

Establishing Special Purpose Vehicles for Investments & Projects Authorised by the SSDC Investment Assessment Group

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Purpose of the Report

1. To outline and explain the requirement for appropriate delivery vehicles that will enable the Council to lawfully trade in future commercial investment opportunities.

Forward Plan

2. This report appeared on the District Executive Forward Plan with an anticipated Committee date of 7th June 2018.

Public Interest

3. The Investment Assessment Group (IAG), which is a member-officer group, was established to enable the council to act in a commercial way so that it could deliver its Commercial Strategy as agreed by Full Council; and to achieve the income targets set out in the Financial Strategy and MTFP also agreed by Full Council. In doing so the approved governance of the IAG permits only unanimous recommendations for approval of investment opportunities to be put forward to the Chief Executive. In consultation with the Council Leader a decision can then be taken under delegated authority to approve the investment proposal, or otherwise.
4. The investment opportunities recommended for approval are proposed in order to generate income for the Council, as set out in the Commercial Strategy August 2017, to protect and enhance services.
5. Some investment opportunities will require the establishment of a separate company vehicle, either wholly or jointly owned, in order to allow such opportunities to trade lawfully and generate income, which is used to support the provision of public services to our communities and enable our regeneration ambitions for our towns and economy. The setting up of companies or appropriate trading vehicles (such as Special Purpose Vehicles) is only required to facilitate particular investments, where that investment has the support of IAG and the vehicle is considered necessary and appropriate by the IAG.
6. Joint ventures and partnership working in this manner can be beneficial to SSDC as it will support the Commercial Strategy aims and objectives, encourage partner working and investment from other companies, attract external expertise and to reduce risks associated with our investments. This action will help the council to create a more balanced investment portfolio and stable revenue environment for the council to be able to supply services into the future, manage central government financial cuts and become more resilient. This in turn supports meeting the wider council objectives and is relevant and of interest to the public that the council serves.

Recommendations

7. That the District Executive:
 - a) Agree in principle to the setting up of limited companies and/or limited liability partnerships where these are required to discharge Council functions and comply with the approved IAG governance for investments and income generation projects that are either, commercially sensitive, include confidential matters or are time-limited
 - b) Delegate authority to the Chief Executive in consultation with the Council Leader as part of the IAG approval process to give effect to a decision to set up such companies or partnerships, including but not limited to:
 - selecting a company/LLP name
 - approving Articles of Association
 - approving Shareholder or Partnership Agreements
 - appointing individuals to positions of responsibility within the company or LLP
 - c) Recommend to Full Council that Part 3 Section 4 of the Constitution be updated to identify that such matters are the responsibility of District Executive but to reflect the above delegation.

Background

8. In August 2017 District Executive approved the Commercial Strategy which sets out the income generation targets for 2018-2021. The aim of this strategy is to ensure the financial sustainability of SSDC, in light of less financial support from Central Government. The Council invests in order to generate income for services. It is the role of Commercial Services & Income Generation Directorate within the Council to act commercially and investigate investment opportunities and manage existing investments to create an income for the Council. The Council invests the income to support services and council plan objectives. In addition, Commercial Services & Income Generation will seek out new service income opportunities and commercial efficiencies across all of its services.
9. However, since August 2017 it has become apparent that some investment projects will require a company to take the opportunity forward. This is because some investment opportunities will result in trading and profits and therefore need to be placed in a Special Purpose Vehicle (SPV). This may take the form of a Limited Company, Limited Liability Partnership (LLP) or a Partnership, depending on the project's requirements. By taking this route risks to SSDC will also be minimised.
10. The proposal contained in this report is to extend the CEO's existing authority under the IAG to include authority to set up an SPV/LLP, should that be required in relation to an investment project. The intention is that The Commercial Property, Land and Development Manager, or other relevant manager will formulate a proposal for the IAG to include recommendations as to the best vehicle to deliver the project. Where other proposals may require a trading company vehicle but are not commercially sensitive, confidential or time limited, these should be considered through the usual council process. E.g. a SSDC wholly owned company that might be set up for the external trading of council services would not necessarily be considered through the IAG approved process.
11. These details can then be considered by the members of the IAG, who comprise of;
 - Portfolio Holder for Property, Climate Change and Income Generation

- S151 Officer
 - Monitoring Officer
 - Director, Commercial Services and Income Generation
 - Commercial Property, Land and Development Manager
12. It is important to remember that a recommendation to the CEO has to be unanimous, so any one of the above officers or Portfolio Holder may recommend that the proposal should not progress further. The Chief Executive Officer, in consultation with the Council Leader, makes the final decision and retains the ability to refer the decision to District Executive for final decision.
 13. There are a number of different types of company structure that can be considered and these will vary dependent on the type of business or project being proposed. For each project proposal advice will be sought and appropriate company structure(s) considered and recommended.
 14. The proposal report to the IAG for each investment or project will follow the existing due diligence and IAG reporting process and governance. Setting up an appropriate vehicle is seen as an additional step for certain investments within the existing governance. For clarity, if a company vehicle were considered required to enable the investment to proceed, the IAG report will include a reasoned case for the setting up of a company and the recommended type of company arrangement.
 15. Additionally, The advantages and disadvantages of doing so, any risks associated with proceeding and how these risks could be mitigated to minimise risk with a final recommendation, would also be presented. The IAG group will then review and debate the overall report, including the case for needing to set up an appropriate company vehicle and make its recommendation to the CEO in consultation with the Council Leader. As per existing approved IAG governance the final decision can then be taken, or if appropriate the CEO in consultation with the Council Leader can refer the decision to the District Executive if they choose to do so.
 16. It should be noted that not all investment or income generation proposals will require a company set up, this will only be considered as and when necessary; examples include where the project involves trading services, where there are commercial risks that the council might wish to isolate through a separate entity; or there are sound financial reasons in relation to tax that would mean that the setting up of a company would be appropriate.
 17. In the context of the council's latest investment in energy storage, an SPV was considered through a Limited Company and an LLP. A Limited Company set up was advised for this investment proposal between the Council and external project partners. The benefits and differences of Limited Companies and an LLP are outlined below.
 18. However, in future the council may consider, for example, that a Wholly Owned Company for various council trading businesses may be an appropriate way forward and the benefits of this set up would be provided at that time as part of the business case which would follow the District Executive process for approval.

The benefits of a Special Purpose Vehicle are:

- **Isolating Risk** – by holding an asset in a different legal entity it minimises risk as it allows SSDC to isolate the property in question from other assets and liabilities we own. Therefore if the investment fails SSDC is not liable beyond the value of its investment in the SPV. It should however be recognised that there will be perceived links with the Council. In the event that the SPV fails to perform, there will still be a risk of reputational damage to the Council even if any financial risk is isolated. The same point applies equally to the use of an LLP.

- **Flexible Structuring** – SPVs can be structured in different ways for raising capital and/or regulating business activities, depending on the investor and purpose of the vehicle. An SPV can raise capital by issuing shares, and multiple share classes can be created to increase control over it. In certain cases the SPV will be able to raise debt finance directly.
- **Ease of Asset Transfer** – By holding assets in an SPV, property and contracts can be sold in an isolated vehicle instead of considerable time and funds being spent on negotiating contracts, licenses, permits, etc. separately. This allows for named Directors to be changed, shares transferred and changes in ownership if one party chooses to sell their share of the asset in the SPV. Where the Council has a controlling interest the application of public procurement regulations and best value duty still applies.

Differences between an LLP and a traditional partnership are:

Limited Liability Partnerships shares some similarities with traditional partnerships:

- A legal business structure that is set up by two or more people for the purpose of making a profit.
- The internal management structure is very flexible.
- Each partner is taxed as a self-employed individual, rather than the business being taxed as a whole and each partner being paid a salary.

However, there are differences between a Limited Liability Partnership and a Partnership;

- An LLP exists as an individual ‘person’ in the eyes of the law. It has a separate legal identity, so it can enter into contracts in its own name and is responsible for its own debts and liabilities.
 - LLP members are only liable for what they invest or agree to contribute toward the LLP’s debts. Partners in a traditional partnership do not have limited liability, so they are responsible for all debts owed by the partnership.
 - LLPs are subject to stricter regulations and reporting requirements than Partnerships.
19. Deciding which SPV structure to use will depend on the investment being made, whether the entity will be deemed to be trading, and also the regulations that govern the activity being undertaken, also those which govern the Council.
 20. For example, an LLP is not the appropriate vehicle if the nature of the activity is to trade for profit in reliance on the Council’s powers under the Localism Act 2011. Relevant legal and financial officers will seek professional advice and decide upon the best vehicle to use for each case prior to making any recommendation to the Investment Assessment Group (IAG) who will then make a recommendation to the Chief Executive; or directly to the Chief Executive where the IAG is not the appropriate route for decision making.
 21. Therefore this report requests Council to agree and approve an additional step to the existing approved commercial process through the IAG, only when necessary and appropriate, to include the setting up of companies or commercial vehicles within the IAG recommendation. The final decision is then to be taken by the Chief Executive in consultation with the Council Leader; without bringing the proposal of the company set up to District Executive for a decision. Unless the Chief Executive and Council Leader wish to do so.

Legal process and SSDC Constitution:

22. This decision is not considered to be a ‘key decision’ as the financial cost of setting up a company or partnership is not significant in terms of the Council’s budget. It is also considered unlikely that

the setting up of a company or partnership would have any significant effect on communities in the Council's area, particularly bearing in mind that these are largely matters of legal formality.

23. The Council's Constitution is currently silent as to who can take a decision to establish a limited company or limited liability partnership.
24. However, all the powers and duties of the Council which are not delegated to another committee or person (other than those which either cannot be delegated to the Executive or are specifically reserved to the Council) are the responsibility of District Executive. There is no further delegation. (*Part 3, Section 4, subsection 1, paragraph 4.26*). This is, in effect, a provision to cover any function or decision which is not otherwise listed, and to avoid a 'gap' in the allocation of functions.
25. It is considered that this would encompass the setting up of a limited company or limited liability partnership, which would be done in exercise of the Council's general power of competence in s. 1 Localism Act 2011.
26. The Council therefore appears to be in a situation where District Executive is responsible for all aspects of setting up a company or LLP apart from the function of appointing individuals to hold offices in such company or partnership. However, there is doubt on that issue due to the way the Constitution splits responsibility between Full Council, District Executive and the Area Committees and due to uncertainty as to the meaning of "office" and "body". It is therefore considered appropriate to determine that District Executive is responsible for this function.
27. Incorporation of a limited company or set up of a LLP requires registration at Companies House and the allocation of a number to the entity. The company or LLP will need to be given a name and a registered address. In the case of a limited company, directors will need to be appointed and shares will be issued to shareholders. For an LLP, members will need to be selected.
28. The objectives for the company or LLP will need to be established and any limitations on its activities established. The number of directors/members as the case may be that will be appropriate and who (within the Council, or external parties where collaboration between the Council and a third party) should fulfil these roles will vary from transaction to transaction. Likewise as to shares insofar as the number, type and allocation of these is concerned. Directors, shareholders and members each have decision making roles and the allocation and limitations of such powers to them will have to be determined. It may be that a Company Secretary needs to be appointed.
29. A company can have model Articles of Association or it may be that Articles of Association which have been amended to reflect the specific objectives of the company that are required. There may also be Shareholder Agreements which specifically set out the roles and powers of the shareholders. There will need to be an LLP agreement for any LLP.
30. Therefore, District Executive is being asked;
 - To agree in principle to the setting up of limited companies and/or limited liability partnerships where these are required in relation to investment and income generation projects.
 - To delegate authority to the Chief Executive in consultation with the Council Leader, in accordance with the IAG approval process, to take all further steps and actions necessary to give effect to a decision to set up such companies or partnerships, including but not limited to:
 - selecting a company/LLP name
 - approving Articles of Association
 - approving Shareholder or Partnership Agreements

- appointing individuals to positions of responsibility within the company or LLP
 - To recommend to Full Council that Part 3 Section 4 of the Constitution be updated to identify that such matters are the responsibility of DX but to reflect the above delegation.
31. The alternative to delegating authority to the CEO is for investment proposals to be presented to DX for discussion and approval. The risk associated with this route is that it introduces delays in decision making, which might jeopardise the Council's ability to complete deals in time.

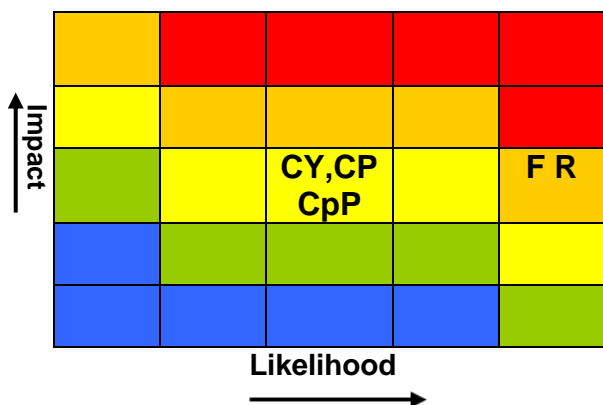
Financial Implications

32. The key purpose of this report is to establish clear and transparent governance together with delegation of powers that enable the Council to establish and participate in alternative delivery models for investments and traded activities.
33. There are no financial implications directly and immediately related to the recommendations.
34. As referred earlier in this report, appropriate specialist legal and financial advice will be used as appropriate to determine whether an SPV is the most appropriate approach for a specific investment or project. Costs in obtaining this advice may be through a combination of using in house and external specialists, and funded from existing budgets and project-specific acquisition budgets.
35. In establishing the SPV, appropriate provisions will also be made for areas such as accountancy and finance advice, financial systems and procedures, tax optimisation and compliance, banking arrangements, insurances, etc.
36. Establishing an SPV may be necessary in order to have the power to trade for profit, and will also be designed to minimise financial risks for the Council. Where an SPV is a joint arrangement this also enables the investment to be supported with relevant expertise and management, and to share risks. An SPV can also limit the Council's direct exposure to financial losses.
37. Costs specifically related to the setting up of a company or LLP, e.g. registration at Companies House, are usually relatively small and would be covered within existing core or project budgets.
38. Granting the Chief Executive delegated authority to decide upon and create an appropriate vehicle, the financial risk to SSDC can be managed through its investment in a separate entity.

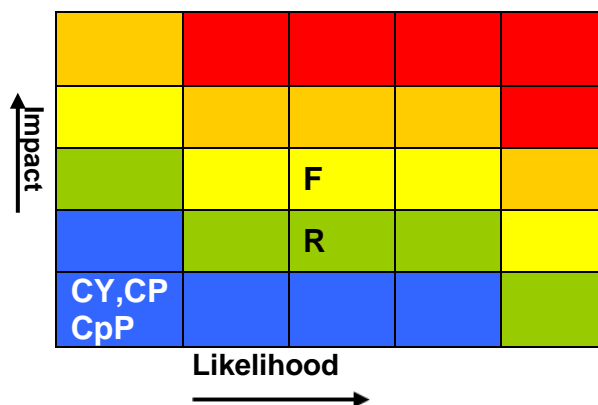
Risk Matrix

39. By approving delegated authority to the CEO in consultation with the Council Leader the Council lowers potential risks of missing out on investment opportunities, resulting in an inability to meet the Commercial Strategy targets.
40. If delegated authority is not given to establish separate companies when required, there is a high likelihood and high impact risk profile as the Council would be exposed to higher risks and have to absorb any failures and the financial and reputational impact of these. However, if an investment is encapsulated in a separate entity, the risk to SSDC is substantially reduced due to all liabilities falling to the Limited Company or Limited Liability Partnership. This would result in a medium impact profile as certain reputational or financial losses could still be associated with the Council, for example if the enterprise failed to recoup the initial investment made by the Council.

Risk Profile before officer recommendations



Risk Profile after officer recommendations



Key

Categories	Colours (for further detail please refer to Risk management strategy)
R = Reputation	Red = High impact and high probability
CpP = Corporate Plan Priorities	Orange = Major impact and major probability
CP = Community Priorities	Yellow = Moderate impact and moderate probability
CY = Capacity	Green = Minor impact and minor probability
F = Financial	Blue = Insignificant impact and insignificant probability

Council Plan Implications

This report links to the following Council Plan objectives

- Actively manage assets and resources to ensure the best financial or community return
- Seek business opportunities for the council
- Work with businesses and use our assets

Carbon Emissions and Climate Change Implications

None

Equality and Diversity Implications

This report has been assessed by SSDC's Equalities Lead as unlikely to have any equality implications that would have a negative impact on either our residents or staff who are from the Protected Characteristics.

Privacy Impact Assessment

In order to set up a Limited Company or Limited Liability Partnership it is necessary to detail names of Directors with Companies House. A joint bank account will also need to be set up, which requires names and signatures of account holders and signatories.

It is not envisaged that any investment company will process personal data.

Background Papers

Commercial Strategy 2017