



Cabinet

14 June 2017

Item
7(ii)

Report of	Chief Executive	Author	Adrian Pritchard ☎ 282211
Title	Creation of New Commercial Companies		
Wards affected	All wards		

This report requests Cabinet to approve the creation of new commercial companies.

Summary

This report requests authority from the Cabinet to the creation of a holding company and a subsidiary company (Trading Company). Two companies have already been approved by Cabinet (Housing Company and Energy Company) and these companies together with the Trading Company will be subsidiaries of the holding company. This structure is being created in order for the Council to progress its stated social policies in housing and energy provision together with some commercial ambitions.

1. Decisions Required

- 1.1 Approve the Business Case and the formation of Colchester Commercial (Holdings) Limited (Colchester Commercial) and its group structure.
- 1.2 Approve the Business Case and formation of a subsidiary company (TradingCo) as part of Colchester Commercial.
- 1.3 Note that the Business Cases have been approved separately by Cabinet for the Colchester Heat Network Company (EnergyCo) and the Housing Development Company (HouseCo) and will now form subsidiaries of the Holding Company (Colchester Commercial).
- 1.4 Delegate to the Chief Executive in consultation with the Leader of the Council, authority to finalise the Articles, and the Shareholder Agreement including the associated Reserved Matters for Colchester Commercial and the TradingCo.
- 1.5 Approve the Board of Directors for Colchester Commercial of up to 5 Directors, comprising 4 Borough Councillors, and the Managing Director of Colchester Commercial.
- 1.6 Approve the Board of Directors for EnergyCo comprising 3 Directors, being the Managing Director and Assistant Director of Colchester Commercial, and a Colchester Borough Council Senior Officer.
- 1.7 Approve the Board of Directors for HouseCo comprising 3 Directors, being the Managing Director and Assistant Director of Colchester Commercial, and a Colchester Borough Council Senior Officer.

- 1.8 Approve the Board of Directors for TradingCo comprising 3 Directors, being the Managing Director and Assistant Director of Colchester Commercial, and a Colchester Borough Council Senior Officer.
- 1.9 To note that the Trading Board Terms of Reference will be revised to include their role regarding new trading opportunities, and performance monitoring for Colchester Commercial.
- 1.10 To note that the existing budget and financial forecasts will be used as the basis of operation for the group structure for this financial year.
- 1.11 Authorise the Chief Executive to determine the Colchester Commercial and subsidiary company names.
- 1.12 Authorise the Chief Executive, following consultation with the Leader of the Council to agree the Human Resources policies that will be adopted by Colchester Commercial and its subsidiary companies.
- 1.13 To note that Service Level Agreements for services between the Council and the company group structure will be based on existing recharge levels for this financial year as set out in the Business Case, and will be reviewed as part of the 2018/2019 Business Plan.
- 1.14 Authorise the Chief Executive, following consultation with the Leader of the Council to take any other actions that are required to establish the Group Company Structure with its three subsidiaries described in this report and to enable them to commence trading activities.
- 1.15 To authorise the Monitoring Officer to make any consequential amendments to the Constitution.
- 1.16 To appoint the Chief Executive of the Borough Council as Managing Director of Colchester Commercial on a one day a week basis on pro rata pay terms to that currently received with effect from 1 July 2017. This will reduce the Chief Executives current contract with the Borough Council to four days a week.
- 1.17 To note the Chief Executive has the authority to appoint, within the Council restructure, the Assistant Director and Commercial Services Manager posts within the Company.
- 1.18 To agree to allocate £250k from the New Homes Bonus to meet one off costs in respect of set up and implementation of proposed companies as set out in section 4.

1.2 Reasons for Decision(s)

Following the Cabinet's decision on 15 March 2017 the proposed company structures will enable the Council to operate in a more commercial culture and environment to address the challenges of further budget reductions. The company structure together with a more efficient senior management structure within the Council will contribute to the Council's savings targets.

1.3 Alternative Options

Not to create the company structure but to consider commercial opportunities on an ad hoc case by case basis. This is not considered appropriate and accordingly is not being recommended.

2. Background

- 2.1 Cabinet at its meeting on 15 March 2017 approved a report regarding the senior management restructure. One of the decisions agreed was that a further report to Cabinet be presented on the most effective Company structure for the social policy responsibilities and commercial opportunities together with a relevant business case. This report deals with those issues.
- 2.2 As financial constraints on local authorities specifically and the public sector more generally continue over the next 5 to 10 years then local authorities need to look towards more self-sufficiency in generating income and being more efficient in service delivery. This then enables the focus of resources to be on providing services to those in most need in society together with continuation of the more universal local government services provided to all residents within the Borough.
- 2.3 Therefore there needs to be a renewed emphasis on the delivery of some major policy initiatives (housing and energy supply) and more commercial services to grow business and increase income and resources. Equally important is the use of our assets for income generating purposes and a greater need to concentrate on creating and taking opportunities in the commercial market place. In addition financial borrowing to invest in business and property investments is another area to help generate much needed revenue funding for the Council. Much of this we have been doing to date but a more appropriate company and senior management structure provides for the focus and expertise to deliver even more fully on the Council's aspirations and commercial aspects of the Council's financial needs.
- 2.4 The Borough Council has a well-established company structure in Colchester Borough Homes. It also has a smaller but equally focussed Colchester Community Stadium Company which specifically concentrates its efforts on the Community Stadium activities and both the commercial and community benefits derived from its use.
- 2.5 Cabinet at its meeting on 15 March 2017 approved the business case for the establishment of a heat network company (Energy Co) subject to a further report being submitted regarding governance arrangements. This report also deals with those issues.
- 2.6 The establishment of company arrangements and the delivery of services via a company has a number of advantages over continuing within the local authority structure. These include:-
 - Clear focus on its remit
 - Quicker decision making processes
 - Ability to take advantage of business opportunities as they arise
 - Scope to change the employment package offered
 - Ability to attract different skills and workforce
 - Accelerating the different culture required
 - Better tracking and response to market changes
 - Integration into the commercial sectors' networking opportunities

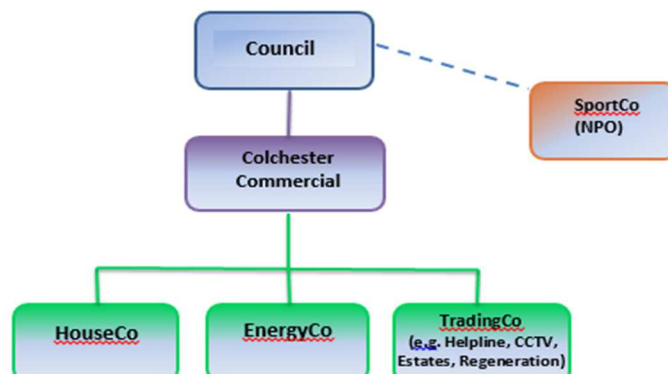
- Speeding up delivery of redevelopment more generally and affordable homes specifically
- Take advantage of other public sector partner aspirations in better utilisation of their land and property assets

- 2.7 A wholly owned local authority company allows appropriate democratic control retaining a public sector ethos but enables it the freedom to operate more commercially and respond to the needs of its customers and the business sectors in which it operates.
- 2.8 There are some potential financial implications relating to creating and operating a Company including changes to VAT requirements and corporation tax on profits made. Advice has been sought on these implications from Grant Thornton together with legal advice from Pinsent Mason which have been used to inform the business case for the proposed company structures. These are provided as confidential background papers.
- 2.8 As part of the senior management restructure it was proposed to place Sport and Leisure within the company structure. This remains an expectation but due to VAT and NNDR issues in particular further work needs to be completed before finally determining if Sport and Leisure makes financial sense to include as a subsidiary of Colchester Commercial. A further report will be provided to Cabinet once that work is complete.

3.0 Proposed Company Structures

- 3.1 It is proposed that the Council establishes a holding company, Colchester Commercial (Holdings) Limited (Colchester Commercial) which will be wholly owned by the Council, which in turn will own three wholly owned subsidiary companies specialising in housing development (HouseCo) , energy services (EnergyCo) and estates services, regeneration, events, cut and helpline (TradingCo). It is intended that Colchester Commercial will be a non trading company.
- 3.2 Cabinet at its meeting on 15 March 2017 approved the business case for the establishment of a Heat Network Company and in a separate report to this meeting has been asked to approve a business case for the formation of a Housing Development Company. This report seeks Cabinet approval for the establishment of Colchester Commercial and TradingCo. It is proposed that the three subsidiaries would be overseen by Colchester Commercial which would manage the over-arching business of the three subsidiaries. For completeness this report refers to all three subsidiaries for approval even though two have already now been approved.

Proposed Company Structure



- 3.3 This proposed structure has the potential to enable a greater degree of flexibility around management and funding and ensures that the Council retains overall strategic control. The Council will exercise its control via:
- (a) Nominating councillors to the Colchester Commercial Board;
 - (b) approving an annual Colchester Commercial Business Plan which will govern the over-arching business of the subsidiary companies; and
 - (c) implement a decision making matrix that will ensure certain strategic decisions require Council approval.
- 3.4 With the formation of any company there will be some legal company documentation that is required to be agreed and completed. This report seeks delegated authority to the Chief Executive to finalise this as set out in the decisions required at paragraph 1 above.
- 3.5 It is proposed that Colchester Commercial goes live on 1 July 2017 with 4 posts consisting of Managing Director, Assistant Director, Commercial Services Manager, and Finance Manager. The subsidiary companies of HouseCo, EnergyCo, and TradingCo will be established from 1 October 2017.

4. Financial Implications

- 4.1 This report and attached business case sets out the proposals to create a commercial company structure. It should be read in conjunction with the separate report setting out the housing company business case and with reference to the business case agreed in respect of the Northern Gateway Heat Network company.
- 4.2 The table below sets out a summary of the Council' revenue budget position for the proposed Colchester Commercial and TradingCo. The position also includes the senior management review savings and a summary of the estimated revenue impact on the Council of the EnergyCo and proposed HouseCo.

	2017/18	2018/19	2019/20	2020/21
	£'000	£'000	£'000	£'000
Management Fee / charges for services	1,426	1,216	1,086	1,086
Income re:-support functions	(586)	(586)	(586)	(586)
Senior Management restructuring	(60)	(208)	(208)	(208)
Total cost to Colchester Borough Council (CBC)	780	422	292	292
Existing budget - trading services	494	494	494	494
Existing budget - senior management roles	241	241	241	241
Total existing budgets	735	735	735	735
Comparison to existing budget	45	(313)	(443)	(443)
<i>New business case areas:-</i>				
Energy Company - CBC position	66	(80)	(77)	(74)
Housing Company - CBC position	(4)	(26)	(103)	(286)
Overall Net change compared to 17/18 budget	107	(419)	(623)	(803)

- 4.3 The summary shows a forecast saving to the Council compared to the current budget of £0.8m. It should be noted that this includes some projections already included in the MTFF.
- 4.4 The business case makes a number of assumptions including:-
- The companies will use support services provided by the Council.
 - An allowance has been made for additional one-off and recurring costs as a result of the company proposals.
 - The existing budget plans and forecasts for existing 'commercial' services have been included within the business case with an additional uplift reflecting an improvement in financial performance from the company arrangements.
 - Consideration has been given to taxation implications but further work is required to fully assess the impact for the company in particular in respect of VAT.
 - At this stage a neutral impact across the Council and companies in respect of employer pensions.
- 4.5 It should also be noted that the position for 2017/18 shows full budget costs and it will be necessary to apportion costs between the Council and companies when they start. There is also further work required to finalise and agree SLAs (Service Level Agreements) between the Council and companies. This will all be considered as part of the steps to agree the management fee for the companies in 2018/19.
- 4.6 A detailed business plan will be produced by the companies setting out the 2018/19 budget with projections for later years. This will inform the Council's 2018/19 budget and MTFF.
- 4.7 There remains work to conclude the setting up of the Colchester Commercial and TradingCo and to fund one off costs, some of which will require further work to confirm. The Council agreed to allocate £2.036m in the 2018/19 budget from the New Homes Bonus to support a number of objectives. As part of the decision in respect of the EnergyCo it was agreed by the RIF committee that £300k from the New Homes Bonus be earmarked to support the initial set up of the company. Given the forecast costs shown in this report it is proposed that the Council allocates a further £250k from New Homes Bonus in 2017/18 to support the delivery and implementation of the company proposals including those set out within the HousingCo business case.
- 4.8 In setting up the proposed companies it is important to consider the transfer of risk from the Council to the company. The Council does not include any general contingencies within service budgets with any 'in year' budget variances managed corporately as part of the normal budget monitoring process. The Council does though consider financial risks as part of the assessment of the recommended level of balances.
- 4.9 When the Council setup Colchester Community Stadium Ltd a 'cashflow' loan was provided to cover setup costs and initial cashflow. As part of finalising the company arrangements consideration will be given to an appropriate loan facility.

5. Legal Implications

- 5.1 The result of the proposals contained in this report are that:
- (a) the Council would be a shareholder of a holding company (Colchester Commercial) and indirectly through Colchester Commercial own and control

three subsidiary companies limited by shares TradingCo, HouseCo and EnergyCo.

- (b) Colchester Commercial would appoint a board to each subsidiary company.
- (c) the Council will enter into a Shareholder's Agreement with Colchester Commercial through which it would be able to control the company and via Colchester Commercial have control over; HouseCo, EnergyCo and TradingCo.

5.2 The Council will approve a Decision Making Matrix which clearly shows the major decision making powers held by the Council; Colchester Commercial; and the three subsidiaries.

5.3 The Local Government Act 2003 ("2003 Act") enables the Council to borrow (Section1) and/or invest (Section12) money for any purpose relevant to its functions. Accordingly, in order for the Council to have the vires to prudentially borrow and/or lend funds to either HouseCo or EnergyCo, it must be shown that doing so is relevant to the Council's 'functions'.

5.4 There have been no cases under the 2003 Act to assist in the interpretation of 'functions'. However in, relation to the incidental power in Section 111 of the Local Government Act 1972 Act, the Court held that 'functions' refers to the "multiplicity of specific statutory activities that a Council is expressly or implicitly under a duty to perform or *has power to perform* under any relevant legislation".

5.5 The Council has the following powers that are relevant to the commercial ventures pursued by HouseCo, EnergyCo and TradingCo:-

- (a) the power to produce heat, establish and operate generating stations for the purposes of producing heat and the power to sell heat (Section11 of the Local Government Miscellaneous Provisions Act 1976);
- (b) a multitude of powers and duties in in respect of the development and provision of housing pursuant to the Housing Act 1985 and other relevant legislation; and
- (c) the power to establish wholly owned companies to carry out trading and commercial activities pursuant to the General Power of Competence (Section1 Localism Act 2011); the incidental powers (pursuant to Section 111 of the Local Government Act 1972); and the trading powers (contained at Section 95 of the Local Government Act 2003).

5.6 Accordingly, the Council has the legal power to carry out the relevant commercial ventures and, as such, these commercial ventures can be said to be 'functions' of the Council. On this basis, it is clear that the powers under Sections 1 and 12 of the 2003 Act can be used as authority for the Council to borrow and invest money to fund capital expenditure required by HouseCo, EnergyCo and TradingCo's working capital requirements.

5.7 The legal advice confirms that Colchester Commercial and the subsidiaries will be considered Contracting Authorities and be subject to the procurement requirements contained in the Public Contract Regulations 2015. However the advice confirms that the exemption contained in regulation 12 of the Public Contract Regulations 2015 (otherwise known as the Teckal exemption) will permit the Council and each of the subsidiaries to award contracts to each other without the need for a procurement process.

6. Human Resources Implications

It is proposed that staff currently employed in the areas within the Council where the functions are being transferred to the subsidiary companies will be transferred pursuant to the Transfer of Undertakings Protection of Employees Regulations 1998 (known as TUPE). The staff would transfer into the employment of the relevant Subsidiary on the same terms and conditions that they received in the employment of the Council.

In relation to other support or ad hoc Council staff these would be seconded to the company and paid for by the company or the service bought from the Council again paid for by the company.

7. Risk Management Implications

A risk register has been developed and is included as an appendix to the Business Case.

8. Strategic Plan References

- 8.1 The strategic plan sets out the direction of the Borough and Council in the medium term. This company structure will ensure implementation of the plan and capacity in the areas of priority.

9. Equality, Diversity and Human Rights, Publicity, Consultation, Community Safety, Health, Safety Implications

- 9.1 None particularly identified at this stage.

10. Publicity Considerations

- 10.1 It will be important to inform residents, via our web presence of these changes. In addition, we will inform our public sector partners with whom we provide services to the public and to the private sector, who can take advantage of some of our property development requirements via contract for goods and services.

Exempt Background Papers

Grant Thornton's report – Council Holding Company Financial, Tax and Legal Advice.

Not for publication by virtue of paragraph 3 of Part 1 of Schedule 12A to the Local Government Act 1972 (financial / business affairs of a particular person, including the authority holding information)

Pinsent Mason's report - Colchester Borough Council's Colchester Commercial Ventures Legal Options Report.

Not for publication by virtue of paragraph 3 of Part 1 of Schedule 12A to the Local Government Act 1972 (financial / business affairs of a particular person, including the authority holding information)