considered the options available and decided to implement a more comprehensive refurbishment scheme costing £979,000. This provided a coating for the entire roof and had the benefit of extending the life of the roof to more closely match the term of the lease. It was also considered that this option would minimise operational and reputational risks, assist with the ongoing management of the property and would make the property more saleable should Welsh Government seek to dispose of the property in the future.

It is almost impossible to accurately ascertain the cost of ongoing repairs to the roof because it would depend on how quickly the roof deteriorated in the future. At the time, officials established that circa 90% of the water ingress that the property was experiencing was due to deterioration of the lining of the gutter system. We may have been able to undertake isolated repairs to address the identified leaks at a cost of £15-20K. However, this option would not have guaranteed a watertight building going forward. The property was circa 16 years old. A roof system would usually be expected to have a life span of between 20 and 25 years, depending on the environment that it is exposed to. Consequently, further deterioration could reasonably be expected during the term of the proposed lease to Pinewood. If this deterioration was limited to the gutters more comprehensive works to reline the gutters could be implemented with an estimated cost of £100,000.

However, it is likely that in addition to the issue relating to the gutters there would be future problems with the roofing sheets that make up the majority of the roof. Isolated repairs of this type could be implemented on an as needed basis, but would be unlikely to fully resolve the issue.

Taking this type of reactive approach might have proved cheaper over time, but it would have meant more frequent maintenance and additional financial and reputational risks. For example if filming schedules were impacted or sets damaged due to ongoing water ingress productions could have been delayed with significant budget implications to the production companies.

The property was acquired in the open market with the purchase price taking into consideration the fact that the roof was a significant way through its expected life. The scheme undertaken significantly extends the life of the roof and includes a 20 year guarantee, which would be taken into consideration by a purchaser should Welsh Government seek to sell the property in the future.

On the matter of the listed farmhouse, the vendor was unwilling to sell the property without the buyer also acquiring the derelict Grade II listed house located adjacent to the main building. In purchasing the house, Welsh Government were under the usual statutory obligations to renovate the building accordingly. There is no set deadline for these renovations. The building or £360,000 renovation costs have not been re-evaluated since purchasing the building in 2014. Officials do not have an estimated sale value after refurbishment. There are no immediate plans to use the building. However, in renovating the building, it could become a valuable asset that can be leased or sold, either with or separate to the main building.

The Welsh Government was not provided with a schedule of works by Pinewood for its proposed £800,000 Tenant's contribution as this was not a condition of either the Collaboration Agreement or the Lease. This was a commitment made by Pinewood. These costs were not

included in the Agreement for Lease. The contribution was worded so that this would be provided over the term of the Lease.

The roof height at the studio has meant that productions requiring aerial shots have been precluded from use. As previously indicated, the search undertaken by both Pinewood and Welsh Government officials identified only two suitable sites for a potential studio based on Pinewood's specific requirements. Pinewood subsequently identified the former Energy Centre building at Wentloog as the better of the two shortlisted options. Pinewood recognised the limitations of the Wentloog building from the outset including the fact that productions that need to hang lighting from the ceiling will not be able to use the facilities due to the height and weight loading restrictions of the roof. Nevertheless, the Wentloog building still provided the best solution at that time for the company to operate from Wales.

There are workable rigging solutions to hanging lighting from the ceiling which makes the facility usable to all productions that can work to the height of the facility. The studio has been used for feature films *Showdogs* and *Journeys End*, and the TV series *Sherlock*, *Doctor Who* and Channel 4's *Jerusalem*, which demonstrates that it is still eminently usable as a studio facility by a broad range of productions.

There is still a huge shortage of studio space across the UK and in Wales. The Pinewood Wales facility has its market and is therefore an important asset for the industry here.

At the time of re-negotiation of the Collaboration Agreement it was considered important to retain the Pinewood brand in Wales and the facility as a studio. There are licensees in the studio who took a business decision to take office space at the site to be close to productions.

The demand for studio space in Wales is proven by the number of enquiries received for studio space and the number of studio visits undertaken by Wales Screen. Since July 2017, Wales Screen has received over 36 enquiries for studio space in Wales, with Pinewood being included in at least 30 of these requests.

In addition, there are economic benefits which arise from productions that use the site. For example, *Ravers*, which filmed at the site in 2018, reported a Welsh spend figure of £1m. We estimate that on average the Welsh spend from Productions using the studio could range between £5m and £10m per annum.

The suitability of the site has been further demonstrated by *The Crown* one of Netflix's key shows, using Pinewood Studio Wales as its production base for workshops and office space whilst filming parts of Season 2 on location across South East and North Wales. This sort of activity and the economic and cultural benefits it can bring to the area is very welcome; a number of local people have roles as actors and supporting cast in the drama. We are building a strong relationship with Netflix, with this being one of several productions that have filmed in Wales in recent months.

The Management Services Agreement

Welsh Government contracted with Pinewood under a new three year 'Management Services Agreement', which had two complementary parts:

- the sales and marketing of the studio; and
- its operation and management

Under the terms of the new agreement, Pinewood would continue to operate the studio on behalf of the Welsh Government. It should be noted that either party may terminate this

agreement at any time by giving 6 months' written notice to the other party to expire no earlier than 12 months after the commencement date.

The annual net cost to the Welsh Government of operating the management services agreement:

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|--|----------------|
| Annual studio running costs | 890,000 |
| Reimbursement of Pinewood production costs | 216,000 |
| Less: Projected studio revenues | (714,000) |
| Net annual operating cost before management fee | 392,000 |
| Plus: Management fee payable to Pinewood | [redacted] |
| Net annual operating cost | [redacted] |

The annual studio revenue forecast of £714,000 was supplied to Welsh Government by Pinewood. The net operating cost totals in the above table assume that this figure is realistic. The reliability of the forecasts were tested and scrutinised by officials and also by independent property advisors.

At the time it was acknowledged that should a new agreement with Pinewood not go ahead, then the Welsh Government would incur annual property holding costs of around £890,000 (including VAT), and could expect only around £124,000 of annual income from the letting of office space. If these estimates were accurate, then the likely net annual cost to the Welsh Government under that alternative scenario would have been £766,000.

In addition, should the site not have been continued as a studio facility, the economy would not benefit from the additional revenues of productions using the studio. This is estimated to be between £5m and £10m per annum.

When the Minister for Culture, Tourism and Sport attended the Culture, Welsh Language Committee in July this year, it was stated that Pinewood was on track to achieve the forecast revenues for the first financial year of the new agreement.

Since that time projected revenues have dropped and the facility has been less busy than earlier in the year. This is not unusual for studio facilities, with demand being dependent on the right projects at the right time. Many of the projects that have filmed in Wales since July, have been location based projects rather than studio based projects. Wales still has a very healthy pipeline of projects looking to film in Wales over the next 12 months.

Pinewood Studio Wales is currently generating a sustainable annual income of circa £100,000 from the Media Hub Licences on the site. 17 key supply chain companies are located at the facility including Marigold Costumes Limited, Sgil Cymru Cyf, Alpha Grip (Cardiff) Limited, Movietech Camera Rentals Limited and Oh So Small Productions Limited.

The stages, production offices and workshops shop have generated circa £350,000 income from the start of the agreement to date.

More recently the facility has been home to the well known production 'The Crown' while they film on location across Wales for the forthcoming series. It has also recently been used by a Channel 4 production Jerusalem, Doctor Who and independent feature film Ravers, thereby continuing to demonstrate its suitability as a studio facility.

Should either party chose to terminate the agreement officials are confident there is enough demand for studio facilities across the UK to find another operator for the facility. The site is a popular commercial location with good links to the M4 Motorway and benefits from good quality office accommodation finished to a high standard. The lack of freehold opportunities within the market should enhance the property's appeal.

Bad Wolf

Pinewood executives told WAO that the opening of a new film and TV production studio by Bad Wolf Studios (Wales) Ltd in Trident Park, Cardiff, in May 2017 had a detrimental impact on the occupancy of Pinewood Studio Wales. Pinewood argued that the number of enquiries they received for it had fallen as a consequence, although demand for Pinewood studios within the UK remains strong. Wolf Studios Wales, Trident Park, is currently full and is not in competition with Pinewood. Wales Screen promotes all facilities in Wales equally and there is sufficient demand for studio space in Wales for both Pinewood Studio Wales and Wolf Studios Wales to operate alongside each other. Bad Wolf has its own slate of productions worth circa £300m and to date Wolf Studios Wales has only been home to Bad Wolf Productions. Recent productions include:

- Deborah Harkness' All Souls Trilogy, the first of which is A Discovery of Witches, The first season was filmed in Wolf Studios Wales and on location in Wales. Bad Wolf will look to adapt all three books in the series for television. The first series is expected to generate £10m in Welsh Spend. This is currently on being aired on Sky.
- Phillip Pullman's His Dark Materials, an adaptation of the contemporary classic trilogy of novels for the BBC. The production currently filming in stages at Wolf Studios and on location in Wales its expected to spend £15m in Wales. The series is likely to run over five seasons, with eight episodes in each and filming is due to begin shortly.

South Wales has a cluster of studio facilities and there is always room for competition when growing a successful film and television industry. Pinewood was happy to recognise this.

In advance of Welsh Government entering into any studio deal with Bad Wolf, the then Chief Executive of Pinewood confirmed in writing by email that they were content for us to proceed in supporting Bad Wolf with a studio facility.

Conclusion

The importance of studio infrastructure has been a key part of our strategy for the Sector and is critical to the development of the film and television industry in Wales. The Pinewood deal was instrumental in taking the industry in Wales to the next level, raising our profile and making Wales the place to bring productions, outside of London.

These arrangements have brought significant value to the industry, but there have also been a number of lessons learned within the Sector Team and across Welsh Government as a whole.

Timeline

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| 02/10/2013 | Pinewood Chief Executive writes to officials regarding preferred site at Wentloog |
| 30/01/2014 | Pinewood submit Collaboration Agreement Business Plan |
| 07/02/2014 | Legal completion of the purchase of the Property by Welsh Ministers from Vendors (Standard Life). |
| 01/03/2014 | Commencement of Collaboration Agreement |
| 04/2014 | Set up Media Investment Panel |
| 19/05/2014 | Approval of 1 st project under MIB "Take Down" May 2014. |
| 02/06/2014 | Production Finance Agreement executed for the film <i>Take Down</i> |
| 16/07/2014 | Agreement to Lease signed by the Welsh Government and Pinewood Studio Wales Ltd |
| 12/01/2015 | Lease Commencement Date |
| 01/2015 | First Production begins at Pinewood Studios Wales |
| 16/03/2015 | First Minister visits Pinewood Studios Wales |
| 20/01/2016 | Officials send note to Cabinet Secretary regarding issues relating to the Media Investment Budget performance. |
| 28/04/2016 | Property Leadership Team recommendation of Central Roofing Bid |
| 08/2016 | Concerns by Creative Industries Sector Panel and Media Investment Panel about Media Investment Budget Performance |
| 22/08/2016 | Further note to Cabinet Secretary - Issues with Media Investment Budget. |
| 23/10/2016 | Lease Agreement Signed |
| 02/11/2016 | Officials issue letter to Chief Executive, Pinewood regarding issues with the Media Investment Budget. Ongoing dialogue on these matters until 23 rd January 2017. |
| 12/01/2017 | Rent Commencement Date |
| 23/01/2017 | Officials write to Chief Executive, Pinewood regarding the requirement to make changes to the MIB. Further dialogue commences on proposed changes to the MIB until April, when Chief Executive departs Pinewood. |
| 30/03/2017 | Wolf Studios Wales project approved |
| 31/03/2017 | Agreement from Chief Executive of Pinewood to proceed with Bad Wolf studio |
| 04/2017 | Change of management at Pinewood as Chief Executive departs and interim Chief Executive takes over. A new period of negotiation starts with the interim Chief Executive. |
| 16/08/2017 | Pinewood make the decision to withdraw from third |

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| | party fund management |
| 11/09/2017 | Cabinet Secretary for Economy and Infrastructure meets with Pinewood's interim CEO to discuss the future relationship |
| 29/09/2017 | Property Leadership Team noted the Pinewood Operator Agreement |
| 31/10/2017 | Termination of Original Collaboration Agreement and Lease |
| 01/11/2017 | Commencement of New Management Services Agreement |
| 12/06/2018 | Wales Audit Office – facts only report into the Welsh Government's relationship with Pinewood |

Agenda Item 6

By virtue of paragraph(s) vi of Standing Order 17.42

Document is Restricted