

Report

Cabinet

Part 1

Date: 17 April 2019

Item No: 8

Subject Commercialisation Strategy

Purpose Present a commercialisation strategy for cabinet to consider.

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Ward City-wide

Summary The financial position facing local government continues to be a significant challenge. Over the period to 2022 the projected savings required to balance our annual budgets will cumulatively be around £30m.

The council has demonstrated very effective financial management over an unprecedented period of austerity. Much of our success has been due to our focus on managing demand and improving efficiency. Whilst we will continue to look at these areas, the scale of our financial challenge requires a different approach.

The purpose of this report is to outline a council wide approach to commercialisation, which will aim to generate income to support service delivery in future budget processes.

Proposal Cabinet is asked to:

- 1) Agree the outline approach set out in this report
- 2) Delegate operational decision making regarding the commercialisation strategy to the Chief Executive
- 3) Establish the Investment Board, as outlined in the report, with immediate effect to manage the property investment portfolio.
- 4) Agree the principle of a commercial property fund to be taken to the Council for approval within the Capital Strategy, including the approval of £50m for this purpose, noting that detailed terms of reference and investment guidelines and parameters for the Investment Board will be agreed by the Cabinet before any activity commences.
- 5) Ask the Chief Executive to progress a feasibility study on the establishment of a local authority company to manage our commercialisation activity and approve up to £100k from the Council's Invest to Save fund for this purpose.

Action by Chief Executive,

Timetable Immediate

This report was prepared after consultation with:

- Chief Executive
- Strategic Director (Place)
- Head of Law & Regulation
- Head of Finance

Signed

Background

Over the last few years, as government funding to support local government services has failed to keep pace with cost pressures, authorities have looked at alternative ways of delivering financial sustainability. As a result, an increasing number of councils have focused on generating new sources of income, often outside core activities, to support ongoing service delivery.

Newport City Council faces a particularly challenging set of circumstances:

- Welsh Government 'Revenue Support Grant', which funds around 80% of the council's net revenue budget has failed to meet our rising costs and there is no certainty of future levels of support.
- We have seen significant increases in demand in social care and education/schools, which has been the main pressure on our budget in recent years.
- Savings of circa £45m have been delivered over the last 5 years and on current projections we will need to find a further £30m of savings by 2022.
- Newport City Council spends around £8m less than its standard spending assessment, due to its relatively low council tax. So we are a relatively low funded council.

Faced with these circumstances it is appropriate to look at how putting in place a commercialisation strategy can help meet the challenges we are facing.

Adopting this approach requires careful thought as it introduces new activities and different types and levels of risk. This report sets out a proposed framework and a number of proposed actions. Further work will be necessary as part of this approach. In particular, we need to conduct a feasibility study on establishing a company to manage our commercial activity.

Generating additional and sustainable sources of income is very challenging. Cabinet needs to set out a very clear framework, and there will need to be an acceptance that as we are exploring new activities we may not succeed in everything we try. Nevertheless, as this report sets out, developing a more commercial approach is an important element of our ongoing financial sustainability.

It is also important to understand this report is just the first step in creating an overall commercialisation strategy. Further reports will be submitted to cabinet in due course, which will set out in more detail the long term approach. However, as with any new approach, we have to make a start, which is the purpose of this report.

Proposed Framework

Although the adoption of a commercialisation strategy will steer the council into new activities it needs to be rooted in the overall vision set out in the Corporate Plan – "Improving People's Lives". The proposed strategic objectives of the strategy are set out below:

1. We will target activity to promote social value
2. We will prioritise activities to generate a net profit, which can be used to support core services.
3. Our income generating activities should stimulate economic growth by creating employment.
4. Where appropriate, we will modify methods of service delivery to reduce costs to ensure we take a more commercial approach.
5. We will develop new skills in the organisation to create a modern council

Agreeing the objectives will not in itself guarantee success in generating additional income. Careful consideration will have to be given to creating the right organisational environment to nurture innovation and develop robust proposals. This will require active support from Cabinet members and senior managers, involving the following:

- Producing a framework to encourage the development of new propositions
- Capturing lessons learned ensuring they inform future actions
- Adopting a robust project management approach for the implementation of the programme.

Actively moving to adopt a more commercial approach to service delivery is an organisation wide leadership challenge. For this reason, the Chief Executive will lead this work, co-ordinating activity through the Modernised Council programme board.

Priority Opportunities

In 2018 we commissioned a study to identify potential opportunities to form the basis of a commercialisation strategy. Essentially three strands of activity were identified:

- 1) Current services we could provide on a more commercial basis e.g Trade Waste
- 2) New services we could look to provide e.g energy services
- 3) Property investment – commercial and residential

Each of these streams of activity need to be examined in much greater detail with business cases developed for each proposition. If cabinet agrees the outline strategy today the detailed work will commence in due course.

We do however need to reflect on one immediate opportunity – commercial property investment. A proposed governance structure to manage the detailed decision making of investment is outlined below. Cabinet would also need to approve a set of detailed terms of reference and investment parameters for the Investment Board to operate under before any activity in this area. Firstly however, Council would need to approve this broad approach to commercialisation, understanding the high level risks and mitigation associated within it plus authorising the borrowing of funds for this specific purpose, if Cabinet recommends this approach.

Over the last few years, a number of councils have invested in commercial property, both within their municipal boundary and beyond. This generates a rental income, which can be used to support ongoing service delivery. There are numerous commercial property opportunities within Newport and the council should be in a position to invest to help our ongoing budget challenge.

Governance

This part of the report will cover two issues:

- 1) Proposal to create an Investment Board with immediate effect to oversee the development of a property investment portfolio.
- 2) Authority to commission a feasibility study to create a trading company to deliver services aimed at creating a profit in line with the strategic objectives set out earlier in this report.

Investment Board

Developing a property investment portfolio requires appropriate oversight, with a clear process in place to exercise our responsibilities with regard to the use of public money.

The investment board should be responsible for the following:

- Ensuring that investment opportunities are thoroughly evaluated, that there is an appropriate balance between risk and reward and that the acquisition contributes to the overall aims of the strategy.
- Approving property investment acquisitions, property management expenditure, property investment disposals and the provision of finance to enable the council to purchase assets.
- Monitoring the progress made in respect of achieving an appropriately balanced and diversified portfolio of assets and its performance.

The Investment Board should prioritise property acquisitions within the Newport City Council municipal boundary but will have authority to invest outside Newport as well. Detailed terms of reference and investment parameters will need to be established for the Board to operate under. These will need developing and approval by Cabinet. It should be recognised that many authorities have now adopted this approach so we would not be doing anything outside the experience of local government.

The Investment Board will be a sub set of cabinet and function as a public committee with all the associated governance. The recommended membership is as follows:

Members:	Leader Deputy Leader Cabinet Members x3
Advisors:	Chief Executive Strategic Director (Place) Head of Regeneration, Investment & Housing Head of Law & Regulation (Monitoring Officer) Head of Finance (Section 151 Officer) Supported by NORSE as specialist professional advisors

Cabinet will have to decide the level of property investment fund required but a fund of £50m is recommended. The finance section of the report below outlines the issues which need to be considered in more detail.

Establishment of a Trading Company

A number of councils have created trading companies through which commercial activities are managed. There are a number of issues to be considered here and the first step is to commission a feasibility study on the option of creating a trading company. Once this is done a further report will be presented to cabinet.

Financial Summary

This report deals with a number of strands in the Council's approach to Commercialisation:

- (1) A feasibility study on the setting up of a trading company. This study could be funded from the Council's Invest to Save Fund and Cabinet are asked to authorise up to £100k for this purpose, managed by the Chief Executive.
- (2) The setting up of a property investment fund as an approach to generate income. This element, if approved, has significant financial impacts and potential inherent risks associated with it, including:
 - A significant increase in the Council's long-term debt and therefore any income generated would need to be sustained over that period as the 'capital financing costs' would be incurred, irrespective of what happens to the income generated
 - Potential uncertainty in the income generated. These are long term investments and therefore, the property market will change over that period which could introduce risk to the income being generated and/or value of the investment held. For example, whilst investment could have long term leases associated with them, over the long term, tenants could cease trading or enter into company voluntary arrangements to re-negotiate terms.

These will need to be set out to Council, in broad terms, when seeking approval to pursue this approach to commercialisation.

This approach and the taking of commercial risk also needs to be viewed alongside other financial liability's and risks the Council is currently exposed too (e.g. Friar's Walk, city centre regeneration loans and other financial incentives, repayable town centre development funding, home improvement loans) and may increase in the future as it pursue' other objectives, in particular the regeneration agenda. In the context of future uncertainty in funding and significant gap in the Council's MTFP, these are key issues to consider when approving this approach.

Links to Council Policies and Priorities

The overall mission statement of Newport City Council is "Improving People's Lives". The report sets out a clear framework for developing a commercialisation strategy which will need to be aligned to the priorities set out in the corporate plan.

Options Available and considered

Option 1 – Agree the recommendations and framework set out in the report and work towards developing a detailed commercialisation strategy.

Option 2 – Reject the recommendations and retain our current approach to financial sustainability

Preferred Option and Why

Option 1: A number of councils have recognised the need to take more control of their financial position by engaging in activities, which generate additional income. The challenges we face are very significant, therefore we need to look to develop a strategic approach to help us build greater financial sustainability.

Comments of Chief Financial Officer

The broad areas of this commercialisation strategy will require approval by full Council as part of its Capital Strategy. This is required under the Prudential Code, which the Council has a legal duty to adhere to. In this context, the Code requires the Council to be fully aware of the issues and risks around pursuing various commercial strategies and this is met by setting these out in the Capital Strategy. Council approves the Capital Strategy at least once per year and when there is a significant change.

In addition, the report confirms further work that will need to be completed in relation to setting out the Investment Boards terms of references and investment parameters before any activity in this area is undertaken.

Both of the above will provide an opportunity to consider further, and in more detail, the key issues and risk around the approach recommended here and key governance arrangements to manage this.

The financial summary in the main report above sets out some key issues & risks around the pursuit of a commercialisation strategy, in particular, pursuing a property investment fund approach. A key consideration of this Cabinet and Council both now and on-going will be the assessment of:

- (i) The risks and associated reward of the different projects that will come under this, in particular the commercial property element, and the Council's and Cabinet risk appetite for this
- (ii) The increased financial risks associated with this and the capacity to manage and absorb these so that core services to the public are not adversely affected. Key issues which Cabinet and Council will need to consider before progressing this strategy will include:
 - A significant increase in the Council's long term debt which this will entail. This will have to be funded, irrespective of what happens to the income, over a long term period
 - Managing and sustaining a significant increase in external income, which will be needed to underpin core services
 - Poor liquidity of these types of investments i.e. relatively long timeframe to sell / change these investments
 - Context – the current financial risks which the Council is already exposed to, mainly through its regeneration activities
 - Context – the future demand on its core capital programme to support core services and how that might be funded, potentially from further increased borrowing and further income generation

These issues will need to be managed through the appropriate governance arrangements and investment criteria which will need to be developed, as the report sets out. Cabinet and Council will need to understand the above in sufficient detail as the strategy is reviewed further and developed.

Comments of Monitoring Officer

The proposed action is in accordance with the Council's legal powers under the Local Government Acts 1972, 2000 and 2003. The Council has a general power to invest for the purposes of discharging its functions or for prudent financial management under section 12 of the Local Government Act 2003 and can prudentially borrow for this purpose, subject to compliance with Prudential and Treasury Management Codes and the capital strategy. Any investment in property would be in accordance with the Council's general powers to acquire and dispose of property under sections 120 and 123 of the Local Government Act 1972. Any investment decisions would be an executive function for Cabinet and the

Investment Board would need to be established as a sub-committee of Cabinet, with delegated powers. Therefore, Cabinet would need to set the detailed terms of reference and parameters for the Board to take investment decisions. However, the establishment of the £50m investment fund and the commercialisation approach will require a change to the Council's capital strategy and this forms part of the policy framework under the constitution. Therefore, this will need to be approved by full Council, who will also need to agree the risk appetite and the long-term sustainability of the commercial investment strategy as an integral part of agreeing to the establishment of the fund. Any investment policy needs to have regard to the security and liquidity of any investments and the appropriate balance of risk and reward.

The Council has the power to establish or participate in trading companies under section 2 of the Local Government Act 1972 and section 95 of the Local Government Act 2003, in order to provide commercial services to the private sector.

Comments of Head of People and Business Change

Under the Well-being of Future Generations Act (2015) the Council has a duty to have regard to the impact on future generations of decisions taken today, whilst applying the sustainability principles to those decisions – long term, prevention, integration, collaboration and involvement. The report rightly points out the potential impacts and risks associated with setting up a property investment fund. It is important to note that the Well-being of Future Generations Act does not prevent Local Authorities from taking well managed risk and it will be for Cabinet to recommend to Council the 'risk appetite' for this particular decision, taking into account the other financial and service delivery risks currently being managed, along with risk associated with any future decisions. As the report also states, there is already a financial risk due to the continuing budget pressures so there is no 'risk free' option.

The broader development of a commercialisation strategy and approach, as described within the report, supports general delivery against both the Corporate Plan and Well-being Objectives, with a focus on social value, support for core services, economic growth, more sustainable delivery methods and modernisation of the Council.

There are no specific human resources implications arising from this report, although the Local Authority should have regard to the skills and resources required to ensure the inherent risks associated with the proposal can be managed effectively.

Comments of Cabinet Member

The Leader of the Council supports the proposals in this report.

Scrutiny Committees

Scrutiny will comment on an on-going basis.

Equalities Impact Assessment and the Equalities Act 2010

N/A

Children and Families (Wales) Measure

N/A

Wellbeing of Future Generations (Wales) Act 2015

The report seeks to address the requirements of the Well-being of Future Generations Act through implementation of a new commercialisation approach. The aim of this approach is to take well managed risks in order to off-set the long term impacts of continuing budget reductions. The risks associated with this are detailed within the report, as are the impacts of 'doing nothing'. The development of a commercialisation strategy and approach seeks to enable the Council to mitigate the on-going impacts of budget reductions on the long-term prospects of individuals, families and communities. Whilst the other sustainability principles are not explicitly addressed within the report, the commercialisation strategy will seek to address them through a focus on social value, economic growth and new ways of delivering services.

Crime and Disorder Act 1998

Section 17(1) of the Crime and Disorder Act 1998 imposes a duty on the Local Authority to exercise its various functions with due regard to the likely effect of the exercise of those functions on, and the need to do all that it reasonably can to prevent, crime and disorder in its area.

Consultation

Background Papers

Dated: February 27th 2019

