

PLYMOUTH CITY COUNCIL

Subject: Proposal for a Plymouth City Council wholly owned agile Company

Committee: Cabinet

Date: 7 March 2017

Cabinet Member: Councillor Darcy

CMT Member: Andrew Hardingham (Interim Joint Strategic Director for Transformation and Change)

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Ref: SRA/CoLtdG08022017

Key Decision: No

Part: I

Purpose of the report:

The Council is embracing financial challenges in driving up revenue, reducing cost, utilising the full range of its resources and assets whilst ensuring customers receive high quality services and value for money. The purpose of this report is to set up a flexible, scalable wholly owned Teckal style company to allow the Council to take advantage of innovative solutions to a broad range of financial challenges it currently faces and may well face in future.

Initially this report seeks the approval to set up the company. There will be a series of challenges over the medium term financial planning horizon. This report addresses the first challenge associated with the investment in the City Market.

The City Market investment will cost in the region of £4.1m (£3.4 net of VAT) and sets out the Council's ambitions to provide a high class city market. The City Market is a historic asset that will continue to support the local plan and sustain and grow the economy in the west of the city whilst also ensuring the physical building can also be enjoyed by future generations.

In order to ensure the affordability of the project it is important that the Council can recover the tax. The Council cannot "opt to tax" the site because this would have a significant impact on the market traders, most of whom would not be able to recover the tax harming the financial vitality of the City Market. The report sets out the financial model operated through the company that will enable the capital investment whilst ensuring the City Market economy is not hindered. This will include leasing the City Market to the Company using a peppercorn rent. The Council will continue to operate the City Market.

As further challenges need to be resolved or opportunities arise separate business cases will be required to seek Cabinet approval to expand and broaden the business of the company.

The Corporate Plan 2016/17 -2018/19:

The Council continues to adopt a pioneering approach to find flexible and innovative solutions to the challenges it faces, some of which are technical finance issues whilst others will resolve operational challenges to ensure best value for customers and the citizens of Plymouth. Adopting a strategic forward thinking approach will also ensure the company is set up to adapt, flex and ensure scalable solutions. Protecting the City Market investment will also create a financially sustainable model so that shoppers and visitors to the City Market can enjoy it for years to come whilst enabling the traders to flourish.

Implications for Medium Term Financial Plan and Resource Implications: Including finance, human, IT and land:

There will be a range of direct and indirect financial implications relating to the setting up of the company and its first innovative solution and these are set out below.

1. The cost of setting up the company will be in the region of £29k covering all legal, tax, financial advice and the company registration.
2. The company will have nominal running costs of £10k and will operate with Council staff seconded for the purpose of getting the company running. As each initiative is scoped and developed any expansion of the running costs together with associated operational costs and revenues will need be quantified and included with a cost benefit, risk assessment and options appraisal as part of a separate business case to inform any decisions to expand the business of the company.
3. The cost of creating the sustainable financial model for the City Market will be in the region of £24k. This will include all the work on the required lease arrangements
4. The company will need to access funds to meet its peppercorn lease obligations of maintaining the asset. Therefore, a transfer of planned maintenance budget from the City Market trading account to the company will be required or the ability for the company to draw down on a case by case basis the cost reimbursement of any maintenance required. The impact of this will be cost neutral as the company can only draw on the resources contained in the City Market budget.

Other Implications: e.g. Child Poverty, Community Safety, Health and Safety and Risk Management:

There are no material risks associated with the creation of the company. Using a business case proposal for each proposal to expand the business of the company allows risks to be considered on a case by case basis as part of the decision making process.

There are some risks associated with the proposed City Market arrangements. These relate to the compliance with legislation and taxation policies. To mitigate these professional advisors have been advising Council officers on ensuring the correct arrangements are put in place to set up the company and associated lease arrangements for the City Market.

Equality and Diversity:

Has an Equality Impact Assessment been undertaken? An Equality Impact Assessment has been completed and no adverse impact will arise as this is a technical finance adjustment. There will be no adverse implications for City Market traders, tenants, shoppers, visitors or the employees at the City Market resulting from the decisions in this report.

Recommendations and Reasons for recommended action:

Cabinet is recommended to

1. Approve the creation of a flexible and scalable company limited by guarantee wholly owned by the Council to enable financial solutions to challenges the Council faces.
 2. Approve the process of a case by case Business Case as the authorised method of expanding the company's portfolio.
 3. Approve the business case for the City Market to protect the economic vitality of the city market whilst preserving the building for future generations to enjoy.
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Alternative options considered and rejected:

The following alternative options were considered and rejected

1. Do not set up a company and seek to utilise the Council's existing powers. Whilst this approach will always be the primary route to resolve challenges the Council faces it is not always possible to solve challenges without innovative solutions.

In relation to the challenge of the City Market:

2. Do nothing. This would result in triggering the Councils 2016/17 and possibly the 2017/18 5% partial exemption limit costing the Council in the region of £1.5m for both years.
3. Opt to Tax and pass on the tax. This would enable the Council to recover tax on the City Market investment but would then add tax of 20% to fees and charges which the majority of traders would not be able to recover, potentially harming the economy.

4. Opt to Tax and absorb the tax which would reduce the City Market income by £0.180m per annum impacting on the ability to repay the capital borrowing charges for the City Market investment without earlier and more substantial increase in fees and charges.

Published work / information:

None

Background papers:

Title	Part I	Part II	Exemption Paragraph Number							
			1	2	3	4	5	6	7	
Equality Impact Assessment	x									

Sign off:

Fin	djn16 17.7 7	Leg	AT27 575	Mon Off	LT27 576	HR	n/a	Assets	n/a	IT	n/a	Strat Proc	n/a
Originating SMT Member													
Has the Cabinet Member(s) agreed the content of the report? Yes													

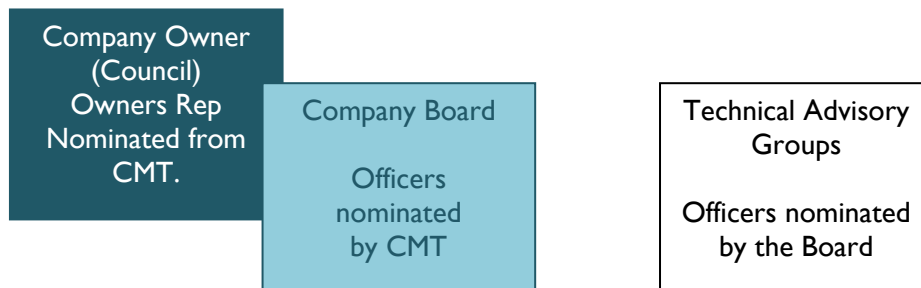
Introduction

- 1.1 The Council is embracing financial challenges in driving up revenue, reducing cost, utilising the full range of its resources and assets whilst ensuring customers receive high quality services and value for money. The purpose of this report is to set up a flexible, scalable wholly owned Teckal style company to allow the Council to take advantage of innovative solutions to a broad range of financial challenges it currently faces and may well face in future.
- 1.2 This report addresses the following two issues; the company itself and the company business for which the first financial challenge of the City Market is also contained in this report. The report sets out both in more detail.

2. The Company

- 2.1 The company will be a Teckal company limited by guarantee wholly owned by the Council. As a company limited by guarantee there will be no distribution rights.
- 2.2 In order to ensure the company is agile, flexible and can be scaled, care will be needed to ensure that it has the scope and support to respond to a range of financial challenges the Council is facing, some borne out of operational or financial necessity and some to address technical financial challenges and others to take advantage of opportunities.
- 2.3 Therefore, the company will need to deal with the following range of potential challenges and opportunities
 - Technical Financial Solutions
 - Cost Reduction Initiatives
 - Revenue generation
 - Trading potential
 - Potential to perform activities more effectively and efficiently
- 2.4 The company is not an off the shelf model so there will be some set up costs to ensure the company is scoped to deal with the range of business the Council may need. The set up costs are estimated in the region of £29k which will include the tax and legal advice and the company registration.
- 2.5 The company will initially cost no more than £10k to operate annually with most of the support coming from seconded officers.

- 2.6 A business case will be required for each decision to use the company setting out the challenge or opportunity, the financial and legal position, a cost benefit appraisal and a record of the risks.
- 2.7 As each business case is approved and the company grows and diversifies there will be a need to consider the operational costs and revenues associated which will need to be reflected in the company business plan. Generally, it is anticipated that the operational funds will exist in the council's budgets already or the solution being sought will generate the resources. In addition, it will be necessary to consider the underlying running costs of the company as part of each business case to ensure the company remains fit for purpose.
- 2.8 As a wholly owned company limited by guarantee there will be one owner which will be the Council. The Council owner will be represented by a Council Officer. A board of directors will be set up to manage the company with the scope to draw on a number of council officers to fulfil these roles based on the scale, diversity, experience and skills needed to run the company. Technical Advisory Groups (TAGs) may be required to support the board. Officers of the council may be seconded to support the company although the company will be set up to have the potential to have direct employees as and when required. The role of the Technical Advisory Groups (TAGs) is to support the Council in the production of business cases for including new business in the company and then updating the Companies business plan and monitoring progress. The TAGs will pull together relevant subject matter experts.



3. Business of the Company – Business Case

- 3.1 The company purpose will be set up with a wide remit to cover the range of potential solutions needed. However, each decision to introduce new activity into the company will require a business case covering
- Activity
 - Business Driver (rationale for the opportunity or solution being sought)
 - Options and Proposed Solution
 - Capital, revenue and Tax implications
 - Financial appraisal (cost, benefit, investment, return on investment or cost avoidance)
 - Resources needed (non-financial)
 - Risks
 - Impact on the company

3.2 Business cases will be prepared for decisions made using the Councils scheme of delegation. If a business case is approved then the activity will be included in the Company business plan, operationalised and delivered, reporting back to the Council via the Company structure.

4. Business Case – City Market

Activity

4.1 The City Market is a historic building in the West of the City providing an important, thriving and vibrant economy for traders and shoppers. The City Market has turnover of over £1m pa, creates over 200 jobs and achieves occupancy of 95%+ let on a consistent basis.

Business Driver

4.2 The City Market is not only an economic hub for the west of the City but a historic asset in its own right and a key part of the Plymouth Plan aspiration to attract investment to the area. Therefore, it is important to maintain and invest in the asset for future generations

4.3 The current investment in the City Market is costing £4.1m (£3.6m net of tax). In order to ensure the investment is affordable it is imperative the tax is recovered without adversely impacting on the market traders and perimeter shop tenants, either directly or indirectly. In addition, the Council needs to ensure it's tax planning is efficient to ensure it complies with tax limits.

4.4 There is also a need to ensure the bottom line on the City Markets financial activity is not affected as this underpins the financial model to support the borrowing associated with the investment in the City Market.

Options and Proposed Solution

4.5 There a range of options as set out below:

4.6 Option 1. Do nothing. Investing in the City Market at £3.4m and recovering £0.6m exempt tax would result in the Council breaching its 5% tax limits triggering the wider corporate £1.5m clawback of tax.

4.7 Option 2. Opt to Tax the site. This would allow the Council to recover the tax without triggering the 5% tax limit. However, it would result in charging 20% to the fees, charges and rents which would have an adverse impact on the traders who would not be able to recover the tax. This could impact on the 95% occupancy rate diminishing the financial viability and therefore the overall ability to continue to invest in maintaining the asset for future generations to enjoy.

- 4.8 Option 3. Opt to Tax the site and absorb the ongoing tax. This would also enable the Council to recover the tax on the investment. The Council would have to charge tax on the fees, charges and rents but instead of adding 20% the Council could keep the charges as they are and pay over the tax. This will effectively reduce the income the City Market receives by £0.180m pa and as option 2 reduces the resources for maintaining the asset for the longer term
- 4.9 Option 4. Split the City Market site into the superstructure and the floor within. Complete all investment works recovering the tax. However, this results in some tax being recoverable and some included within the 5% exemption calculation. The exempt element can be contained in the 5% exemption calculation without triggering it, thus avoiding a potential £1.5m liability. The Council then issues a peppercorn lease to the company for the superstructure together with the responsibility for maintaining it for the benefit of future generations. The Council continues to operate the City Market activity, without adversely impacting on the market traders and tenants thus supporting the local economic growth and potential for inward investment.
- 4.10 Option 4 is the proposed option for recommendation.

Capital, Revenue and Tax Implications

- 4.11 The capital investment in the City Market has already been approved by The City Council Investment Board (CCIB) and is contained within the financial resources approved by the Council. The project is underway and is due to be finalised early in 2017/18. This report is not seeking to revisit this other than to ensure the project is delivered within the financial resources without impacting on traders whilst remaining within the Councils financial and tax planning limits. Therefore, this business case is concerned with the options to remain within the financial and tax planning limits without impacting further on traders beyond the CCIB business case to seek investment in the City Market.
- 4.12 There are no capital implications associated with the preferred option 4.
- 4.13 There will be a revenue implication but this will be contained within existing revenue resources. Essentially the company will need to insure and maintain the City Market superstructure. There are two options for this. Option 1. Pass the budgets from the City Market account to the Company. Option 2. Set up a cost reimbursement process for the company to claim back maintenance costs.
- 4.14 The company will not be registered for tax so there will need to be careful consideration for the activity it undertakes.

Financial Appraisal

- 4.15 The preferred option will cost in the region of £23k to construct the leases. This will preserve both the £180k of potential lost tax the Council would have to absorb and also ensures the Council does not trigger the 5% exempt tax limit which would result in a repayment of £1.5m of tax.

Resources Needed

4.6 In order for the Company to successfully take its responsibilities for insuring and maintaining the City Market superstructure it will need access to existing revenue budget. In addition, the subject matter experts will need to support the Company Board on matters relating to the City Market superstructure, this is expected to be on a secondment basis and part of the current ongoing activity of existing employees from within Economic Development (Commercial Surveyors)

Risks

4.7 The following risk matrix sets out the key risks and mitigation of the preferred solution:

Ref	Risk	Initial Probability	Initial Impact	Mitigation	Mitigated Probability	Mitigated Impact
1	Risk of City Market Traders being adversely affected	Medium	Medium	The proposed option solves the risk of the City Market traders and tenants from being subjected to a 20% increase in fees, charges and rents they would have to pay	Low	Medium
2	Risk of financial viability of the City Market	Medium	Low	The proposed solution makes the financial model cost effective for everyone. The capital investment is both affordable and tax efficient and does not result in further borrowing. A financially viable financial model maximises the maintenance funds for the improved asset	Low	Low
3	Risk of triggering the 5% exempt tax limit and having to pay £1.5m	High	High	The proposed option allows the Council to ensure financial planning complies with the 5% exempt limit without impacting on the traders/tenants.	Medium	High
4	The risk that HMRC will challenge the approach being taken by the Council in setting up the company and giving it the responsibility for the City Market Superstructure.	Medium	High	Tax and Legal (QC) advisors assisting in setting up the company so it has clear purpose and function. The arrangements for the City Market peppercorn lease fall within widely accepted HMRC concessions.	Low	High

Impact on the Company

4.8 The company will need to set up a Technical Advisory Group drawn from Economic Development, Legal and Finance to support the company with this business case and the transition from the Council to the company to ensure the impact on City Market traders, tenants, shoppers, employees and the financial position are all preserved.