

Appendix 5

Statements of Clarification Provided to District Executive Following Scrutiny Committee

Why propose a trading company?

The purpose of trading services for a Council is to generate business, leading to additional profits/income; and cost reduction to internal services in some circumstances. The council can only 'trade' i.e. work outside of council core business and make a profit if it sets up an arms-length company vehicle to do so. Which is why this proposal is coming forward, the proposal is the next step in delivering the already approved Commercial Strategy.

Why is council approval needed at this stage?

Without approval for the principle of setting up a trading company, as per the proposed structure in the report and the set up loan funds, we cannot commission the detailed tax advice and legal company set up documents; as there is no budget to do so.

We seek approval now to proceed further in the setting up of a trading company in order to commission the due diligence and set aside loan funds required to do this, covering early set up costs for trading. We believe that this is the amount needed, having considered all that we can at this stage. These next steps and expert advice will answer the detailed operational outstanding questions preparing for implementation to trade as a company.

What are the Costs of a Holding Company (as separate to the trading co subsidiary)?

We acknowledge that there is a cost to the creation of the Holding Company which will be in addition to the trading entity itself. Example costs could include e.g. Director remuneration, Co. Secretary remuneration, cost of accountancy and other expert/management services etc. This is considered to be nominal amount each year and would be recovered by way of a management charge to each of the subsidiary trading companies. This is built into costs at Appendix 3 for the proposed trading company, Elleston, and contingency sums are allowed for in Year 1 until trading is fully underway.

Where is the reference to Governance, Scrutiny and Audit roles?

Appendix 4 refers to Governance, including elements that the external legal adviser has identified. It is the case that we haven't yet identified named individuals as client officers, directors, who will be responsible for monitoring, and what the scrutiny and reporting arrangements will be, as this forms a part of the next steps following the provision of more detailed legal documents including a Shareholder Agreement to be commissioned and finalised.

However, having discussed the proposed delegation with our Monitoring Officer and taken further legal advice the following applies. Under our council constitution appointments to outside bodies should be made by the relevant Portfolio Holder. In this case the Holding Company and Trading Co would constitute 'outside bodies' and therefore fall under the remit of District Executive. Therefore, for this specific element it is proposed that an additional recommendation is added to the District Executive report (final wording agreed at DX) **'to note**

delegated authority to the relevant Portfolio Holders to make the initial appointments to the 'outside bodies' of Holding Company and the Local Authority Trading Company.

Once set up, a Council wholly owned company would act as any other private limited company and have its own governance, audit and reporting procedures to the Board of Directors and regularly report back to Shareholders. The Council is the Shareholder and under the Shareholders Agreement will be able to agree, (once it is drafted) how the company is run and who holds the key decision making responsibilities. Therefore, this is not something that officers can provide answers to at this time. It is proposed that expert legal advice and best practice will be followed in due course.

The initial delegated authority in the recommendations is proposed to 2 senior officers with the relevant expertise in this field and the 2 portfolio holders involved in the proposal if/once the principle to take forward and the loan is approved. This is in order to drive forward the detail in a commercial manner. The S151 officer is there to ensure funds and governance are appropriate following due diligence. The Commercial Director to ensure that only a viable commercial proposal in line with the approved Commercial Strategy proceeds. If the proposal after due diligence is not financially sound, with appropriate governance or in line with approved strategy, then it would be the duty of the senior officers to revert to PFHs and agree not to proceed, or what further work is required prior to the implementation of the company proceeding.

What are the Next Steps?

In officer opinion **the headline next steps** (if recommendations are approved) would be to:

- Commission the detailed corporate and VAT tax advice, in order to build in refined financial provisions to the company business plan financial forecast. This will be funded through the set up loan. S151 Officer to approve the advice and implement.
- Commission the detailed suite of legal documents to allow formal company set up.
- PFHs to initially consider and agree the initial Shareholder Agreement and legal documents, with key officers obtaining expert advice on the implications of key decision makers, rights and responsibilities of Shareholders and the make-up of Board of Directors.
- To register the company and proceed to implementation once all proposed governance and financial set up is agreed and the proposal is considered acceptable by PFHs in consultation with S151 and Commercial Directors. Scrutiny Chair and Deputy to be briefed in advance.

Elleston Financial Forecast, VAT & Tax – Is the loan request sufficient?

The S151 has reviewed the financial forecast and is content. The S151 & Deputy have received advice on the VAT position and are content. However, further specific advice is required from an external specialist on the wider tax position, especially corporation tax. But for the present purposes, the worst case tax position has been taken into account in the Financial Forecast and the S151/Deputy are content with that.

Where are the Objectives of the Holding Company?

We consider these are set out in the report– sections 10 & 13 specifically refer.

Other Clarifications and Queries to more general queries raised:

- Each future trading service proposal will be brought through DX and Scrutiny prior to proceeding any further.
- The company will be required to have an external audit, which would be reported back to Shareholders.
- Group accounts for the council will need to be produced, including the company. These will also be considered by Council's Audit Committee.
- General 'scrutiny' and oversight of the company operations going forward would be undertaken through the Shareholder Group (or their agreed representatives) and the Board of Directors will be answerable to Shareholders.
- For 'Cabinet' in the report read 'District Executive' (external legal advisors have used generic terms in their advice to us as not all councils have/use the term District Executive)
- Risk – This has been viewed in the report as positive or 'opportunity' risk as a 'shell' ltd company is proposed in order to trade, we believe that we have mitigated potential financial or reputational risk. Through this proposal there are no staff assets or substantial capital in the company. It is an arms-length and separate legal entity to the council.

However as with every new venture there are risks, in this case the financial risk is the set up loan funds requested and the reputational risk if the worst case scenario happens and the company is unsuccessful. Potential clients are already asking and waiting for SSDC (Elleston) to be able to trade and contracts will be priced to ensure that they are profitable, we believe that the risks are lower in beginning our trading services in an area of demand for which we already have experience and strong reputation. The risk of failure cannot be completely mitigated and should be noted.

- Examples of other council trading are noted in the report and have been investigated to provide lessons learned and best practice on the company set up structure and to advise what has worked well or not so. We are following this advice which also concurs with our expert legal advice to date in terms of the company structure and necessary due diligence on financial forecasting and legal company set up.