Outline Business Case

for Funding to Convert STG Consultancy

into an Local Authority Trading Company (LATC)

Version 3 – 19 May 2016

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[Glossary of terms to be added later]

1. INTRODUCTION

1.1. Following the presentation by Trowers & Hamlins to Joint Committee in October 2015 Members and Steering Group officers requested a report to be taken to December's meeting indicating how progress could be made in developing the Local Authority Trading Company (LATC). It was agreed that set up costs would be in the region of £50,000 to £60,000 and that the partner authorities could fund this through an invest to save type loan which could be repaid over a specified period of between three and five years.

1.2. In order to agree this sum of money through their respective Cabinets, they would require an outline Business Case indicating the potential income and repayment methods together identifying any associated risks. Members requested that this Business Case be brought back to the March Joint Committee. It was agreed that given the timescale and the level of expertise required a sum of £6,000 would be provided by the three authorities (£2,000 each) to fund the engagement of consultants to assist in the delivery of the Business Case.

2. BACKGROUND

2.1. The original concept of developing our consultancy services was to use the skills and expertise within the existing staff to provide additional and complimentary services to the building control service which would generate additional income for the partnership.

2.2. The original services offered related to energy assessments (SAPs, SBEMs, Trade-off calculations), access statements, fire risk assessments and party wall agreements. In 2011 the consultancy began delivering decent homes surveys for the housing department at Medway Council and from then has developed a number of additional surveys including; stock condition surveys, scoping surveys and fire risk assessments for both communal areas and individual flats. The successful collaboration with Medway's Housing department culminated in a service level agreement for the consultancy to deliver stock condition surveys over the next two years.

2.3. The development of this work, which began by using shared resources of existing building control staff, developed into a more appropriate use of specialised skills through the engagement of stock condition surveyors. This both enhanced the product we were able to provide to Medway and released the building control surveyors back for use in the building regulation service.

2.4. Over the years a number of staff have left the partnership often taking those specialised skills with them but this new model of using specialised staff to deliver these additional services has become more viable now that markets are beginning to be established. In order to maintain the resilience of the partnership it was identified, following the financial crisis in 2008/09, that additional income streams were important and investigations began into how changing the delivery model of the consultancy could achieve surpluses or profits being generated which could be repaid to the partner authorities.

2.5. In 2009/10 a number of exercises were carried out with KCC Commercial Services to identify how that organisation was set up and what the benefits to the partnership could be. This included several meetings with KCC's Commercial Director and advice from their legal team.

2.6. Whilst formation of a Local Authority Company was discussed it was felt, at that time, the partnership needed to mature and develop potential markets.

2.7. Since 2011 further powers have become available to Local Authorities and Central Government have encouraged spin offs into the commercial sector. A number of presentations by both Government led and private companies seeking to advocate the development of Local Authority Companies, mutual's or social enterprises were attended. Following a presentation by Trowers & Hamlins, a connection was re-established with the legal company, who previously gave advice on the original setup of the partnership.

3. OVERVIEW OF CONSULTANCY SERVICES

3.1. The consultancy currently provides the following services:

- SAP & EPC assessments
- Trade Off assessments
- Code for Sustainable Homes Standards (report)
- SBEMs
- DECs
- Stock Condition surveys
- Decent Homes scoping surveys
- Decent Homes compliance surveys
- Access Statements

3.2. In the main the energy assessments are carried out for applicants from the private sector and the housing surveys are provided for Local Authority Social Housing departments.

3.3. An excellent working relationship has now built up between Medway's Housing department and STG culminating in a Service Level Agreement for the next two years. A number of approaches have been made to Gravesham Council in respect of carrying out similar survey work but unfortunately to date nothing has been arranged. However, emergency cover for a vacancy in Private Sector Housing has been arranged for a temporary period until full appointment can be achieved.

4. LEGAL FRAMEWORK

4.1. Section 102 of the Local Government Act 1972 enables two or more local authorities to set up a Joint Committee (JC) to discharge their functions jointly. These arrangements must comply with the Local Authorities (Arrangements for the Discharge of Functions)

(England) Regulations 2000. JCs may be decision-making or advisory. The councils concerned set the numbers of councillors, terms of office and geographic areas of operation of joint committees. JCs have no legal status, cannot impose financial obligations on their constituent authorities, and have no powers to levy council tax. JCs would not be a separate legal entity therefore they cannot own assets, have liabilities, raise taxes, enter into contracts or employ staff. Employment of staff, entering into contacts and other operational matters would be delivered via a lead authority using a Local Government Act 1972 Section 113 agreement or an arrangement under the Local Government (Goods and Services) Act 1970. Alternatively the authorities could create a jointly owned and controlled company to perform functions.

4.2. Section 95 of the Local Government Act 2003 enables local authorities to provide on a commercial basis, anything that is related to a function of the authority. The powers under the Act enable Local Authorities to trade with private bodies and persons for profit (i.e. charges fixed at more than the cost recovery) through a company. Surpluses on commercial operations under the section 95 trading power would be available to individual authorities.

4.3. This legislation has been further strengthened by the Localism Act 2011, which expands Local Authority's trading activities to areas not related to their existing functions and removes geographical boundaries so trading can take place for a variety of service provisions and anywhere in the UK through a company.

4.4. A local authority must prepare a business case before embarking upon commercial trading (The Local Government (Best Value Authorities) (Power to Trade) (England) Order 2009).

4.5. Normally, the provision of services over certain values from a company to a local authority is subject to the public procurement regime set out in the Public Contracts Regulations 2015. There is an exception to this rule that means, in certain circumstances, a contract let by a local authority to a company it owns will not be deemed to be a contract for the purposes of the public procurement regime. This exception is known as the "Teckal" exemption and was established by a European legal case but is now set out in section 12 of the Public Contracts Regulations 2015.

4.6. In order to be Teckal compliant (and exempt from the procurement rules), the company would need to abide by the Teckal rules which are:

- the company should be controlled as a department of the local authority;
- the major part of the company's business must be with the local authority owner (80% of revenues); and
- there is no private sector ownership of the company.

4.7. A local authority has statutory powers to form companies jointly with other local authorities under Section 73 of the Local Government and Housing Act 1989. Local authority regulated companies fall into 4 categories:

- controlled companies - the local authority has the ability to control a majority of votes at a general meeting or has power to appoint or remove a majority of the board of directors;
- arms length companies - a controlled company as above, which has made a resolution to be "arms length" for a particular financial year and certain conditions have been met;
- influenced companies - there is a business relationship between the company and the local authority and the authority has a least 20% of the voting rights or number of directors. A business relationship will exist if more than half of the company's turnover or funding is related to that local authority; and
- minor interest companies - all other companies where a local authority has shares/interest in.

4.8. There are statutory controls on controlled companies, arms length companies and influenced companies; the key provisions are listed below. These controls do not apply to minority interest companies:

- identify on company documents (e.g. business letters, notices) that it is a controlled or influenced company;
- limitations on director's allowances and board membership for councillors;
- must provide information to the local authority, auditor and to councillors;
- controls over the appointment of auditors;
- restrictions on publishing political material;
- public inspection of minutes (unless arms length company);
- internal financial controls and accounting required by the Chartered Institute of Public Finance and Accountancy's "Prudential Code for Capital Finance in Local Authorities (CIPFA Code). Generally, the Local Authority behind a controlled, arms length or influenced company must include the company's accounts as part of its own group accounts.

4.9. Regulated companies may also be treated as “public bodies” in relation to the following legislation:

- Freedom of Information Act and Environmental Information Regulations
- Human Rights Act
- Equality Act
- Public Contracts Regulations

4.10. Members of a jointly owned local authority company will need greater controls than the Companies Act 2006 provides so the model articles of association would need to be revised for such a company. Additional controls can be added to meet the Teckal test.

4.11. A shareholders' agreement would also provide for equal participation and control by each relevant authority in a joint venture local authority company. Through a shareholders' agreement between the partnering authorities can:

- provide for decisive influence over both strategic and significant decisions of the company;
- exercise similar control jointly;
- establish governance procedures to ensure effective joint control and show that the joint control has not been delegated

5. CASE FOR CHANGE

5.1. Both the chargeable and non-chargeable accounts are required to be delivered at cost without the opportunity to make surpluses. Should any surpluses arise we are unable to use them to fund cross-functional support or use it outside the building control account.

5.2. The development of the consultancy and its widening portfolio of services provides the opportunity to make a profit but again is prevented from doing so by the legislation it currently operates under, which prevent profit making for the provision of discretionary services to the private sector. However, both the legislation and the markets have changed since 2010 when it was introduced giving greater opportunity and freedoms to commercialise the provision of these services through a LATC.

5.3. Since its inception the partnership has been successful in reducing the partner authority contributions through each Business Plan. The percentage reduction has had to reduce over the years as it is based on the time spent on public protection services and information. The opportunity to further improve efficiencies in this area will become increasingly challenging, particularly given the general increase in workload currently being experienced and therefore any further significant savings could impact on the service that could be provided. Therefore, an alternative method of securing efficiencies would be preferred to bring about any further reductions in each of the partner authorities contributions.

5.4. The consultancy has been able to offer complimentary services to the building industry and therefore increase STG's ability to compete with the private sector. By moving the operation into a LATC there are a number of advantages including;

- Being able to trade in the wider market
- Generate further economies of scale and provide greater efficiency
- The ability to return revenue to the partner authorities through profitability
- Creating a more commercial culture
- Retaining staff knowledge and expertise within the company
- Safe guarding jobs via diversification and contractual commitments
- Reducing procurement costs by taking advantage of procurement exemptions available for contracts between local authorities and Teckal companies

6. THE ECONOMIC CASE

Critical Success Factors

6.1. The consultancy must be able to deliver quality products over a wide and expanding number of services. This is very important to maintain a good reputation in delivering what the customer wants in an agreed timescale so that expectations are met.

6.2. It is also important to have clear responsibilities, well documented and accepted by both parties so that both the client and the practitioner are in agreement of what can be delivered and by when.

6.3. Consideration must be given to improve market share but not at the cost of compromising existing services so that critically we must at least maintain market share and maximise profitability.

6.4. In order to take advantage of procurement exemptions in the short to medium term, it may be appropriate to initially operate as a Teckal company maintain percentage split of work carried out for the local authorities and that carried out for the private sector. This needs to be maintained as close to the optimum 80/20 split but must not provide more than 20% of work to the private sector.

6.5. So as to grow the business it is very important therefore to have the full support from the partner authorities so that this 80/20 split can be maintained in expanding markets generating greater total income.

6.6. The following options appraisal looked at a number of different ways to deliver the consultancy and concluded that the most viable options were to:

- Option 1: stay as we currently are (do nothing);
- Option 2: commercialising the consultancy arm of the building control partnership to enable the delivery of a profit. There are a number of ways the consultancy could be set up to deliver this and examples of these are shown in Appendix 1. Options 2a to 2d indicate how the arrangements could be developed using the setting up of a holding company, the extension of the existing partner authority arrangements or the use of an existing holding company.
- Option 3: not providing the additional services at all but reverting to statutory duties only.

7. OPTIONS APPRAISAL

7.1. The following Options Appraisal was undertaken in order to narrow down the options to the three options set out above and expanded on in the table below.

7.2. **An unincorporated association** is an organisation of two or more persons, who are the members of the association - it is not a legal entity. The membership may change from time to time. The members agree, usually in a written constitution, to co-operate in furthering a common purpose. An unincorporated association would not meet the legal requirement to trade through a company so is not a viable option.

7.3. **Public sector or employee mutual** is an organisation, which has left the public sector (also known as a "spin out") but continues to deliver public services. Specifically, mutuals are organisations in which employee control plays a significant role. Mutuals can take the legal form of a charity, sole trader, partnership or company. An employee mutual is not a viable option as the profits of that company could not be distributed to the partnership.

7.4. **A registered society** under the Co-operative and Community Benefit Societies Act 2014 (i.e. a co-operative society or a community benefit society) - The Financial Conduct Authority is the registering authority for societies. A society registered with the FCA is a legal entity, which exists independently of its members. It can act, sue and be sued and own property, land and other assets in its own name. A registered society would not meet the legal requirement to trade through a company so is not a viable option.

7.5. **A charity** is not a type of legal form or structure; it is a status conferred on a group of individuals or an organisation because of the activities it carries out - this may be relevant where the councils have received specific funding for the creation of such an organisation or in relation to a community asset transfer. A charity can take the legal form of a company, trust or unincorporated association. A charity is not a viable option as the profits of the consultancy could not be distributed to the partnership.

7.6. **A trust** - A trust allows the owner of assets (the settler) to divide the legal ownership in those assets and the beneficial ownership. The trust is created when the trust document (a trust deed) is completed; and the settlor has transferred one or more assets to the trustees or declared himself trustee of the assets. A Trust is not a viable option as there are no specific assets to be shared by the partnership.

7.7. **Corporate structures**

7.8. Local authorities have the power to set up companies in order to trade with the private sector, and can do so to raise revenue. Local authorities cannot exercise the power to trade alongside the private sector without using the vehicle of a company.

7.9. There are four types of corporate structure that can be used:

- A company limited by shares. A company limited by shares offers greater flexibility for a trading company, particularly in relation to the distribution of profit and raising capital.
- A company limited by guarantee with or without a share capital. This type of vehicle is more suited to a not-for-profit company that may also be registered as a charity, so is unlikely to be used to set up a trading company.

- An unlimited company. This type of company is unlikely to offer the level of protection a local authority would want.
- Charitable corporations (Community Interest Company (CIC) and Charitable Incorporated Organisations (CIO). This model may offer a more flexible approach, which will be suitable in some circumstances but not where the purpose is raising revenue.

7.10. Advantages of a trading company:

- Allows the local authority to raise revenue.
- The taxpayer and the public purse are afforded greater protection because of limited liability.
- If it meets the Teckal test, a local authority controlled company is treated as a department of the local authority for procurement purposes, so contracts between the local authority and it's controlled companies will not require a procurement exercise.

7.11. Disadvantages of a trading company:

- The formalities involved in setting up and running a company can be burdensome.
- Officers or members who become directors of a trading company may face conflicts of interest. Members must also be aware of implications for their Disclosable Pecuniary Interests and potential breaches of the Code of Conduct.
- Companies will be subject to taxation, including VAT and Corporation Tax.
- The local authority must be careful not to be seen to be providing unlawful state aid to the company, so the company must be capable of meeting its own costs and providing a return on the local authority's investment.

7.12. Using Existing Corporate Structures

7.13. **Medway Commercial Group (MCG**) - Medway Council is the sole shareholder of Medway Commercial Group Ltd, which has two subsidiary companies: Medway Public Services Ltd and Medway Commercial Services Ltd. MCG provide services and goods for Medway Council such as, CCTV, Assistive Technology, Out-of-Hours Calls handling Service, Consultancy and Lone Worker Solutions.

7.14. It may possible to either outsource a new or existing service to MCG without undertaking a new procurement or setting a new MCG subsidiary to undertake the service. A new subsidiary under MCG could also be a joint venture entity with partners, however, similar setup costs would be incurred as with any holding company.

7.15. If the private sector arm consultancy were delivered through a new MCG subsidiary, all the partnering authorities would hold equal shares in the proposed LATC. However, Medway Council's share would be held on its behalf by MCG and Medway's participation in the new company would be through its MCG directors. Which would affect the current Member participation.

Option Appraisal Criteria	Option 1: Remain as current service	Option 2: Local Authority Trading Company for the private sector arm	Option 3: Revert to Statutory Duties only
1. **Quality of service.** The STG brand needs to be identified as delivering quality products in a timely fashion.	• Opportunity to engage temporary staff to deal with short term contracts. • Opportunities exist to develop existing staff skills • Turn around times more difficult to predict. • Quality of end product may vary.	• Opportunity to engage dedicated staff. • Greater controls over timeframes. • Flexibility in resourcing. • Production of a better quality end product. • Certainty for future services to the partnership as these would continue to be delivered as they are now.	• No availability for delivering consultancy services. • Facilitation only via LAB Consultancy Services.
2. **Income generation.** Better control on costs and recharging trading accounts will allow for maximising income opportunities to exceed the break-even position.	• Ability to balance budget through an `at cost' service. • Inefficiencies between time cost and income generation due to lack of dedicated staff.	• Opportunity to increase income through more flexible employment status. • Opportunity to make a profit. • Greater cost controls over variable cost codes between trading accounts. • Dividend to be paid to all parties from any generated surplus.	• No direct income from consultancy services. • Minimal handling fee for dealing with LAB Consultancy Services.
3. **Commerciality.** For the future sustainability of the organisation it is essential to ensure an organisation that is efficient and commercially sensitive. Strong commercial identity, able to generate income. The arrangement needs to be demand-driven, informed by wider market rates and level of service, and based on clear client	• Close liaison with partner architects and developers. • Improved account management and potential for cross-boundary working. • Unlikely to have scale, resource or expertise to commercialise and expand the service. • Drive, determination and incentives to improve the service are unlikely to be as great as in other model options. • Under the current model there	• Would likely to have scale of resource to facilitate commercialisation and expansion of service. • Performance management across a more commercial unit will produce results. • The opportunity to invest in commercial roles eg marketing • Less restricted employment and engagement regulations. • A Teckal company would be restricted to a 20% income	• No opportunity to introduce commerciality.

Option Appraisal Criteria	Option 1: Remain as current service	Option 2: Local Authority Trading Company for the private sector arm	Option 3: Revert to Statutory Duties only
specifications and monitoring of performance against cost. It needs the ability to widen service offerings across the market and act commercially.	is likely to be limited opportunity to realise extra income as the corporate structure restricts the ability to deal with extra capacity. • Main focus for authorities is likely to be efficiencies and reducing cost over all other services.	generation from the private sector but a non Teckal company could generate 100% of its income from the private sector. • The partnering authority's liability would be limited if the LATC failed.	
4. **Competing with Approved Inspectors.** In order to be competitive we need to be able to offer similar or improved services that the competition are offering.	• Delivery of a number of complimentary services. • Use of remote and agile working and improvements in technology delivering an improved service. • Openiness and transparency required for LAs are not reflected in the private sector. • Statutory requirement for publication of charges provides advantage on competitive bidding.	• Opportunity to deliver an increase in complimentary services. • Greater controls over the quality of the product. • Opportunity to operate as an Approved Inspector. • Opportunity to work with other Local Authority Approved Inspectors as agents for the region.	• Lack of opportunity to supply complimentary services could results in work being lost to the competition.
5. **Diversification and staff development.** As part of a recruitment and retention policy we need to encourage development of existing skills sets and look at opportunities for new development and expertise.	• Strong ethos on continued professional development and individual skill sets. • Capacity issues in dealing with reactive workload impacts on opportunities for staff development. • Staff development costs in fields of expertise are expensive and difficult to fund from a balanced budget.	• Opportunity to invest in developing individual skills. • Opportunity to recover development costs through employment contracts. • Investment in development tends to retain highly motivated staff.	• Very limited capacity to invest in training for staff due to resource issues and budget constraints.

Option Appraisal Criteria	Option 1: Remain as current service	Option 2: Local Authority Trading Company for the private sector arm	Option 3: Revert to Statutory Duties only
6. **Meeting client needs.** Clients needs are far greater than statutory requirements these days. Customers requirements properly managed to ensure brand esteem figures highly in the market place.	• Provision of seminars and training events for architects and developers. • Provision of duty surveyor to give general technical advice. • Development of 24/7 access to building control information. • Limited opportunity to deliver complimentary services with the ability to facilitate some alternatives. • Difficulty in managing customer requirements due to reactive use of resources.	• Change from reactive to proactive service delivery. • Opportunity to acquire lost customers through improved service delivery. • Opportunity to delivery further services through better client management.	• Inability to meet the range of customer requirements could result in further loss of applications.
7. **Adaptability.** The service needs to be able to flex to meet changing demands and circumstances of clients. In a competitive market it is imperative that we can be reactive to change.	• Continued development on processes and procedures to meets the needs of the construction industry. • Positive approach by all staff to development and expansion of the partnership. • Capacity and resource issues can restrict opportunities to be reactive to changes in the market. • Limited opportunity to buy in expertise to meet customer needs. • There are limitations on service delivery based on a fixed staff resource.	• Opportunity to engage external expertise of staff on more flexible contracts. • Greater cost controls in engaging staff as required. • More opportunity to react to market changes and product demand.	• A minimal opportunity to adapt to any changes in circumstances. • Inability to react to changes in the market.

Justification for preferred option

7.16. Whilst continuing as we are will still deliver some additional services customer require it will not provide any scope for expansion and restricts the operational budget to a break-even position with no availability to make a profit.

7.17. Reverting to dealing with statutory duties only would be a retrograde step as it would make the income generation for the business totally reliant on building control chargeable income. The market is extremely competitive in this area with no guarantees that market share can be maintained. It would also become more difficult to match resources with demand with increased difficulty in retaining staff. Should market share or staff resource decline, the quality of service would be affected with potential further loss of work and greater pressures on maintaining a balanced budget. Balancing the resources between chargeable and non-chargeable work would also become more difficult with the risk of reducing services to partners.

7.18. The preferred option would be to develop the private sector consultancy as a LATC which would allow for expansion of services, reallocation of resources as required to retain staff, the engagement of new staff on temporary contracts where necessary to deliver short term projects. Significantly, it would also make available the delivery of a profit which could be returned to the partners by way of a dividend. Initially this would repay the setup costs of the company and then be used for any nominated purpose including compensating the cost of the partners contributions.

7.19. A wholesale transfer of the entire consultancy to a LATC is not advised as this would require the dissolution of the partnership, joint committee and the current structures we work under, with significant work to re-establish new governance structures within the context of a corporate body. A joint approach of having the current partnership working alongside a Teckal LATC will allow both parts of the consultancy (private and public) to support each other, share resource, share services and increase opportunities for profit making.

7.20. If the LATC was also a Teckal company there would be an incentive for partners to ensure local authority work is put through the consultancy where possible as this would meet the 80% threshold and increase income and profitability which would be returned as increased dividend to the partners. In order to incentivise partners there may need to be a link between the value of work put through the consultancy and the dividend paid out to that authority in order to reward partners for their support. All opportunities available to the partners to put work through the partnership need to be explored as indicated in 7.24

7.21. It would be best to start the LATC as a Teckal company and if the market for private sector consultancy increases beyond the 20% Teckal limit, the company can be internally restructured to take advantage of that and cease to be a Teckal company. This would involve amending the company's Articles of Association to make it more independent or arms length and commercially focussed. If the company were to lose its Teckal status, it would also lose the procurement exemption and the partnering authorities would then have to undertake a competitive tender for consultancy work rather then make a direct award to the company. The sharing of resources and services between the LATC and the partnership would also cease.

7.22. If the LATC were to become a successful non Teckal company, the partnering authorities would be incentivised to collect dividends in order to avoid the giving of unlawful state aid which could if unchecked, give the company an unfair advantage in the market place against competitors who were not backed or funded by local authorities. A non Teckal company would also provide opportunities for joint ventures with the private sector as third party participation would become possible.

7.23. The dividend payout from the company for profits would be to the partnering authorities who would own the company in equal shares. The partnership, providing the authorities with services, would continue to be funded as it is now. The benefits derived social value combined with benchmarking pricing will ensure that the joint venture company provides the authorities with best value services.

7.24. Further research will need to be undertaken as part of the overall business model to identify opportunities within each authority. Expertise within the partnership can currently deliver the following services:

- Decent Homes surveys
- Stock Condition surveys
- General surveying work
- Support for partners in-house services (eg, private sector housing)
- Energy assessments (eg, SAP, SBEMS, Trade-Offs)
- Display Energy Certificates for Public Buildings
- Access audits and statements
- Fire Risk assessments
- Asbestos surveys
- Flood risk assessments
- Provision of surveyors to sign off planning conditions

7.25. Each authority will recognise that the engagement of these services through the consultancy would ensure some return on their outlay to carry out a programme of works, whereas engaging outside agencies would not return any funds to the partner authority.

7.26. In examining other opportunities within the Local Authorities remit we are aware of some building control sections who visit sites to monitor planning conditions, even though the site is being administered by an AI. It is believed the cost for this is paid for from the developer so as to ensure a quality product at the end of the build which members of the planning committee are happy to sign off.

7.27. Another opportunity may exist where contract quality issues are not currently addressed. This in particular would apply to such things as: schools, libraries, contact hubs and other public buildings.

7.28. There is potential to pursue an alternative building control service in the same way that Birmingham City Council has engaged in. One issue that is often criticised about the current LABC partner authority scheme is that partner authorities cannot carry out inspections in cross-boundary situations and this can affect the relationship between the authority and the company they are partnered with. Birmingham and others have circumvented this problem by forming their own company as an Approved Inspector. This they have been able to do as a subsidiary of the LATC and it is an area we may wish to consider. This has come to light as Aldi distribution centre is being built on the Isle of Grain and Acivico (Birmingham City Council Building Control) have served an Initial Notice on us. In discussion, it has transpired that had we been an AI, as opposed to a Local Authority we could have carried out the inspections on the distribution centre on their behalf and therefore generated an income stream which could be expanded in the future.

7.29. In considering the Acivico (Birmingham City Council) model, it does offer an alternative option which we can consider in the formal Business Case, in that Medway Council has recently created its own Trading Company (Medway Commercial Group Ltd (MCG)) through which the consultancy could be a subsidiary company. This option would have to be fully investigated to ensure it protects the partnership in maintaining its own independence and governance structures, but could offer an alternative at reduced costs as much of the initial setup costs would have already been dealt with.

8. COMMERICAL CASE

8.1. In order to develop a full commercial case for the LATC a number of aspects need to be determined which will include engagement of outside consultants. This will look at:

- Legal documentation and specialist advice on other matters such as taxation
- Determining an Implementation Strategy for the new venture
- Full Risk Assessment and Management Proposals
- Governance and Charging/Re-Charging Mechanisms
- Performance Management and Accountability arrangements

8.2. Within these elements further consideration needs to be given to the following:

- Capacity/Capability of existing resources
- A quantitative as well as quantitative evaluation of operation and resources need to fulfil the operation objectives of the business, these would include; premises, transport, ICT systems, other plant and equipment and information (including market intelligence, databases and proprietary knowledge).
- What functions can be delegated
- Any third party involvement, although this will not be relevant for a Teckal company
- Relevant powers, presidents etc
- What is the governance model and how can this be made effective and efficient
- Risk identification/allocation/apportionment/mitigation – which parties could bear which risks

- How will the cost of implementation and ongoing administration be covered
- What incentivises performance – organisational and individual level
- Market assessment – market opportunity identification/quantification

8.3. The full commercial case will need to include a description of what the business will deliver and produce and to what standard. It will need to determine what skills and processes are involved. These processes will include performance and quality management, including success criteria and protective measures such as copyrights, licence rights and insurances.

8.4. A full market analysis will need to be undertaken determining who are the current and potential customers and what is the level of competition. Consideration needs to be given to marketing, how will the business promote itself and marketing strategies, how will the business develop. The results of this work would inform the company's business plan should we proceed with this option.

8.5. The process will need to be project managed with an action programme for the development of the business detailing what needs to be done to ensure the Business Plans objectives are met together with an action programme to meet the requirements of clients, reflect economy, demographic or other trends. The Commercial Case will need to describe how the business may need to develop so as to respond effectively to a changing business environment e.g., organisational structure, systems and skills. It is also important to consider addressing intangible issues such as, image and reputation.

8.6. A risk register has been produced at Appendix 2, however, a full risk assessment and sensitivity analysis needs to be undertaken as all businesses are inevitably subject to uncertainty and a degree of risk, e.g., inflation, fluctuations in demand etc. It is therefore essential to build a risk management assessment into the financial projections. Risk and uncertainty can never be fully eliminated and so any assessment should also identify the planned management responses with dealing with each of the main risk factors. Sensitivity analysis will help to determine the most robust options. By identifying the main variables and uncertainties in a project, assessing their cost implications, including any losses of income and reviewing the potential range of feasible outcomes, the sensitivity analysis should establish which options offer the flexibility to cope with change whilst still retaining the ability to deliver the required option.

8.7. Systems for monitoring progress against the plan, comparing performance against targets and success criteria are essential elements in reviewing the plan itself. There are various types of review and revision including frequent monitoring and running adjustments, reactions to unpredicted occurrences and a comprehensive annual review and revision. Systems may be described to monitor expenditure, income and other budgetary control, output returns, non-productive time, employ absence and turnover and analysis of customer complaints and customer opinion surveys. There would need to be frequent reporting to Joint Committee and consideration might be given to the appointment of independent directors with careful consideration of how to prevent conflicts for council appointed directors.

8.8. To enable the engagement of consultants to deliver a full business case and to include all of the above issues we are advised that a figure of £50,000 would be required. Whilst some financial, legal and staffing advice will be able to be purchased from the three partners much of the development of the business case will be reliant on consultants input who have expertise in this field.

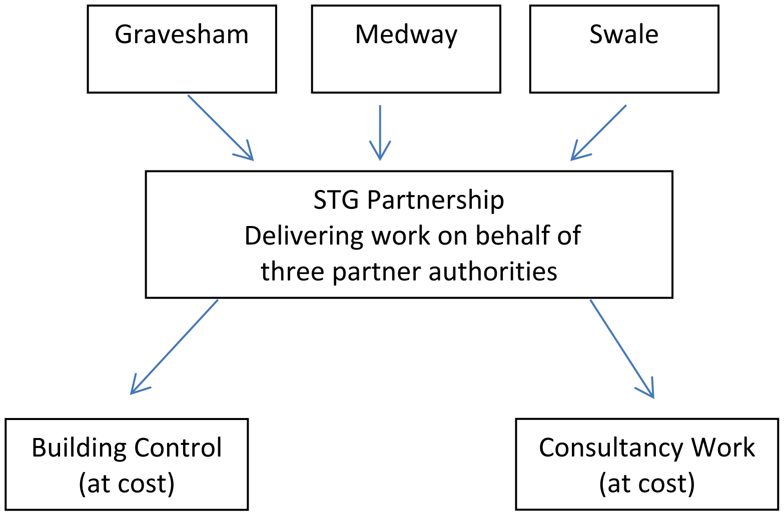
8.9. The financial case below demonstrates how the investment of these funds should be able to be repaid over a three year period with the fourth and ongoing years returning a dividend for the partners and the partnership.

9. FINANCIAL CASE

9.1. To be advised in consultation with the partnerships accountants on future opportunities and following investigation into current contracts that could be delivered through the partnership on corporate workstreams.

9.2. Market research into existing demand of services and potential diversification into other avenues.

Option: 1 - Stay as we are



- Any surplus is ring fenced for Building Control only
- Not permitted to make a profit
- No documents required to be produced

Option: 2a - Local Authority Trading Company (LATC)

Shareholders in STG Holding Co

Gravesham

Medway

Swale

STG Holding Company

needs to generate 80 % of income private from owners

Teckal Co
(public sector)

Non-Teckal

100% income from public or private third parties

- Building Control (BC)
  - any surplus is ring fenced
- Dangerous Structures
- Unauthorised Works
- Demolitions
- Other building control related work
- Consultancy work for Partner Authorities, eg
- Stock condition surveys
- Procurement Exemption

20% income from third parties; public or private

- Consultancy work for other organisations, eg,
  - Private companies
  - Other Local Authorities
  - Developers
- Can make a profit

- Teckal Co would do current partnership activities so no need for partnership
- Joint Committee could be dissolved. Would loose brand and relationships.
- Legal Documents required:
  - Shareholders Agreement
  - Service Agreement
  - Companies House Registration Forms
  - Articles of Association
  - Directors' Terms of Appointment

Option: 2b - Local Authority Trading Company (LATC) moving consultancy to a Non-Teckal when demand exceeds 20%

Shareholders in STG Holding Co

Gravesham

Medway

Swale

STG Holding Company

Procurement rules apply

(Contracting Co.)

Initially set up Teckal Co

Teckal Co
(public sector)

80% income generate from owners

20% third parties – public or private

- Building Control (BC)
  - no profit can be made
- Dangerous Structures
- Unauthorised Works
- Demolitions
- Other building control related work
- Consultancy work for Partner Authorities, eg
  - Stock condition surveys
- Consultancy work for other organisations
- Procurement Exemption

Move to Non -Teckal when Consultancy work for other organisations exceeds 20%

Non-Teckal
(private sector)

- Consultancy work for other organisations, eg,
  - Private companies
  - Other Local Authorities
  - Developers
- Can make a profit
- 100% from public or private Third parties

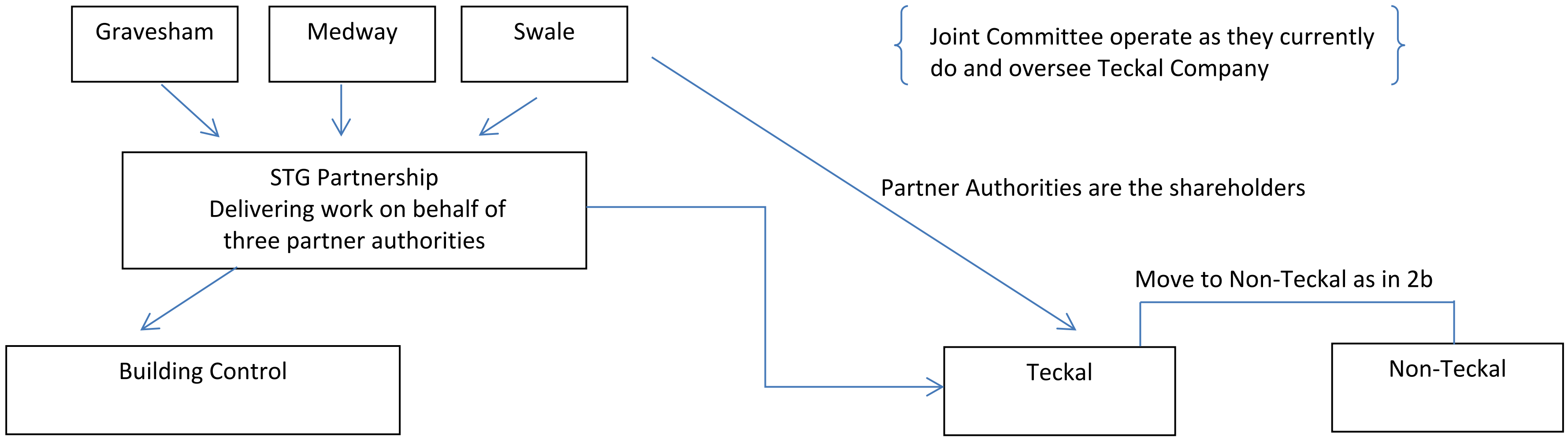
- Teckal Co would do current partnership activities so no need for partnership

- Joint Committee could be dissolved. Would loose brand and relationships.

- Legal Documents required:
  - Shareholders Agreement
  - Service Agreement
  - Companies House Registration Forms
  - Articles of Association

- Directors' Terms of Appointment

Option: 2c - Maintain Partner Authority Arrangements but deliver consultancy through Teckal initially

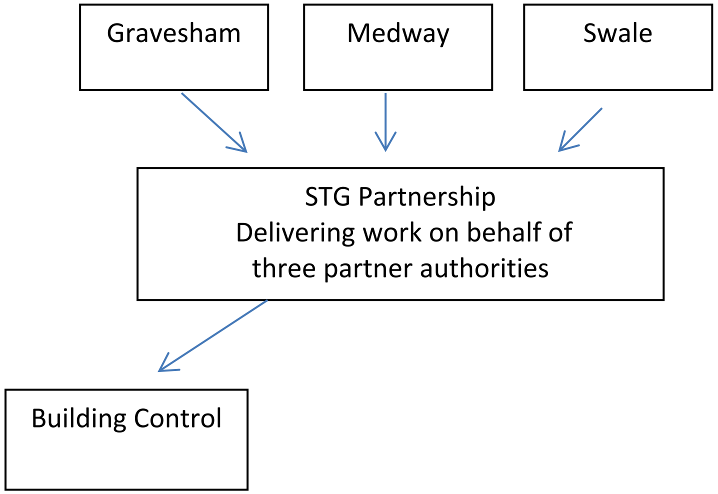


- Building Control (BC)
- Dangerous Structures
- Unauthorised Works
- Demolitions
- Other building control related work
- Any surplus is ring fenced for building control

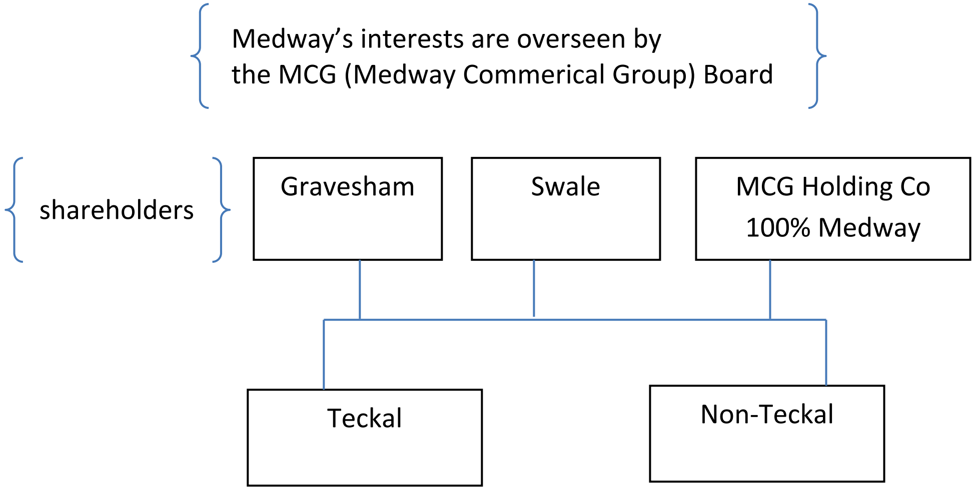
- Consultancy work for other organisations, eg,
  - Private companies
  - Other Local Authorities
  - Developers
- Can make a profit
- 80% income from owners, 20% income from third parties public or private
- Procurement exemption

- Consultancy work for other organisations, eg,
  - Private companies
  - Other Local Authorities
  - Developers
- Can make a profit
- 100% from public or private third parties

Option: 2d - Maintain Partner Authority Arrangements for building control only. Consultancy delivered through separate shareholder arrangement with an existing holding company



- Building Control (BC)
- Dangerous Structures
- Unauthorised Works
- Demolitions
- Other building control related work
- Any surplus is ring fenced for building control



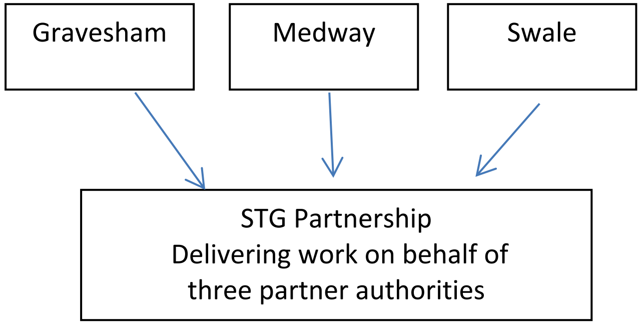
Teckal

- Consultancy work for other organisations, eg,
  - Private companies
  - Other Local Authorities
  - Developers
- Can make a profit
- 80% income from owners, 20% income from third parties public or private
- Procurement exemption

Non-Teckal

- Consultancy work for other organisations, eg,
  - Private companies
  - Other Local Authorities
  - Developers
- Can make a profit
- 100% from public or private third parties
- Move to Non-Teckal as in chart 2b

Option: 3 - Revert back to only Building Control duties



- Building Control (BC)
  - any surplus is ring fenced
- Dangerous Structures
- Unauthorised Works
- Demolitions
- Other building control related work
- No profit can be made

Appendix 2

RISK REGISTER

Purpose:

Risks are associated with any problems or events that may occur in the future and which will adversely affect any of the project aims, in terms of their impact on performance, cost, schedule and quality. Since it is in the future a risk inevitably has a measure of uncertainty associated with it and by definition a degree of loss. A risk has a third element, the choice to do something about it. Once identified, Risk Management offers the partnership the opportunity to implement appropriate mitigating strategies that prevent or reduce the probability of occurrence of the risk and the reduction of its impact.

The Risk Register will record the risks, mitigating actions and risk owner details in relation to the partnerships consultancy services.

Definitions:

Issue/Function - Key areas within the project
Identified Risk – Description of the risk(s) relating to the key risk areas

Risk Areas			
A. Commercial	B. Legal	C. Political	D. Finance
E. Staff/Resources/Change Management	F. Systems	G. Implementation	

Impact, Probability, Level of Risk

Impact		**Probability**		**Level of Risk**	
4	Critical - Stops project	3	High	1 – 3	Low
3	Severe	2	Medium	4 – 7	Medium
2	Moderate	1	Low	8 – 12	High
1	Low				

Risk Score = Impact x Probability

A. Commerical

Issue	Risk	Impact	Probability	Level of Risk	Classification	Mitigation	Ownership
Competitive Products	Inability to identify market trends	3	1	3	Low	Thorough investigation of market trends through market research company and understanding of customer requirements through discussion and feedback.	Director and Consultancy Manager
Quality of Service	Poor reputation causing loss of work and impacting growth	3	2	6	Medium	Ensure all staff engaged in consultancy are aware of the competitive concept and commerciality of running a business. Staff only engaged and retained if able to demonstrate acceptance of these principles.	Director and Consultancy Manager

B. Legal

Issue	Risk	Impact	Probability	Level of Risk	Classification	Mitigation	Ownership
Legislative Constraints	Contravene legal requirements through poor knowledge and advice	3	1	3	Low	Engagement of legal expertise to ensure compliance in all areas of legislation.	Director
Insurance Cover	Inadequate insurance cover to mitigate any claims	3	1	3	Low	Engagement of insurance expertise to ensure appropriate cover is given to all products and services included in the consultancy	Consultancy Manager

Issue	Risk	Impact	Probability	Level of Risk	Classification	Mitigation	Ownership
Corporation law	Unfamiliarity with corporate structure, laws and processes leading to decisions taken by LATC not being legally effective	3	1	3	Low	Engagement of legal expertise and/or company directors with knowledge of and experience of running companies with training of officers/councillors	Director

C. Political

Issue	Risk	Impact	Probability	Level of Risk	Classification	Mitigation	Ownership
Full partner support	Inadequate participation by all members of the partnership to provide avenues of work to generate income	2	2	4	Medium	Each partner needs to identify work which can be put through the consultancy to ensure reciprocal dividend is paid.	Steering Group
Inadequate political support from three partner authorities to fund development of LATC	Budgetary constraints one or more of the partners declined the invest to save funding required to set up the consultancy as a LATC	3	3	9	High	Partner authorities and the partnership will do everything in their power to ensure recovery of set up costs are repaid.	Joint Committee & Steering Group

D. Financial

Issue	Risk	Impact	Probability	Level of Risk	Classification	Mitigation	Ownership
Inadequate funding for initial set up costs	Budgetary restrictions the full funding estimate could not be met and therefore only partial funding available	2	2	4	Medium	Should only partial funding be available much of the research and development of the project would have to be done in-house which	Joint Committee & Steering Group

Issue	Risk	Impact	Probability	Level of Risk	Classification	Mitigation	Ownership
						would impact on day-to-day delivery and length the project timescale.	
Unrealistic payback time	In order to secure funding for the setup of the LATC an unrealistic payback period may be enforced. This may make the acceptance of the funding impractical as no guarantees can be given on profitability.	3	1	3	Low	Full and open negotiations to be taken at the outset to ensure if funding is granted it has a realistic payback period.	Steering Group, Director & Consultancy Manager

E. Staff Resource & Change Management

Issue	Risk	Impact	Probability	Level of Risk	Classification	Mitigation	Ownership
Lack of dedicated staff	Small numbers of skilled practitioners mean that the service can be vulnerable to absenteeism through leave, sickness etc	2	3	6	Medium	As a LATC terms of contract of employment can be more specific with greater freedom to choose alternative service delivery models if in-house provision is compromised.	Consultancy Manager
High cost of training	Should expertise leave the LATC training of dedicated staff is very expensive.	2	2	4	Medium	Ensure sufficient funding available through budget setting for expensive training courses to be paid for.	Consultancy Manager
Impact of shared resources	By sharing resources between different functions and different services a peak in demand in either or both areas can have an adverse effect on the quality of product and	3	2	6	Medium	Dedicating certain days to certain functions with the opportunity to negotiate for additional days on either service during times of peak demand. As the LATC develops more dedicated staff will be included in the	Consultancy Manager

Issue	Risk	Impact	Probability	Level of Risk	Classification	Mitigation	Ownership
	delivery of service in each area.					structure.	

F. Systems

Issue	Risk	Impact	Probability	Level of Risk	Classification	Mitigation	Ownership
Numerous client based systems in operation	As each client operates their own in-house system or requires a specific external system to be used there are a number of risks associated to us as contractor including: training costs, licence costs, support costs, hardware costs and potential lack of IT support.	2	1	3	Low	Engagement of multi-skilled flexible staff who are able to use a number of different systems.	Consultancy Manager

G. Implementation

Issue	Risk	Impact	Probability	Level of Risk	Classification	Mitigation	Ownership
Reliance on sub-groups delivering their individuals parts of the project on time	Because the project will be reliant on a number of different “leads” for various functions such as, legal, finance, HR,	3	2	6	Medium	Dedicated project management with external consultants as necessary. Chief Executive authority necessary to drive each sub-	Steering Group & Chief Executives

Issue	Risk	Impact	Probability	Level of Risk	Classification	Mitigation	Ownership
	IT, management there is a high risk that certain areas may not be delivered on time.					group to deliver.	