

Item 6 (a) – Authority to establish a Local Authority Trading Company

The attached report was considered by the Cabinet on 5 March 2015, relevant minute extract below:

Cabinet – 5 March 2015 (Minute 83)

The Portfolio Holder for Finance & Resources introduced the report and outlined the background to the proposals and the rationale for establishing a local authority trading company which would assist with the Council's future funding position.

The Chairman welcomed the report, which was the culmination of nearly two years' work, and hoped that it might be possible to arrange a briefing for all Members before this was considered by the full Council on 31 March 2015.

The Chief Officer Communities & Business then took Members through each section of the report in detail. She explained that the proposal to set up a Trading Company, which would be a company limited by shares with the Council retaining a 100% shareholding as a single shareholder, would allow the Council to take advantage of the powers to trade for profit introduced under the Local Government Act 2003 and the Localism Act 2011, where opportunities arose in accordance with the Business Plan set out within the report. The Council had been advised by EC Harris Business Asset Consultancy throughout the process and the report reflected the consultants' recommendations building upon their skills and experience of this trading sector. It was stressed that in many cases it would still make sense for the Council to invest directly itself where this was more economically beneficial but that there were cases where the Council could not invest directly, such as for housing development, whereas a Local Authority trading company could do so. By establishing a trading company the Council would have greater flexibility in choosing its investment options and could either invest directly or through the trading company as appropriate. The Business Plan contained in the report established the need to set up a trading company to enhance economic development within the district as well as providing a valuable income stream.

EC Harris had identified key decisions to be taken by the shareholders as determining:

- the purpose and permitted activities of the company;
- the capital structure and how much finance to put into the company and on what terms;
- the distribution policy for trading profit, whether to return all profits to the shareholders or to retain them for future investment;
- to agree the composition of the Board and approve appointments; and
- to appoint auditors.

Once these decisions had been taken it was recommended that the Directors should develop and approve key matters such as:

- to develop an Annual and 5 year business plan, agreeing investment targets and associated budgets;
- specific investment transactions, including acquisitions, sales, borrowing and key transactions;
- to appoint service providers, lawyers, valuers, due diligence advisors, property managers and others; and
- reporting to Cabinet and Council committees.

Member involvement on the Board of Directors had been examined but it was felt that this could create a conflict of interest. It was therefore proposed that initially the Board of Directors would comprise of the following:

- Finance Director - The Council's Chief Finance Officer;
- Managing Director - The Council's Head of Economic Development & Property;
- Director – A Council's Chief Officer to be recommended to Cabinet by the Chief Executive; and
- 2 Non Executive Directors - who will be approved by Cabinet and paid a small remuneration also to be approved by Cabinet.

It was also proposed that the Company Secretary, with no voting rights, should be the Council's Chief Officer Legal & Governance and that the Members' Communications Working Group be tasked with choosing the name of the Company. None of the Council Officers would receive additional payment for undertaking these duties and it was not anticipated that there would be any direct staffing implications for staff currently employed by the Council.

The report also detailed the governance arrangements for the new trading company and the many measures put in place to provide assurance to Members that the Council's position would be protected and that the company could be held to account by them as the shareholder. The Articles of Association would be produced in standard format and would be supplemented by a Shareholder Agreement and these could not be changed without the agreement of the shareholder. There was no requirement to include a business objects clause and this meant that the company would be able to make the same investments as any private individual, although initially the main activity would be property development.

The report also dealt with the tax liability of the new company and the need to ensure that there was no breach with the rules relating to "State Aid" and that the trading company was also mindful of its trading impact on the local economy. The report also asked for authority to make loans to the company to fund the Business Case(s). Where loans were made to the company this would come from the Property Investment Reserve and where loans were made in relation to property transactions the loans would be secured against company assets. However initial loans for working capital for setting up the company would be unsecured. EC Harris had also developed a Property Investment Strategy (PIS)

and having examined past investment trends, the experiences of other trading companies, and the anticipated investment horizon, had concluded that the financial objective of the PIS to deliver a 6% return on investment was deliverable.

In response to questions from Members present it was confirmed that the shareholder was the Sevenoaks District Councillors rather than the Council as the body corporate, and the report confirmed that indemnity insurance would be in place for Members. It was noted that the report did not set out the capital and share structure at this stage and advice would be taken as to how capitalisation would work where there was a single shareholder. It was also re-iterated that no Councillor would be able to serve as a Non-Executive Director of the company as this could involve a conflict of interest.

A Member also questioned whether it might be more appropriate to express the investment return objective as “X% above the rate of inflation” rather than 6%. It was stressed that the 6% figure took into account the funding needs of the local authority against the background in the decline in Government funding and what was considered to be an achievable and realistic rate of return. It was stressed that the EC Harris recommendation of 6% took into account past and predicted returns on this type of investment. There might be some investments which would offer a higher rate of return but also occasions where the Council might wish to invest in projects with lower rates of return where this might benefit local residents. The trading company would have the flexibility to do this but it was felt that it could do so within a balanced approach which would deliver a 6% return. The production of an annual and 5 year business plan would allow for a view to be taken on the balance of property investments each year. Reporting arrangements for Non-Executive Director’s pay was also discussed and it was noted that this would be reported and agreed by Cabinet. It was also felt to be unnecessary to specify whether an Executive or Non-Executive Director should be the company chairman, as the Executive Directors would still form the majority on the Board and this would allow the Board greater flexibility to operate.

The Portfolio Holder for Local Planning and Environment also asked whether the wording of paragraph 17 of the report, describing the content of the Shareholder Agreement could be strengthened, so that words such as “could” or “might” should be changed to “will” and “would”. It was agreed that this should be included in the report for Council.

Public Sector Equality Duty

Members noted that consideration had been given to impacts under the Public Sector Equality Duty.

Resolved: That

- a) the Chief Officer Legal and Governance be authorised to incorporate a company (the Company) wholly owned by the Council in consultation with the Chief Executive, Chief Financial Officer and Portfolio Holder for Finance so as to allow the Council to exercise the power to trade contained in the Local Government Act 2003 and the Localism Act 2011 and to settle the detailed arrangements for the

establishment of the Company together with the Governance structure recommended by EC Harris Built Asset Consultancy (EC Harris);

- b) it be recommended to Council that the Chief Finance Officer be authorised to provide loan facilities to the Company in consultation with the Chief Executive, the Chief Officer Legal and Governance and Portfolio Holder for Finance and Resources in line with the rules set out in this report relating to State Aid;
- c) it be recommended to Council that a budget of £10,000 for set up costs of the Company be approved. This will be funded from Property Investment Reserve.
- d) the appointment of the initial Directors of the Company as set out in the report, be approved; and
- e) the Business Case for setting up the Company be approved.