

## **OVERVIEW AND SCRUTINY**

<b>DATE OF MEETING:</b>	<b>18 AUGUST 2020</b>
<b>TITLE OF REPORT:</b>	<b>THE ESTABLISHMENT OF A CORPORATE VEHICLE FOR PROPERTY HOLDING PURPOSES</b>
<b>Report of:</b>	<b>JOINT CHIEF EXECUTIVE</b>
<b>Cabinet member:</b>	<b>Councillor Radley</b>

### **1 PURPOSE OF THE REPORT**

- 1.1 To recommend in principle the creation of a local authority company to allow commercial trading in property. The objective is to have a flexible corporate vehicle into which residential and commercial property may be transferred and held for investment purposes.

### **2 RECOMMENDATIONS**

- 2.1 Overview and Scrutiny Committee is asked to support the following proposed officer recommendation to Cabinet:
- a) Cabinet agrees in principle to the establishment of a company which would be limited by shares and owned wholly by the Council.
  - b) Cabinet agrees to a further report to be brought forward at the earliest opportunity outlining proposed governance and board membership arrangements, and articles of association for the company before any trading activity commences.

### **3 BACKGROUND**

- 3.1 In 2018 the Council agreed a 'strategic business case' for progressing the Commercialisation project across the Council. Three key themes were agreed one of which was to increase income broadly via asset based investments with the objective being to secure long term additional income returns rather than capital growth. At the same time the Council set an overall budget of £50m to fund the procurement of revenue generating assets. Pursuant to this the Council has sought to develop a mixed portfolio comprising: The Pavillion Office in Eastleigh and in 2021 it will take possession of 41 flats for affordable rent at Edenbrook.

### **4 THE REASON FOR THIS REPORT**

- 4.1 Local authorities have a range of powers to acquire property that can be operated on a commercial basis and the Council already has the ability to trade without needing to start a wholly owned Company. However, if a local authority acquires a residential property and then lets the property, the

residential tenant will effectively become, by default, a protected tenant – i.e. they will have enhanced rights of occupation and over time potentially acquire the right-to-buy. Local authorities, cannot, except in very rare circumstances grant assured short-hold tenancies. If such provisions were maintained it would undermine the purpose for which the Council has sought to base its commercialisation strategy and to procure residential properties.

- 4.2 To protect the Council's objective to retain long term income streams rather than capital growth, the tried and tested solution is to set up a separate legal entity (a Local Authority Trading Company) into which the properties are transferred and held. Many authorities have established similar such entities with the Company being wholly owned by the Council with the Council as the single shareholder. Such arrangements puts the Council in total control over the operations of the Company.

## **5 THE PROPOSAL**

- 5.1 It is intended that a trading company is established immediately so that trading activity can commence at the beginning of the next financial year (2021/2022) with the Council taking possession (at the end of April 2021) of the 41 flats at Edenbrook. At the same time the The Pavillion Office at Eastleigh would also be transferred to the new company.
- 5.2 In terms of process the Local Government Act 2003 requires a full business case to be approved before trading commences. At this stage, this report is simply intended to establish the principles of trading and the company itself with potential governance structures, board membership details and business case information provided in a further report to Cabinet.
- 5.3 The final governance arrangements for the Company will require careful consideration. By way of principle it is often recommended that any directors be formed of Council officers (Southampton City Council's trading company is a local example). Ultimately it will be matter for the Council whether elected members are also appointed as directors. There are however, two key issues to be considered. The first is the practical disadvantage in that elected members are likely, at times, to find themselves in a conflict situation through both being an elected member of the Council as well as a company director, which brings with it a personal legal duty to act in the best interests of Company. The second more practical concern is the relatively more transient nature of Member's tenure in Office or in their respective roles at the Council – this may give rise to the question of the longevity of individual Member's tenure as a Director. It is not something that should be determined on an annual basis.

## **6 LEGAL AND STATUTORY IMPLICATIONS**

- 6.1 There are a number of legal and statutory implications which the council needs to be aware of in regards to establishing a wholly owned company for trading purposes. Legal advice has therefore been sought about how the Council should go about setting up a trading company and this advice is attached as a Confidential appendix to this report.

## **7 RESOURCES**

- 7.1 There are no additional resource requirements to deliver this programme of work in setting up the trading company. All activity within the company will fully recover costs. The proposal itself is intended to develop new income streams for the council. There will however be a small cost in setting up the company and in complying with the regulatory framework for limited companies but that can be reourced through existing budgets.
- 7.2 The council must recover the full cost of any accommodation, goods, services, employees or anything else it supplies to the company in pursuance of any agreement or arrangement to facilitate the power to trade. The majority of this will be accommodated within the hourly rate charged between the council and the company.
- 7.3 One of the specific reasons behind the formation of the trading company is to help secure additional income which will help support the core functions of the council in the longer term. Any commercial activity comes with a degree of financial risk and needs to be managed and understood.
- 7.4 At this stage it is only the principle of the company formation that needs to be agreed, the approval process of the detailed business plans will identify the financial risks and potential returns in more detail.
- 7.5 The company will operate using existing council staff and where appropriate other external resources rather than having directly employed members of staff.
- 7.6 The recharging of staff time from the company to the council provides a mechanism to ensure that the full costs are applied to the company and that there are no issues around "state aid" or uncompetitive practises being used.

## **8 MAJOR RISKS**

- 8.1 The operational risks associated with setting up a local authority trading company are more around the financial returns and the ability of the business to deliver the expected benefits.

- 8.2 The detailed business case for the company will contain a risk assessment with details of the risks that have been identified and what mitigation action has been or will be taken to minimise that risk. The financial risk is considered to be limited given the scale and nature of the business during the initial business plan period.
- 8.3 Overall it is considered that the risk associated with the actual formation of the company is low and that the trading activities and resultant impact on the council will be beneficial.

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**CONFIDENTIAL Appendix 1** - Advice on the establishment of a corporate vehicle for property holding purposes (Freeth's Solicitors)