

**NOT FOR PUBLICATION**

Parts of Appendix A and Appendix C to this report contain exempt information as defined in Paragraph 3 of Part 1 of Schedule 12A to the Local Government Act 1972 (information relating to the financial and business affairs of the Council).

Report to: **Special Council**

Date: **28 July 2016**

Title: **LOCAL AUTHORITY CONTROLLED COMPANY (LACC) BUSINESS CASE**

Portfolio Area: **Leader of the Council - Strategic Vision**

Wards Affected: **All**

Relevant Scrutiny Committee: **N/A**

Approval and clearance obtained: **Yes**

Urgent Decision: **N/A**

Date next steps can be taken: **Immediately**

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**RECOMMENDATIONS**

**That Council RESOLVES:**

- 1. To proceed with the implementation of a Local Authority Controlled Company (LACC) jointly owned with West Devon Borough Council scheduled for 1<sup>st</sup> April 2017, subject to there being a satisfactory outcome to the outstanding pension, tax and governance questions and actions as set out in paragraph 5.4 of this report;**

- 2. That a Joint Steering Group (JSG) is established to deal with matters concerning the implementation of the LACC as detailed in paragraph 5.5 of this report and the draft terms of reference at Appendix B;**
- 3. That the date of transfer of staff to the Company and the commencement of the contract between the Council and LACC is to be decided by Council on the recommendation of the Joint Steering Group; and**
- 4. That the Council approves the use of up to £126,750 of the 2016/17 Budget Surplus Contingency Earmarked Reserve for the set-up costs of the LACC as detailed in paragraph 5.8.**

## **1.0 Executive Summary**

- 1.1 This report sets out and comments on the findings of a detailed business case which has been prepared by PriceWaterhouseCoopers (PwC) at the request of Members. The preparation of the business case followed the Council's decision on 25 February, 2016 (minute reference 63), that a detailed business case and implementation plan be produced to enable further consideration of the merits of establishing a Local Authority Controlled Company (LACC) jointly with West Devon Borough Council.
- 1.2 Please refer to Appendix A for the detailed business case which has been prepared by PwC (*Please note that some of Appendix A has been redacted for reasons of commercial sensitivity*).
- 1.3 The outline proposal considered by Members in February 2016 was to establish a company jointly owned by South Hams District Council and West Devon Borough Council for the purpose of:
  - Delivering services to the communities of South Hams and West Devon;
  - Generating income by delivering services on behalf of other organisations;
  - Creating a vehicle which gives both Councils a mechanism to generate profit from certain activities; and
  - Ensuring the future viability of both organisation's through appropriate strategic positioning in the public sector.
- 1.4 The findings of the detailed business case are that there is a credible case for the establishment of a LACC, based on HM Treasury's 5 case model, which reviews the strategic, economic, commercial, financial and management cases.
- 1.5 The PwC report recommends that the Councils proceed with establishing the LACC subject to positive resolution of questions relating to corporation tax, pension arrangements, governance and state aid.

- 1.6 The PwC business case states that the staff and services currently provided by the Council's Commercial Services, Customer First and Support Services would be transferred across to the new LACC, with the view that the LACC would be operational with effect from April 2017. (However, the recommendation set out above from the Executive meeting on 21<sup>st</sup> July 2016 is that the company is scheduled to be set up in April 2017 but that the decision on the actual date of transfer of staff and commencement of the contract between the Council and the LACC will be a future recommendation to Council by the Joint Steering Group that will be set up to oversee the implementation).
- 1.7 A contract between the Council and the LACC would be put in place for the delivery of all the services that are transferred. In reality services would continue to be delivered by the same people, in the same locations, it is simply the governance framework that would change. From a customer perspective there would be no change to the delivery of Council services.
- 1.8 It is proposed that in the longer term the delivery of West Devon's waste collection and street cleansing services are also transferred to the LACC. This would benefit South Hams DC in respect of efficiencies to be gained from shared management arrangements. In the short term it is being proposed to West Devon BC that a managed service be provided by an external contractor to West Devon, for a 2 year period to minimise the risk to service performance and reputation in the initial set up year of the LACC. This approach also offers another saleable option to the model for future local authority customers.
- 1.9 The LACC would also be able to generate income and profit by delivering a full range of services to other organisations, and would provide the opportunity for other Councils to buy into the company and commission services from the company.
- 1.10 The LACC is likely to provide better protection to the delivery of services and to staff in the event of local government restructure.
- 1.11 A similar recommendation relating to the implementation of the LACC and the establishment of a Joint Steering Group is being made to West Devon Borough Council on 26<sup>th</sup> July 2016 and is set out in Appendix E. The LACC will only be established by the agreement of both West Devon Borough Council on the 26<sup>th</sup> July 2016 and South Hams District Council at this meeting on the 28<sup>th</sup> July 2016.

## **2.0 Background**

- 2.1 On 25<sup>th</sup> February 2016, this Council considered a report entitled "Proposals relating to a Local Authority Controlled Company". At that meeting, the Council resolved that a detailed business case and implementation plan be produced to enable further consideration of the merits of establishing a Local Authority Controlled Company

(LACC) jointly with West Devon Borough Council. This report presents the findings of that detailed business case.

- 2.2 Since 2010 Local Authorities have been subject to increasing budgetary pressures and decreasing grant income from central government. This position is looking significantly worse for the future given the most recent budget settlement. The recent decision to exit the European Union is extremely unlikely to improve financial prospects for the public sector in the short to medium term.
- 2.3 The purpose of the councils' T18 transformation programme had been to position both councils to meet their financial obligations until 2018 and be able to continue to deliver the full range of services without cuts or long term reduction in quality. However both councils are keen to secure the future of services beyond 2018.
- 2.4 During 2015/16 the councils reviewed their priorities and Members from both Councils agreed the top priority for each organisation was to achieve financial sustainability. Both councils also stated that they did not want to see a reduction in the level or quality of services delivered to their communities.
- 2.5 The success of the T18 programme in delivering efficiencies (joint savings of £5 million) has meant that both councils are in a position to generate a surplus for the financial year 2016/17, however this will not be the case for 2018 onwards, therefore this is the right time to be considering any investment in the organisation.
- 2.6 In terms of the national context, the Local Authority landscape is changing rapidly and a mixed economy is emerging which provides opportunities for forward-thinking councils such as South Hams and West Devon.
- 2.7 Councils also have the opportunity under current legislation to form companies to trade and generate income and to provide services to other councils and organisations at a profit.
- 2.8 Establishing the LACC gives an opportunity for South Hams and West Devon to position themselves at the forefront of this emerging market for delivering services, and therefore able to take advantage of opportunities provided by other, less forward-thinking organisations.
- 2.9 The Government is interested in such solutions should it be faced with failing councils and we are in discussion with DCLG regarding funding for implementation costs for the setup of the LACC. Geoffrey Cox QC, MP for Torridge and West Devon has confirmed that Marcus Jones, Minister for Local Government will be meeting with the Secretary of State for Communities and Local Government, to consider this proposal.
- 2.10 Whilst Local Authority restructure is not currently being proposed by the Government, there is a clear threat that if councils start failing due to financial pressures then there may be a requirement for take-overs, combined councils or unitary arrangements. This could

also be an opportunity for well-placed organisations to step in for mutual benefit.

- 2.11 Initially, it is intended to set up a company that is owned and controlled by the two authorities and does the majority of its work for the two owning authorities. This arrangement follows the rules that allow the councils to pass the work to the LACC without the need to tender in the open market. (This is known as a Teckal exemption).
- 2.12 Under the Teckal arrangement the LACC will also be able to win contracts and deliver services to other organisations for a profit but only up to 20% of its turnover. Once the 20% limit is reached an additional LACC can be set up purely to provide services to other organisations and generate profits for its shareholders (this is allowed for under section 95 of the Local Government Act 2003).
- 2.13 An extension of the model would be to allow other public sector organisations to buy shares in the company, thus allowing them to commission services through the company using the Teckal exemption described above. This would achieve growth, economies of scale and further efficiencies within the company.
- 2.14 This proposal affects both South Hams District Council and West Devon Borough Council, the communities they serve and the staff they employ. The intention is for the range of services to the communities to carry on being provided to at least the current standard, albeit from an arms-length, wholly-owned LACC, so that residents and communities should not feel any adverse impact from this proposal.
- 2.15 Staff in Commercial Services, Customer First and Support Services will be transferred to the new LACC. This will be subject to TUPE (Transfer of Undertakings: Protection of Employment) regulations so that staff would be transferred on their current employment terms and conditions.
- 2.16 No restructure or redundancies are proposed; if the LACC is implemented, there would be a simple transfer of all service delivery staff into the new LACC entity. The staff will continue to provide services to the councils in the same way, but with a new opportunity to expand and grow the overall business.
- 2.17 The LACC will have a two-fold relationship with the two councils:
  - As a provider of services to the councils, controlled by a contractual relationship;
  - As a wholly owned asset of the councils controlled through the shareholders agreement and the associated governance structures.
- 2.18 The West Devon Borough Council resolution in February 2016 was to bring the waste and cleansing contract into the LACC for April 2017. The PwC report highlights the risk of this option given the extension of time taken for the detailed business case and the time needed for vehicle acquisition. An outsourced contract solution

negates the opportunity for LACC benefits to be realised for a 7 year period. A hybrid solution has been considered as part of the detailed business case; this is to provide a managed service by an external provider for a minimum 2 year period based upon the current service configuration and with costs of vehicle provision being met by West Devon Borough Council.

- 2.19 The option of a managed service would also be an offer which the LACC could add to its future marketing portfolio. It offers a market advantage to the LACC in terms of demonstrating the flexibility of the delivery model to maintain service standards, whilst still benefitting from a portion of the economies of scale of an internally delivered service.

### **3.0 Business Case Findings**

- 3.1 The PwC detailed business case reviews the case to establish the LACC against HM Treasury's 5 case business model. This model considers the strategic, economic, commercial, financial and management case for the proposed option. A headline summary of the key findings of each case are set out below along with commentary from the Councils' Senior Leadership Team (SLT).

#### **3.2 Strategic Case (refer to section 3 of Appendix A)**

The strategic case seeks to demonstrate that there is a need for a new approach to service delivery across the Councils, that the objectives are clear and that there is a clear case for change.

##### **3.2.1 PwC view:**

The PwC report finds that the LACC proposal addresses a strategic need and demonstrates:

- there is uncertainty around future funding models for local authorities;
- the Council's T18 programme will not generate sufficient savings to meet the projected funding gap and the LACC could offset some of this;
- a LACC is a way of being proactive rather than reactive to meet this challenge.

##### **3.2.2 SLT comment:**

We agree with PwC's findings that the strategic need for change is identified in the business case. Continuing pressure on public sector finances make it necessary for Councils to look for ways to generate income and reduce expenditure. However the strategic opportunity is only broadly defined in this section of their document, though it is explored in more detail elsewhere.

- 3.2.3 The financial challenges that give rise to the need for action by the Councils also provides the opportunity for the LACC to grow and

gain business as other public sector organisations seek more efficient ways of delivering their services. This is set out in paragraphs 2.6 – 2.10 above.

3.2.4 Devolution or the formation of a unitary authority would also present an opportunity, by which a LACC could gain greater access to a new, enlarged market. Front line services delivered by the LACC would be protected by such a move, due to the existence of a contract between the Councils and the LACC.

3.3 **Economic Case (refer to section 4 of Appendix A)**

The Economic Case seeks to explore the benefits of options available to the Councils in addressing the need for change. It reviews the market context and potential, demonstrates how the delivery options have been considered and determines the preferred option.

3.3.1 PwC view:

PwC state that a LACC would give the Councils the opportunity to trade with other public bodies and agreed that there is already a commercial operating model in place as a result of T18. The LACC proposal scored higher in PwC's options assessment than the "As Is" option.

3.3.2 PwC found that there are no examples of LACCs being established to provide as wide a range of services as is being proposed and that there is market potential which the current operating model is not able to capitalise. In the medium term, contracts will become available for which a LACC could bid, but there is time for the LACC to develop its trading base and commercial skills ahead of such bidding taking place.

3.3.3 Additionally, PwC agree that there is an opportunity to generate efficiencies from the integration of West Devon waste services, but found that the LACC is not dependent on West Devon Waste and street cleansing services being part of the initial LACC offering to make economic sense.

3.3.4 SLT comment:

By not establishing the LACC the Council would deny itself the opportunity of creating an income stream by supplying services at a profit to other organisations.

3.3.5 Whilst PwC have stated the case for a LACC and see the market potential, SLT view is that they have understated the market opportunity arising from the future funding gaps for other local authorities, and in particular for District Council services. It is acknowledged that the market analysis is weakened by the fact that this is as yet a largely unexplored market therefore it is difficult to make direct comparisons and accurate forecasts.

3.3.6 Due to the wide range of services to be incorporated into the LACC by the Councils, the proposed LACC will be in a unique position to offer these services to those local authorities who need to find innovative delivery methods due to the impact of their own funding model pressures.

- 3.3.7 Councils who are struggling to meet their financial burdens may opt to award work to a LACC, given the tendency for public sector to trust other public sector providers over private / outsourcing entities. Being a public sector entity would be a positive selling point of the LACC.
- 3.3.8 Councils could potentially fail (become bankrupt) and Government could step in and award packages of work to a LACC who is able to complete a wide range of local authority services; this is the subject of current discussions with DCLG as referenced in paragraph 2.9 above.
- 3.3.9 It is agreed that the efficiencies generated by the T18 commercial operating model should give the LACC an advantage in comparison to other councils' delivery models.
- 3.3.10 SLT consider there to be a market edge in being able to sell the consultancy services in relation to the transformation model. This would also apply to the locality working model. There has already been interest in these models from a number of other local authorities, this now needs to be offered on a commercial basis. There is a key market advantage in having implemented the model ahead of other local authorities which will only be marketable for a finite period.
- 3.3.11 SHDC members requested that a Member-led working group be set-up to analyse the market opportunity. This group will be in a position to share its findings just in advance of the Executive meeting to discuss the LACC on the 21<sup>st</sup> July 2016.
- 3.4 **Commercial Case (refer to section 5 of Appendix A)**  
The commercial case seeks to identify that the formation of a LACC is commercially viable with clear governance arrangements, appropriate financial and funding structures, can be implemented and that operational responsibilities are assigned properly.
- 3.4.1 PwC view:  
PwC state that the "As Is" model is not able to take advantage of procurement and profit generating opportunities. They state that the identified risks are manageable.
- 3.4.2 In relation to governance, PwC suggest that the LACC is established using the same principles as the 2015 collaboration agreement between the Councils, with equal 50:50 voting rights on reserved matters affecting both Councils; reserved matters would be stated within respective shareholder agreements and; profit share would be linked to actual contribution. PwC go on to suggest that decision making should remain similar to the current model, with joint and individual decisions being made as required by the respective Councils.
- 3.4.3 The proposed operating model maintains the integrity of the operating model established by the T18 programme and it is acknowledged in the report that the changes will be with regard to



ownership and governance arrangements rather than a restructure of the service delivery arrangements.

- 3.4.4 PwC identified that the establishment of a LACC will expose the Councils to a Corporation Tax Liability – however, this could be mitigated by applying for an exemption. It is likely that the Councils can retain their favourable VAT treatments but more detailed modelling on VAT would need to be carried out at implementation stage. The pension deficit treatment needs to be agreed – this is noted in section 5.0 of this report.
- 3.4.5 SLT comment:  
A number of issues are identified in this section that will need to be dealt with during the implementation period. This includes the drafting of the shareholder agreement and the detail of the relationship between the shareholders and the company. SLT agrees with the approach proposed for 50:50 voting rights alongside dividend shares proportionate to the value put in to the company by each Council (this value could be in a variety of forms such as contract value, loans or other assets). It would be possible for the shareholders to invite other councils to buy shares and make use of the Teckal exemption allowing them to passport work into the company without the need for procurement. Existing examples of where this arrangement works are Ubico and iESE.
- 3.4.6 There must be successful resolution to the questions concerning the treatment of the pension deficit and the ongoing LACC pension position before final commitment can be made to the LACC. Treatment of corporation tax and VAT must also be successfully resolved along with confirmation that the Teckal status does apply to the services that are to be transferred to the company. If it is not possible to get successful resolution of these matters then the decision to implement will need to be reviewed.

### 3.5 **Financial Case (refer to section 6 of Appendix A)**

The financial case focuses on the financial benefits of the new model and considers affordability and funding requirements.

#### 3.5.1 PwC view:

PwC identified set-up costs of £400k and additional on-going running costs of £60k per annum. They also calculate that there is an opportunity to generate trading profits and potential savings in the provision of the West Devon waste provision. This equates to a payback for West Devon by 2020 and South Hams by 2022, based on assumptions made in the report.

#### 3.5.2 SLT comment:

The costs already committed to pay for the business case are not included in the estimated set-up costs of £400k identified by PwC as they considered them to be “sunk costs”. These “sunk costs” total

£76,750 for the South Hams share of the business case costs. (Including these sunk costs in the business case modelling increases the year of payback for South Hams). The set-up costs would be split 50:50 across both Councils. SLT view is that set-up costs of £400k are a high estimate and that the implementation could be achieved at lower cost to the Councils. Our research shows us that implementation costs for establishing the local authority owned company Ubico were £200k, and the establishment of a shared working programme called "Vision 2020" by a group of four authorities (Cheltenham Borough Council and Cotswold, Forest of Dean and West Oxfordshire District Councils) is estimated at £170k (excluding IT costs). We also have received a significantly lower indicative cost for legal work from a leading legal firm that specialises in this field of less than a quarter of the cost estimated by PwC though this would require support by in-house project management and legal specialists.

- 3.5.3 The on-going running costs assume that the LACC's mix of external and member board of directors are minimal or unpaid. This mirrors the arrangements of other local authority owned companies.
- 3.5.4 Whilst the PwC report identifies a significant saving for West Devon waste provision, this is modelled on the transfer of the contract into the LACC in April 2017 (not the managed service option proposed by SLT) and does not allow for the current recycling market volatility.
- 3.5.5 SLT consider the margin modelled by PwC for initial business won to be an optimistic figure, however this is balanced by the rather conservative view that no income would be generated before 2020 and no efficiencies have been identified in the PwC report which would off-set any ongoing additional revenue costs. Additional work has been completed by PwC to model the effect of a reduced profit margin figure as well as earlier income generation and efficiencies to offset any additional running costs. A summary of this work has been included at Appendix C (*note this is exempt from publication as it is deemed commercially sensitive*).
- 3.5.6 It is worth noting that the combined value of the South Hams and West Devon contracts with the company will be worth in the region of £27million per annum from the first day of operation.

### 3.6 **Management Case (refer to section 7 of Appendix A)**

The management case seeks to demonstrate that the benefits of change are achievable with clearly identified transition and delivery requirements.

#### 3.6.1 PwC view:

PwC found that the T18 programme has brought commercial focus to the Councils and the proposed LACC can provide the flexibility to respond to changing market conditions. They acknowledge that the LACC has greater risk from set-up costs but this is off-set by the greater opportunity to generate revenue and therefore deliver the Council's identified priorities. PwC state that the LACC model is

deliverable and suggest an implementation plan is progressed as a priority.

#### 3.6.2 SLT comment:

We agree the PwC findings in relation to the Management Case though we do not consider the timescale feasible for full transfer of the West Devon waste contract into the LACC by April 2017. If the short term management option is chosen for the waste contract then SLT consider that the April 2017 timetable for the establishment of the LACC is ambitious but achievable. SLT do not foresee a risk to service delivery by establishing a LACC, given the staffing structure will largely stay the same.

### **4.0 Options available and consideration of risk**

- 4.1 This report essentially offers Members two options: either to continue with the decision made in February to establish a LACC for the delivery of the Council's services (including waste collection); or not to implement the LACC but to retain the current structure and service delivery model of in-house services with some out-sourced services (e.g. Leisure and waste collection etc.).
- 4.2 Establishing the LACC provides no greater risk to the delivery of the Council's services than the provision through the current in-house model.
- 4.3 There is a risk that the Councils will invest in implementing and operating the LACC but may not win the predicted levels of business from other organisations to achieve the payback periods modelled in the business case.
- 4.4 Conversely, there is a risk that the Council may be more successful at winning external business. This would need careful monitoring to ensure that it does not adversely affect the delivery of services back to the Councils.
- 4.5 By not establishing the LACC and transferring the waste contract into it, there is a risk that the Council will not gain efficiencies.
- 4.6 The risk of trying to bring West Devon waste contract fully into the LACC for April 2017 is very high but can be mitigated by putting in place an interim management solution.
- 4.7 There is a risk that if the LACC is not established then further outsourcing of services will need to be considered in the future.

### **5.0 Proposed Way Forward**

- 5.1 The fundamental issue that Members will want to weigh up when making their decision is between cost and opportunity. The cost of establishing the LACC along with any additional ongoing expenditure associated with the new model needs to be considered against the opportunities presented for future growth and income, and the strategic position that it achieves for the future delivery of services to our communities.

- 5.2 PwC's independent view and recommendation, having considered all 5 elements of the business case, is to proceed with the implementation of the LACC.
- 5.3 It is the view of all members of the Councils' Senior Leadership Team (SLT) that the growth opportunities and the long term sustainability of services offered by establishing the LACC outweigh the risk associated with the costs and that the Councils should proceed with implementation.
- 5.4 The PwC report concluded that there were a number of outstanding questions and actions, which should be resolved positively before the full LACC implementation process commences and further significant spend is incurred. These questions and actions are shown below for ease:
  - 5.4.1 Seek advice from HMRC regarding an exemption from paying corporation tax on profits related to income derived from services provided to the Councils. This is to be undertaken prior to incurring further significant cost as it is fundamental to the assumptions made in the PwC report.
  - 5.4.2 Seek advice from the LGPS on how the current pension deficit should be treated and analyse the ongoing LACC position to ensure there is no detrimental effect to the Councils.
  - 5.4.3 Obtain legal advice and support to deliver the proposed corporate and associated share structure of the LACC to ensure that it meets both the governance and spend requirements. This has been factored in to the implementation phase, including the drafting of the company's constitutional documents such as articles, memorandum and shareholder agreement. Both councils will also need independent legal advice during implementation phase.
  - 5.4.4 Obtain legal advice in relation to the Council's vires (powers) to trade the identified services, and ensure the LACC constitution has the flexibility required for future change in scope if envisaged as part of the LACC strategy. This will be covered as part of the legal support during the implementation phase. *Please refer to Appendix D for information on this point, produced by the Council's legal team.*
  - 5.4.5 Obtain legal advice to confirm that the business plan conforms with State Aid requirements and public procurement regulations. This will be covered as part of legal support during implementation phase.
  - 5.4.6 Obtain legal support and advice in relation to pensions, TUPE, and employment matters. This will be covered as part of implementation phase.
- 5.5 If Members agree to continue with the implementation of the LACC, it is recommended that a Joint Steering Group (JSG) is formed consisting of 4 Members from each Council, to deal with matters

concerning the implementation of the LACC. A draft terms of reference / scope of the JSG is shown in Appendix B. The scope of the JSG in establishing and implementing the LACC shall include but is not limited to:

- 5.5.1 agreeing the company constitutional documents such as, the articles, memorandum, shareholder agreement and incorporation of the company.
  - 5.5.2 dealing with and addressing within the company constitutional document reserved matters, financing, assets, share of dividends, deadlock, directorships, audit and exit arrangements
  - 5.5.3 agreeing the company name and location of its registered office
  - 5.5.4 establishing a position on the outstanding issues referred to in 5.4 above and make a recommendation back to the Councils regarding these outstanding issues before the LACC can be incorporated.
  - 5.5.5 reporting back to the councils once the implementation is complete
- 5.6 In order to address any concerns over the capacity of the organisation and the performance of services to the community prior to commencing trading with the LACC, it was recommended at the meeting of the Executive held on 21<sup>st</sup> July, 2016 that the decision on the actual date of transfer of staff and commencement of the contract between the Council and the LACC will be a future recommendation to Council by the Joint Steering Group.
- 5.7 If the Councils decide to progress with the establishment of the LACC then the implementation phase will need to commence and this will require professional support to complete. This work was subject to a value-for-money procurement exercise and the total cost has been included within the business case (see section 6.4 of Appendix A). It is estimated by PwC that the implementation cost will be £400,000 and this will need to be split 50:50 between the two councils subject to both Councils agreeing to proceed. Each Council has approved a 2016/17 budget of £150,000 for the set-up costs of the LACC.
- 5.8 However, £76,750 of the £150,000 has already been committed to pay for the work carried out Grant Thornton on an initial business case and the work carried out by PwC on the detailed business case.
- 5.9 Therefore the South Hams share of the one-off investment costs of up to £200,000 could be met by £73,250 from the 2016/17 budget already approved for the LACC set-up costs and the remainder of £126,750 could be funded by the 2016/17 Budget Surplus Contingency Earmarked Reserve.

- 5.10 The 2016/17 Budget Surplus Contingency Earmarked Reserve currently has a balance of £489,023, therefore there are sufficient funds available to fund this proposal. This is made up of the £767,995 Budget Surplus for 2016/17 (as per Council on 11th February 2016) less the £278,972 approved to fund transitional resources (as per Council 30<sup>th</sup> June 2016).
- 5.11 It should be stressed that where possible, these costs will be minimised and internal resources will be used wherever possible. It should also be noted that SLT have obtained indicative legal costs from a leading law firm of less than a quarter of that quoted by PwC, though in-house resources would also be required.
- 5.12 Officers will continue to engage with Staff, Members and Trade Unions to ensure that all stakeholders are appraised of developments and progress.
- 5.13 To date there has been a concerted effort to engage with staff and promote an understanding of the proposal and the implications for staff. This has been through briefings, FAQs, videos and drop-in sessions. The senior leadership team have also engaged with Union representatives from Unison, GMB, Unite and UCAT and have gone through the business case with them. All the Unions have been invited to submit their comments in relation to the business case for consideration by Councillors prior to the Council meeting.

## 6.0 Implications

Implications	Relevant to proposals Y/N	Details and proposed measures to address
Legal/ Governance		<p>The Councils can only trade for commercial purposes through a company, and only the Council can make this decision due to the financial, governance and operational considerations involved. In order to do this, the Councils must approve a business case.</p> <p>Local Authority trading powers as contained in Local Government Act 2003, Localism Act 2011, Local Government (Best Value Authorities) (Power to Trade) (England) Order 2009 have been considered and there are known legal issues for the Councils to consider prior to the establishment of a LACC. These have been identified in 5.4 above. Incidental powers to participate in external organisations (Local Government Act 1972) have also been considered and these have been identified in 5.4 above. Refer to Appendix D for further information about this point from the Council's in-house legal team.</p> <p>Therefore, legal advice and support will be required during the implementation phase, should the Council agree to the setting up of a controlled company on</p>

		<p>matters such as, pensions, tax, incorporation, state aid, shareholder agreement and TUPE. This is factored into the implementation phase of the LACC establishment.</p> <p>Detailed governance arrangements and constitution of the LACC will need to be agreed between the councils.</p> <p>If Members agree to continue with the implementation of the LACC, it is recommended that a JSG is set up as detailed in paragraph 5.5 above. Powers to set up a joint committee (Joint Steering Group) between two or more local authorities are set out in the Local Government Act 1972.</p> <p>The LACC's constitutional documents will need to be clearly drafted so that the newly formed LACC can satisfy the Teckal requirements as codified in the Public Contracts Regulations 2015.</p> <p>Borrowing decisions can only be made by Full Council under the Council's Constitution.</p> <p>Parts of Appendix A and Appendix C are exempt from publication because they contain information about the Council's financial affairs as defined in Paragraph 3 of Schedule 12A to the Local Government Act 1972. The public interest test has been applied and it is considered that the public interest lies in not disclosing all of this information because it contains commercially sensitive financial information which could prejudice the Council if the information was disclosed at this time.</p>
Financial	Y	<p>One-off Investment costs of setting up the LACC of up to £400,000 and ongoing running costs of £60,000 per annum, split between the two Councils have been identified by PwC. (This is set out in paragraph 6.4 of PwC's report - Appendix A).</p> <p>Each Council has approved a 2016/17 budget of £150,000 for the set-up costs of the LACC.</p> <p>However, £76,750 of the £150,000 has already been committed to pay for the work carried out by Grant Thornton on an initial business case and the work carried out by PwC on the detailed business case.</p> <p>Therefore the South Hams share of the one-off investment costs of £200,000 could be met by £73,250 from the 2016/17 budget already approved for the LACC set-up costs and the remainder of £126,750 could be funded by the 2016/17 Budget Surplus Contingency Earmarked Reserve.</p>

		<p>The 2016/17 Budget Surplus Contingency Earmarked Reserve currently has a balance of £489,023, therefore there are sufficient funds available to fund this proposal.</p> <p>A LACC will provide greater longer term opportunities to reduce costs and generate additional income from outside the Councils from other public sector bodies and the private sector. However, based on the assumptions made by PwC it will take five years before it will become profitable. Its profitability will be dependent on it generating additional income, as discussed in the Economic case section of the PwC report (page 79 onwards).</p>
Risk		<p>A key risk is the capacity to get everything in place for April 2017, particularly given that the organisation is still undergoing significant change from the implementation of the T18 programme. A consideration could be to phase the transfer of services into the new LACC. However, this would be much more complex and is unlikely to yield economies of scale and other efficiencies due to the way in which the organisation is now structured following T18. The cost of implementation would be as much, if not more, therefore this is not recommended.</p> <p>If West Devon Borough Council were to opt not to establish the LACC, SHDC will be unable to pursue this option and the officer recommendation would be rescinded. A fresh review and benefit analysis would need to be prepared in order to determine the best course of action.</p> <p>See also page 137 onwards of Appendix A for a summary of the key risks in a risk matrix format that have been identified by PwC.</p>
<b>Comprehensive Impact Assessment Implications</b>		
Equality and Diversity		<p><b>Staff</b> – Existing staff will transfer to the LACC under protection of TUPE regulations. This protects staff terms and conditions. The LACC would adopt Equality and Diversity policies in line with the Councils existing policies. It is unlikely that there will be any negative impact on any individuals or groups. New employees appointed to the company could be offered access to pension schemes which are less costly than the LGPS, however employees transferring to the LACC would continue to be entitled to access the LGPS or a comparable scheme.</p> <p><b>Community</b> – There is no intention to change service provision as a result of these proposals.</p>



Safeguarding		There is unlikely to be any positive or negative impact on safeguarding. Employees will continue to deliver the same jobs in the same ways from the same locations.
Information Management		<p>The wholly owned LACC will continue to be subject to the requirements of the Freedom of Information Act 2000 in respect of the services provided to South Hams District Council and West Devon Borough Council. As a LACC looks to become more commercially focused with trading etc, there may be an increase in information that is exempt from publication. However this will all be subject to the usual assessment process.</p> <p>The LACC will be required to register with the Information Commissioners Office and will adopt existing information governance protocols. The Data Protection Act would also continue to apply.</p>
Community Safety, Crime and Disorder		There will be no impact on Community Safety, crime and disorder
Health, Safety and Wellbeing		<p><b>Staff</b> – Staff will be transferred to the wholly owned company and there would be no requirement for any job assessments as these were undertaken as part of the T18 programme with a LACC in mind. A communication plan will be developed to ensure that staff are kept informed and discussions have already commenced with unions during the development of the proposal. On the whole, staff should notice little difference at the commencement of the new company working in the same places, carrying out the same jobs with the same pay and conditions as they currently do. There could be opportunity for negotiation on terms and conditions however this negotiation would take place in exactly the same way as it would do currently. A positive impact may be that new job opportunities present themselves to staff as the LACC begins to successfully trade.</p>
Other implications		<p>Procurement and Contracts – we will look to novate existing contracts to the LACC on existing terms. As contracts expire, the LACC would look to enter into new contracts.</p> <p>Property – the Councils existing property portfolio will continue to be utilised in delivery of the services</p> <p>Economy – if trading is successful there could be a positive impact on the economy through new job offers however this is unquantifiable at this stage</p>

## **Supporting Information**

### **Appendices:**

Appendix A – PwC Establishing a local authority controlled company – business case and implementation plan (*Note: Parts of this report are exempt from publication due to the commercially sensitive information contained within it*).

Appendix B - Draft Terms of Reference / Scope for the Joint Steering Group (JSG)

Appendix C – PwC Analysis of Alternative Profit Margin Scenarios (*Note: This report is exempt from publication due to the commercially sensitive information contained within it*).

Appendix D - Note on trading and charging regime

Appendix E – Recommendations to West Devon Borough Council from the meeting of West Devon Hub Committee held on 12th July 2016

### **Background Papers:**

- Proposals Relating to a Local Authority Controlled Company, presented to South Hams District Council on 25<sup>th</sup> February 2016
- Grant Thornton Options appraisal for the establishment of a local authority controlled company, presented to South Hams District Council Executive Committee on 4th February 2016
- Agenda Item 4 entitled “Transformation Programme 2018” presented to SHDC Special Council on 31st October 2013
- Agenda Item 11 entitled “Torridge and the Future Operating Model” presented to SHDC council on 2nd October 2014

## **Appendix B: Draft Scope / Terms of Reference for the LACC Joint Steering Group**

The Joint Steering Group (JSG) shall have the authority to:

1. Consider and approve the constitutional documents such as the articles of agreement, memorandum of association and the shareholder agreement
2. Sign off any document required for incorporation of the LACC.
3. Consider and approve the relationship between SHDC and WDBC.
4. Consider and approve the nature and scope of business of the LACC
5. Consider and approve reserved matters (key decisions i.e. strategy, appointment of directors)
6. Consider and determine the decision making process for the LACC
7. Determine undertakings (if any)
8. Consider and determine how shares shall be sold and purchased
9. Consider and determine rules for admission of new members
10. Consider and determine number/appointment/removal/executive or non-executive/independent chair
11. Set out and deal with issues around joint scrutiny (joint management board)
12. Strategic direction of the company
13. Consider and determine how the LACC will be controlled by the Councils i.e. decisive influence etc.
14. Consider and determine how pension shall be dealt with and report back to the councils
15. Consider and determine how assets shall be distributed
16. Consider and determine a detailed exit strategy in the unlikely event of LACC failure
17. Consider and determine the location of the LACC head office
18. Consider and determine how and if any loans are to be granted to the LACC by the councils
19. Consider and determine LACC directorship including type i.e. executive and non-executive and number and term of office
20. Consider and approve the process for determining LACC directors remuneration
21. Consider and determine the communication protocol between the LACC and the councils
22. Determine number and class of shares
23. Consider and approve company name.
24. Consider and determine the way and manner in which the LACC shall be financed
25. Consider and approve the LACC business plan
26. Consider and approve LACC accounting and other information including, LACC accounting dates and audit

27. Consider and approve the dividend policy
28. Consider and approve tax related matters such as application to HMRC for corporation tax exemption
29. Consider and approve a resolution mechanisms for deadlock both within the boardroom and shareholder meetings.
30. Consider and approve Insurance and indemnity for members and directors